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TECHNICAL ASSISTANCE REPORT—IPSAS IN ICELAND—TOWARDS ENHANCED FISCAL TRANSPARENCY

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IPSAS IN ICELAND: TOWARDS ENHANCED FISCAL TRANSPARENCY

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Abbreviations and Acronyms

CBI	Central Bank of Iceland
FAD	Fiscal Affairs Department
FRA	Financial Reporting Act 1997
GFSM	Government Finance Statistics Manual
GoI	Government of Iceland
INAO	Icelandic National Audit Office
IFRS	International Financial Reporting Standards
IPSAS	International Public Sector Accounting Standards
ISA	International Standards on Auditing
ISSAI	International Standards of Supreme Audit Institutions
MoF	Ministry of Finance
OBL	Organic Budget Law
PPP	Public-Private Partnership
StatIce	Statistics Iceland
TA	Technical Assistance

PREFACE

In response to a request from the authorities, a technical assistance (TA) mission from the Fiscal Affairs Department (FAD) of the IMF visited Reykjavik during the period November 5–18, 2013 to advise the government on the reform of its accounting and reporting policies and practices in accordance with international public sector accounting standards (IPSAS). The mission was led by Abdul Khan, and included Johann Seiwald (both FAD), and Frans van Schaik (PFM expert).

The mission builds upon the findings and recommendations of previous FAD TA missions to Iceland. The mission discussed its main findings with Mr. Bjarni Benediktsson, Minister of Finance; Mr. Guðmundur Árnason, General Secretary; Mr. Thórhallur Arason, Deputy Secretary of the Ministry of Finance (MoF); Mr. Gunnar Hall, Director General, Government Financial Management Agency (Fjársýsla); and other senior officials. This mission was organized mainly around a series of discussions with an IPSAS Working Group to discuss existing policies and practices, and compare them to IPSAS to identify and address any gaps. The working group was led by Mr. H. Hall and included Mr. Stefán Kjærnested, Mr. Pétur Jónsson, and Ms. Helga Viðarsdóttir from Fjársýsla, Mr. Jóhann Rúnar Björgvinsson, Mr. Ingþór Karl Eiríksson from Ministry of Finance (MoF); and Mr. Albert Ólafsson from Icelandic National Audit Office (INAO).

The mission also met with Mr. Nökkvi Bragason, Director General, MoF and discussed the implications of the plan to move to IPSAS. At the INAO, the mission met Mr. Sveinn Arason, Auditor General; Mr. Ingi K. Magnússon, Head of Financial Audit Department; and Mr. Jón Loftur Björnsson, Head of Review of the Execution of the Budget, and discussed audit implications of the plan to move to IPSAS. Discussions were held with officials from the Central Bank of Iceland, Statistics Iceland (StateIce), Icelandic Road and Coastal Administration, Real Estate Agency, Landsvirkjun, Icelandic State Electricity, Student Loan Fund, and the Association of Local Authorities in Iceland. The mission also met the Budget Committee of the Althingi.

The mission would like to thank all of the above for the frank and open exchanges of views on all matters discussed. The mission would also like thank the authorities for the generous hospitality and courtesy extended to the mission.

Executive summary

The government of Iceland has decided to reform its legal framework for budgeting by introducing a new organic budget law (OBL). This is part of a series of reforms introduced by the government following the economic crisis of 2008. Among other improvements, the proposed OBL requires that fiscal reports should follow internationally accepted standards. This would imply that financial statements would be prepared in accordance with International Public Sector Accounting Standards (IPSAS) and statistical reports would be prepared in accordance with Government Finance Statistics Manual of 2001 (*GFSM 2001*). This mission worked closely with officials, particularly a working group set up for this purpose, to undertake a gap analysis with a view to identifying the major reforms that would be required to implement IPSAS. The mission also discussed the issue of maintaining alignment with budgets and budgetary reports that are expected to focus on *GFSM 2001* indicators.

Consolidated "whole-of-government" financial statements of the central government will facilitate fiscal policy informed by a broader view of public finances. IPSAS requires the central government to prepare accounts that consolidate the accounts of the central government and all entities that it owns or otherwise controls. This will help to provide a more complete view of all resources controlled by the government, and the liabilities, contingent liabilities, and other fiscal risks to which it may be exposed. Most of the entities controlled by the government produce financial statements in time and the larger ones follow International Financial Reporting Standards (IFRS) or similar standards. This will reduce some of the challenges normally associated with the preparation of consolidated financial statements.

Recognition and systematic accounting of physical assets will enhance transparency and facilitate management and budgetary decisions. Under the current framework such assets—including roads, bridges, tunnels, land, and buildings—are treated as expenses and written off in the year in which they are acquired. Under IPSAS these items will be recognised as assets and the balance sheet will provide a more complete view of the government's financial position. Preliminary discussions indicate that such assets are likely to constitute a material amount—probably in excess of 60 percent of GDP that could nearly double the gross assets shown on 2011 financial statements. Fortunately, registers of these assets exist that provide a full listing of the material assets and, in some cases, also show their values. This information base is more advanced than in many other countries and is expected to provide a solid foundation for constructing a list of assets and their valuation for incorporation in the IPSAS-based accounts.

Some changes in valuation of financial assets and liabilities may also be required. For example, revisions to the recognition and measurement of pension and debt liabilities are required. Other material financial instruments should be reviewed in detail and the accounting and disclosures (including on credit, interest rate, and other risks) required under IPSAS should be introduced.

The cash flow statement should provide information about key revenues and expenditures. The current cash flow statement is prepared using the indirect method that does not show specific operating revenues and expenses such as tax revenues, employee emoluments, and transfer payments. The direct method provides a more useful cash flow statement by providing this important information. The Iceland government cash flow statement using the direct method was discussed during the mission and is illustrated in Appendix IV.

The alignment between the budget and the financial statements must be maintained. One of the strengths of the existing legal framework is this alignment and the proposed OBL also stresses the importance of this feature. First, budget documents should include a full set of projected or estimated financial statements for each of the budget and forward years that are fully comparable to the ex post financial statements. Second, although the budget would focus on GFSM 2001 indicators such as net lending/borrowing and IPSAS statements usually focus on surplus or deficit—also referred to as operating result—a common harmonized presentation of the operating statement should be adopted for both budgets and accounts.

The budget should recognize depreciation as an expense but need not appropriate for depreciation at this stage. The budgeted operating statement should include depreciation as an expense to determine the operating result. Although depreciation could also be appropriated, it is suggested that in order to avoid complexities, this should be deferred. Instead, appropriation should continue to be for accrual-based expenses (excluding depreciation) and capital expenditure. This issue should be revisited after the implementation of IPSAS for ex post reporting has been completed and some expertise has been developed in dealing with depreciation, particularly estimating depreciation for budget and future years.

A phased implementation approach should be adopted. The implementation strategy recognizes that the government's existing accounting and fiscal reporting framework is based on accrual and other concepts that are in many respects consistent with international standards. The implementation strategy focuses on the key areas where the existing accounting policies and practices would need to be changed to be consistent with international standards.

The phased approach involves the preparation of opening balance sheets as at January 1, 2014 that would constitute the starting point of the transition to IPSAS. Trial financial statements would be prepared for 2014 and 2015 in parallel with existing reports. The opening balance sheet and the trial financial statements should be reviewed by the INAO who should provide detailed comments and suggestions for addressing any issues that may be identified. Assuming that the proposed OBL is enacted in 2014, the budget of 2016 would be the first to follow IPSAS requirements, notably the inclusion of depreciation as expenses. This will also allow the replacement of the existing financial statements with the IPSAS-based statements from 2016, which will be used to, among other things, compare budgets with actuals.

System implications of the proposed changes should be identified and addressed. The existing Oracle system has the functionality to address the recording and reporting of nonfinancial assets and other systems have records of the more significant assets such as roads, bridges, tunnels, land, and buildings. The consolidated financial statements would initially be produced using simple Excel-based systems, but the need for a more sophisticated system solution should be reviewed based on the experience during the initial phases. Options may include further development of the existing system or the acquisition of a system that is specifically designed to support consolidated reporting. The budget system may also need to change.

It will also be important to identify and address training and communication needs. As far as training needs are concerned, given the long tradition of officials working with accrual-based accounts, it is not expected that these would be extensive. Nevertheless, a targeted training plan should be adopted to ensure that relevant staff has the necessary level of proficiency in the new accounting and reporting framework. In addition to training, a communication strategy should be developed to ensure that all stakeholders, including the ministers and senior officials at the ministries and the members of Althingi, are provided with relevant information and explanations with a view to facilitating a proper appreciation and effective use of the new information.

Table 1 provides a summary of the key recommendations with indicative implementation timelines.

Table 1. Summary of Key Recommendations and Indicative Implementation Timelines

Key Recommendations	Phase I 2014 Jan - Jun	Phase II 2014 Jul - Dec	Phase II/III 2015	Phase IV 2016	Phase V 2017
Prepare detailed implementation plan including communication and training strategy (Fjársýsla, MoF)					
Prepare opening balance sheet as at January 1, 2014 incorporating values for all assets and liabilities and (Fjársýsla)					
Establish mechanisms to eliminate intra-government (including class A-C) transactions and balances (Fjársýsla)					
Revise financial statements including notes in accordance with IPSAS (Fjársýsla)					
Prepare consolidated financial statements (Fjársýsla)					
Trial financial statements (2014 and 2015)					
Official financial statements, including comparison with budget (2016)					
Include both original and final budget in financial statements and explain the differences (Fjársýsla, MoF)					
Review and report on opening balance sheet and trial financial statements (INAO)					
Audit and report on financial statements in accordance with ISSAI (INAO)					
Adopt harmonized presentation of budget and financial statements displaying net lending/borrowing and operating result (Fjársýsla, MoF)					
Include estimates of depreciation in budget as part of operating expenses but not appropriations (MoF)					
Prepare first budget (2016) aligned with IPSAS financial statements (MoF)					

Legend: Shaded bars indicate timing of implementation of proposed reforms including refinement.

I. Introduction and Background

1. **Following the 2008 economic crisis the government of Iceland has undertaken a series of reforms to improve fiscal management.** The Fiscal Affairs Department (FAD) of the IMF has worked closely with the authorities to help design and implement the reforms in the areas of budgeting, cash and debt management, fiscal risks, municipal finance, and the revision of the legal framework for public financial management.

2. **A new organic budget law (OBL) is expected to be enacted to reform the legal framework for budgeting.** The proposed OBL is designed to improve fiscal discipline, codify existing good practices, support sustainable fiscal policy, and put Iceland at the forefront of international budget practice.[1] In particular, the proposed OBL requires improvement of the fiscal reporting framework consistent with internationally accepted standards.

3. **Iceland's current reporting framework is relatively advanced.** The framework, based primarily on the Financial Reporting Act (FRA) of 1997, requires the reporting of an operating statement, a balance sheet, and a cash flow statement—three primary statements that are also required by internationally accepted standards. Another strength of the existing system is the close alignment of budgets and financial statements. Iceland was one of the first countries to introduce accrual concepts in budgeting, and is still one of the few countries in the world to have what may be referred to as an accrual budgeting framework—with some modifications.

4. **The implementation of international standards will provide a more informed basis for fiscal policy and further improve transparency.** Despite its strengths, the current framework should be updated. When the FRA was introduced in 1997, international reporting standards, particularly for the public sector, were not advanced—statistical standards were based on cash accounting and accounting standards did not exist. However since 1997, much progress has been made, with the Government Finance Statistics Manual (GFSM) of 2001 introducing accrual basis for statistical reports, and the issuance of International Public Sector Accounting Standards (IPSAS) on a wide range of issues. The European Commission is also considering developing public sector accounting standards using IPSAS as a reference. Implementation of IPSAS in Iceland would lead to a number of improvements, including in the coverage of fiscal reports by including companies and other enterprises controlled by the government, and the comprehensiveness of the balance sheet by recognizing nonfinancial assets. These improvements would put Iceland at the forefront of public sector fiscal reporting practice.

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[1] See *Iceland: Toward a New Organic Budget Law*, by Richard Hughes, Tim Irwin, Iva Petrova, and Edda Ros Karlsdottir, January 2012.

5. **This mission undertook a review of the existing accounting policies and practices and identified the main differences with IPSAS.** The mission worked closely with the working group set up by the Government Financial Management Agency (Fjársýsla).[2] The focus of the gap analysis was on major issues where there are material departures from international standards, while other issues were covered to the extent practicable. The mission also discussed the issues associated with the implementation of IPSAS based national standards and developed an implementation strategy supported by a detailed plan.

6. **The mission's findings and recommendations are set out in this report.** These were discussed extensively with the members of the working group and their input has been invaluable in developing the final recommendations. Chapter II of this report sets out an analysis of the existing reporting policies and their differences with IPSAS, Chapter III proposes some general improvements to the financial statements, Chapter IV discusses alignment of the budget and the financial reports and harmonization of accounting and statistical reports, Chapter V discusses some issues related to audit, and Chapter VI describes a strategy for implementation, which is supported by a detailed implementation plan.

II. Gap Analysis between GoI Accounting Policies and Practices and IPSAS

7. **This section discusses the main differences between the Government of Iceland's (GoI) current accounting policies and practices and the accrual basis IPSAS suite of standards.** This gap analysis is based on a review of an English translation of the 2011 audited financial statements of the government and focuses on identifying where GoI policies and practices deviate from the requirements of IPSAS and recommends measures to address these issues.

A. Consolidated Financial Statements

8. **The financial statements issued by the GoI do not present information on all government-controlled entities on a consolidated basis.** This is because the consolidation is confined to the budget sector. Key figures from selected entities' operating statements, balance sheets, and cash flow statements are disclosed but not consolidated. IPSAS 6 *Consolidated and Separate Financial Statements*, however, requires the presentation of consolidated financial statements of all entities controlled by the government. IPSAS 7 *Investments in Associates* and 8 *Interests in Joint Ventures* deal with related topics of reporting for investments in associated and joint ventures. Box 1 summarizes the rationale for the preparation of consolidated financial statements.

[2] See preface for a description of the composition of the Working Group.

Box 1. Rationale for the Preparation of Consolidated Financial Statements

Although the central government, its state-owned enterprises (such as government commercial companies, commercial statutory authorities, and majority owned companies), and other related authorities prepare their own financial statements, individually those statements provide only a partial view of the overall activities of the government. Consolidated financial statements are needed to obtain a complete view of the government's overall activity, whether for decision making purposes or for demonstrating accountability for the resources provided by, and managed on behalf of, the resource providers such as taxpayers. Even when budgets are prepared for just the central government, it is important that fiscal policy is set and budgetary decisions made on the basis of information about the finances of the government or the public sector as a whole, not just the budget sector.

Consolidated financial statements provide an accounting of the full nature and extent of the financial affairs and resources of the government, including those of its controlled entities. Such statements are a key element of financial reporting by governments because they serve to report on how it managed its affairs and resources at a consolidated level. Consolidated financial statements recognize that even though the government and its controlled entities may be separate legal or organizational entities, together they make up a single economic entity. Providing consolidated information helps users gain an overall understanding of the government's assets and liabilities, revenues and expenses, and cash flows, and also helps to inform planning and decision making.

The reporting boundary - why is it important to identify controlled entities?

The issue of what should be included when a government prepares its consolidated financial statements is critical because choosing to include or exclude certain entities can have a significant impact on the financial statements and the view they provide about public finances. Having clear boundaries for including or excluding entities helps users understand and assess the magnitude of the financial affairs and resources entrusted to the government. It also facilitates a full appreciation by the leadership of the government of the extent of the financial affairs and resources for which they are responsible.

9. **The GoI's 2011 financial statements include lists of "state entities" which are entities that "hold state authority and those institutions and enterprises which are owned 50 percent or more by the state," and a separate list of entities where GoI has a minority shareholding.** The Fjársýsla manages to collect the financial statements of virtually all of these entities by the end of April, which is within four months after reporting date. Some minor entities submit their financial statements in May, and only one entity had not yet submitted its financial statements for the year 2012 by November 2013. The GoI should undertake an analysis of entities to identify those that are controlled by the government and those that are more in the nature of associates or joint ventures as defined by IPSAS. The new OBL divides these entities into classes A (central government part of the general government sector), B (mainly public nonfinancial corporations), and C (mainly public financial corporations).[3]

[3] References to class A, B, and C entities throughout this report are in accordance with the new Organic Budget Law (OBL). Class B includes the entities formerly (i.e., prior to the new OBL) referred to as class B and C, and class C includes entities formerly referred to as class D and E.

10. **IPSAS 6 determines the boundaries of consolidation on the basis of control for financial reporting purposes.** Under this approach the controlling entity includes in its financial statements all those entities which it controls. Whether an entity controls another entity for financial reporting purposes is a matter of judgment based on the definition of control in IPSAS 6 and the particular circumstances of each specific situation (Box 2). This means that consideration must be given to the specific nature and substance of the relationship between the identified entities. The definition implies strategic control and it is at the level of being able to decide the strategy of another organization that is essential for control rather than having control over the routine daily processes through which a strategy is implemented.

Box 2. Definition and Examples of Control [1/]

IPSAS 6 defines control within a public sector context and provides guidance on determining whether control exists. It defines control as "the power to govern the financial and operating policies of another entity so as to benefit from its activities." Both the power aspect and benefit aspect are required to be present for control to exist.

For example, if an entity has the power to appoint or remove a majority of the members of the governing body of another entity and the power to dissolve the other entity and obtain a significant level of residual economic benefits, it would control the other entity in accordance with IPSAS 6.

1/ IPSASB Study 14, Transition to the Accrual Basis of Accounting: Guidance for Public Sector Entities, (January 2011).

11. **Controlled entities apply accounting policies that appear to be broadly consistent with IPSAS.** In Iceland, most government-owned business enterprises apply accrual accounting principles complying with either International Financial Reporting Standards (IFRS) or national accounting standards in accordance with the European Directives. IPSAS are based on IFRS and only deviate from IFRS for public-sector specific reasons. The similarity between IFRS and IPSAS would facilitate the preparation of consolidated financial statements for GoI without the need for significant adjustments to the amounts reported in the financial statements of the entities.

12. **The preparation of consolidated financial statements requires the elimination of all inter-entity transactions and balances.** IPSAS requires that when accounts are prepared at the consolidated central government level, the transactions and balances between the government entities are eliminated. Balances, transactions, revenues, and expenses between entities within the economic entity are required to be eliminated in full. Mechanisms will need to be established to identify, reconcile, and eliminate common transactions.

13. **IPSAS contains transitional provisions relating to elimination.** Entities are not required to eliminate balances and transactions between entities within the economic entity for a period of three years from first-time adoption of IPSAS. The IPSASB has

acknowledged that controlling entities adopting IPSAS for the first time may have difficulties in identifying transactions and balances that need to be eliminated when preparing the consolidated financial statements. For this reason, IPSASB provides this temporary relief from the requirement to fully eliminate balances and transactions between entities within the economic entity.

B. Investments in Controlled Entities and Associates

14. **In its separate financial statements, the GoI should continue accounting for its controlled entities and associates (class B and C) at cost (Note 1.2 Accounting Principles 3 and in Note 38).** In accordance with IPSAS, in the GoI's separate financial statements investments in controlled entities, associates and jointly controlled entities may be accounted for in either one of three ways:

a) Using the equity method as described in IPSAS 7 *Investments in Associates*;
b) At cost; or
c) As a financial instrument in accordance with IPSAS 29 *Financial Instruments: Recognition and Measurement*.

The mission recommends applying the cost method in GoI separate financial statements, since, among other things, this will ensure that no gains and losses appear in the operating statement. This will, in turn, help maintain the alignment of actual and budget figures in the operating statement.

15. **In its consolidated financial statements the GoI should account for associates using the equity method.** Currently, the GoI accounts for its associates at historic cost which is not in compliance with IPSAS. An associate is an entity over which an investor has significant influence, being the power to participate in the financial and operating policy decisions of the investee (but not control or joint control), and investments in associates are, with limited exceptions, required to be accounted for using the equity method. The equity method is a method of accounting whereby the investment is initially recognized at cost, and adjusted thereafter for the post-acquisition change in the investor's share of net assets/equity of the investee. The surplus or deficit of the investor includes the investor's share of the surplus or deficit of the investee (IPSAS 7, paragraph 7).

C. Property, Plant, and Equipment

16. **Property, plant, and equipment play a vital role in service delivery.** They represent a significant investment and therefore warrant being properly recorded, maintained, and safeguarded to ensure continued effective, efficient, and economical service delivery. Providing comprehensive and consistent reporting on the value of an entity's assets is essential for effective asset management. Moreover, up-to-date and relevant information on assets will enable the government to exercise sound asset management, including:

- Assessing if assets controlled by an agency are adequately maintained and able to support the agency's current and future activities;
- Planning for the future replacement or upgrading of assets;
- Identifying assets that are obsolete, surplus to requirements, underutilized or uneconomic to maintain, and plan for their disposal;
- More effectively managing the risks associated with control of assets; and
- More accurately determining the costs of delivering a service (i.e., using accrual accounting principles).

Failure to adequately manage assets increases the risks of misuse, pilferage, loss, sub-optimal utilization, and incurrence of excessive maintenance and replacement costs.

17. **The GoI's class A entities do not recognize property, plant, and equipment on their balance sheets.** This accounting policy is inconsistent with IPSAS 17 *Property, Plant, and Equipment* which requires recognition on the balance sheet. IPSAS 17 allows a choice of accounting model between cost and revaluation model. IPSAS requires a consistent choice for an entire class of property, plant and equipment but allows different choices for different classes. The cost model may, for example, be applied to IT equipment, while the revaluation model is applied to road infrastructure. The GoI should analyze by class of property, plant, and equipment which model is most suitable. Under the cost model the asset is carried at cost less accumulated depreciation and impairment losses. Under the revaluation model the asset is carried at revalued amount, which is fair value at revaluation date less subsequent depreciation and impairment losses. Revaluations should be carried out regularly. Revaluation increases are credited directly to a revaluation account in equity. However, the increase should be recognized as revenue in surplus or deficit to the extent that it reverses a revaluation decrease of the same class of assets previously recognized as an expense in surplus or deficit in the operating statement. Revaluation decreases are debited first against the revaluation surplus related to the same class of assets, and any excess against surplus or deficit.

18. **The GoI should apply the component approach to property, plant, and equipment.** This means that each part of an item of property, plant, and equipment with a cost that is significant in relation to the total cost of the item should be depreciated separately. Depreciation is charged systematically over the asset's useful life. The depreciation method must reflect the pattern in which the asset's economic benefits or service potential is expected to be consumed by the entity, e.g., the straight-line method, the diminishing balance method, and the units of production method.

19. **The GoI should complete the extensive asset registers it already maintains for a large number of assets.** One example is the Iceland Road and Coastal Authority that maintains a register of most of central government's transport infrastructure assets. The register does not show values, but the Authority estimates that the replacement cost of its infrastructure assets could exceed ISK 1,000 billion (ISK 1 trillion, 61.4 percent of GDP).

The authority holds 13,000 km of roads, bridges, and tunnels. Another example is the Registers Iceland Agency that keeps a register of central government's land, and building showing both market values and depreciated replacement cost, the latter totaling approximately ISK 120 billion (7.4 percent of GDP). The key challenge for the GoI is to complete the identification of all material existing assets, record them systematically, and value them. The INAO should subsequently review the existence and completeness of the assets and their valuation.

20. **The GoI is considering recognition of the property, plant, and equipment of all entities within class A on the balance sheet of a new agency under the MoF.** The agency will be responsible for the maintenance of the assets and would rent out the assets to other class A entities. The entity would thus serve as a lessor, while all other class A entities would serve as lessees. Although this arrangement would require negotiations about lease contracts and rental payments, the expectation is that this arrangement would simplify the process of asset recognition and accounting required under IPSAS by centralizing the accounting of assets and avoiding the need for the class A entities (lessees) to undertake this function. As these individual entities are not required to prepare IPSAS-based financial statements, they would simply report the rent expense. However, if an entity prepares IPSAS-based financial statements, it may have to report the asset on its balance sheet and a corresponding liability if the lease arrangement transfers to the lessee substantially all the risks and rewards incidental to ownership of the asset (finance lease). The financial statements of the central government as a whole would not be affected by these leasing transactions and balances as they would be eliminated on consolidation of class A entities.

21. **IPSAS contains transitional provisions allowing the government to not recognize property, plant, and equipment for reporting periods beginning on a date within five years following the date of first-time adoption of IPSAS.** However, it should be noted that by not recognizing all assets at transition date and gradually adding classes of assets during an extended period of time, the integrity and transparency of the financial statements will only improve over the years. The mission therefore does not recommend applying this transitional provision.

D. Intangible Assets

22. **The GoI does not present intangible assets in its financial statements.** IPSAS 31 *Intangible Assets*, however, requires recognition of intangible assets, defined as identifiable non-monetary assets without physical substance. The GoI's intangible assets mainly consist of computer software licenses such as Oracle E-Business Suite and internally developed software. IPSAS 31 does not apply to rights sold by the government to third parties, e.g. fishing rights and rights to use the radio spectrum (3G).

23. **IPSAS contains transitional provisions allowing a government that has not previously recognized intangible assets to apply IPSAS 31 *Intangible Assets***

prospectively. In such circumstances, no intangible assets would be recognized on the opening statement of financial position. The intangible assets item on the statement of financial position would only be populated gradually in future years to the extent new intangible assets are acquired. This option limits transparency and understandability of the government's financial statements because some, but not all, intangible assets held by the government will be recognized on its balance sheet. Complete transparency of all intangible assets held by the government will only be achieved when the government has disposed of all intangible assets currently held. The mission therefore does not recommend applying this transitional provision.

E. Leases

24. **The GoI does not report on finance leases in accordance with IPSAS.** IPSAS 13 *Leases* establishes requirements for financial reporting of leases and sale and leaseback transactions by public sector entities, whether as lessee or lessor. Amongst others, in case of finance lease, IPSAS 13 requires lessees to recognize an asset and a liability. A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. The GoI should therefore amend its accounting policies of finance leases in order to comply with IPSAS 13.

F. Inventories

25. **The GoI measures inventories at cost, taking into account impairment**. IPSAS 11 *Inventories* requires inventories to be measured at the lower of cost and net realizable value. Where inventories are acquired through a non-exchange transaction (e.g., a donation), their cost should be measured at their fair value as at the date of acquisition. Fair value reflects the amount for which the same inventory could be exchanged between knowledgeable and willing buyers and sellers in the marketplace. Inventories are required to be measured at the lower of cost and current replacement cost (the cost the government would incur to acquire the asset on the reporting date) where they are held for:

- Distribution at no charge or for a nominal charge;
- Consumption in the production process of goods to be distributed at no charge or for a nominal charge.

The GoI should therefore amend its accounting policies for inventories to align them with IPSAS 11.

G. Employee Benefits

26. **The GoI is legally liable for obligations of Division B of the Pension Fund for State Employees and the Nurses' Pension Fund.** The government's liability is not limited to the pension liabilities of ministries and state institutions but also includes obligations of other parties who belong to the funds. These include various companies and organizations who are

members of the funds, for example, various independent institutions which are funded primarily by the GoI. As noted in the GoI financial statements, the statutory contributions to these funds are insufficient to cover fund members' benefits earned. The mission recommends a careful analysis of these arrangements to determine the appropriate accounting and actuarial treatment.

27. **Under defined benefit plans, IPSAS requires a liability to be recognized in the statement of financial position equal to the net total of:**

- The present value of the defined benefit obligation (the present value of expected future payments required to settle the obligation resulting from employee service in the current and prior periods);
- Plus any deferred actuarial gains minus any deferred actuarial losses minus any deferred past service costs; and
- Minus the fair value of any plan assets at the reporting date.

Actuarial gains and losses may be: (a) recognized immediately in surplus or deficit; (b) deferred up to a maximum, with any excess amortized in surplus or deficit (the "corridor approach"); or (c) recognized immediately directly in net assets/equity (in the statement of changes in net assets/equity).

28. **The GoI's pension arrangements with the Pension Fund for State Employees and the Nurses' Pension Fund may qualify as multi-employer plans.** The government should classify a multi-employer plan as a defined contribution plan or a defined benefit plan by analyzing the terms of the plan. A brief review of the arrangement indicated that these plans are defined benefit plan. Where a multi-employer plan is a defined benefit plan, the government should account for its proportionate share of the defined benefit obligation, plan assets, and cost associated with the plan. When sufficient information is not available to use defined benefit accounting for a multi-employer plan that is a defined benefit plan, the government should account for the plan as if it were a defined contribution plan. The government should then provide additional disclosures, such as the reason why sufficient information is not available to enable the entity to account for the plan as a defined benefit plan.

29. **Some apparent liabilities related to pensions are not recognized.** Note 45 (d) provides information about pension liabilities due to Division A of the Pension Fund for State Employees (LSR). The governing law, Act No.1/1997, appears to contain contradictory provisions. Thus Article 13 states that the wage-payers' (government's) liability is limited to their contributions, while elsewhere the law also states that the wage payers' contribution should be based on generally ensuring that the Fund has sufficient assets to cover its obligations. The note provides information about the accrued liabilities of the Fund (LSR) and concludes that the overall negative position of the Fund indicates unequivocally that contributions need to be increased to address this situation. This note is shown as part of contingent liabilities. However, this appears to be a liability to the extent that the accrued

liabilities exceed relevant assets. Therefore these liabilities should be recognized in accordance with IPSAS 25 *Employee Benefits*.

30. **The GoI does not recognize vacation earned, but not taken.** A maximum number of six weeks can be carried over to the next year. An accrual for those accumulating paid leave should be recognized on GoI's balance sheet in accordance with IPSAS 25, paragraph 17.

H. Financial Instruments

31. **The GoI's financial statements provide limited insight into its financial instruments.** The information presented falls short of the extensive requirements included in IPSAS 28 *Financial Instruments: Presentation*, IPSAS 29 *Financial Instruments: Recognition and Measurement* and IPSAS 30 *Financial Instruments: Disclosures*. These are complex standards and the requirements are extensive. Box 3 summarizes the key requirements relating to financial instruments reporting under IPSAS. The GoI should revise its accounting policies and notes to take into account these and other requirements of these IPSAS.

Box 3. Summary of Key IPSAS Requirements Related to Financial Instruments

- Accounting policies, key definitions, and methods adopted, including criteria for recognition and the basis for measurement in respect of each class of financial asset and financial liability should be disclosed, usually in the note on significant accounting policies.
- Details of concessionary loans and financial guarantee contracts entered into at nil or nominal consideration.
- Net income, expense from, and other changes (other economic flows) related to, financial assets.
- Description of financial management objectives and market risk (including interest rate risk, currency risk, and other price risk), credit risk, and liquidity risk. Risks associated with each major class of finance instruments need to be discussed.

32. **The GoI has not entered into any swap agreements.** This has been confirmed to the mission by GoI's debt management unit, led by the Central Bank of Iceland. Following the example of other countries in the region, the government, however, is giving consideration to entering into swap agreements to guard the government against two types of future risks:

- Interest rate risk on borrowings with a variable interest rate; and
- Foreign currency risk on borrowings denominated in foreign currencies, notably Euro and US dollar.

Interest rate swaps and currency swaps aim to reduce risk and the variability in cash flows or earnings that arise from those risks. IPSAS 28, 29, and 30 provide extensive guidance on the recognition of gains or losses on financial assets and financial liabilities associated with derivatives. When considering the use of swaps, the GoI should take this IPSAS reporting guidance into account.

I. Public Debt Valuation

33. **A typical example of a financial instrument that needs more extensive note disclosures is the GoI's long-term borrowings.** Long-term borrowings for the central government part of the general government sector amount to ISK 1.4 trillion as per December 31, 2012 (87 percent of GDP). The GoI's financial statements provide a breakdown by foreign currency denomination, but should also provide a breakdown by maturity date and interest rate.[4]

34. **The GoI measures its public debt including Treasury bills at face value.** Any premium or discount is taken to surplus or loss at the moment of issue of the Treasury bill. IPSAS, however, requires many assets and liabilities, including public debt, to be measured at amortized cost.

35. **Public debt should be measured at amortized cost rather than historical cost or face value if the difference between the two is material.** Amortized cost is the amount at which a financial asset or liability is measured at initial recognition, less principal repayments and plus or minus any unamortized original premium or discount. IPSAS 29 *Financial Instruments: Recognition and Measurement* requires the amortized cost to be calculated using the effective interest method. The effective interest rate exactly discounts the expected stream of future cash payments or receipts through maturity to the net carrying amount at initial recognition. By applying the effective interest rate there is a constant interest rate on the carrying amount. The effective interest rate is the internal rate of return (Box 4). The mission recommends measuring public debt liabilities in accordance with IPSAS 29.

[4] Most of this information is available at the website of the debt management unit: www.ndma.is.

Box 4. Amortized Cost Method using the Effective Interest Rate

The following illustrates the amortized cost method using the effective interest rate.

Assumptions:

- Coupon rate of 4 percent;
- Face value of the bond of 100 (redemption amount);
- An initial consideration (actual receipts from issuing the bond) of 90;
- Transaction costs of issuing the bond of 1; and
- Duration of five years.

The effective interest rate is calculated as 6.66 percent which is the internal rate of return (=IRR function in Excel) of a cash inflow of 89, followed by annual cash outflows of 4 and a redemption amount of 100. The carrying amount shown in the table is measured at amortized cost.

Amortized cost				
Redemption amount (face value):			100	
Year	Carrying amount brought forward	Interest charge at	Cash flow	Carrying amount carried forward
Initial consideration			90	
Transaction cost and discount or premium			-1	
01-01-2010		6.66%	89	
2010	89.00	5.93	-4	90.93
2011	90.93	6.05	-4	92.98
2012	92.98	6.19	-4	95.17
2013	95.17	6.34	-4	97.51
2014	97.51	6.49	-104	0.00

J. Presentation of Financial Statements

36. **The GoI presents the balance sheet showing that total assets equal total liabilities and equity.** A more informative presentation may be to show assets less liabilities equaling equity. This is particularly true in the case of Iceland, where the equity is negative. The current presentation could lead users to interpret equity as a "negative liability"—a difficult concept to understand. Also the classification of assets and liabilities could be made consistent with *GFSM 2001*.

37. **The GoI's balance sheet classifies assets into "high-risk assets and long-term receivables" and "current assets."** IPSAS 1 *Presentation of Financial Statements* (paragraphs 76 to 87) requires current and non-current assets to be separately classified on the face of the statement of financial position, except where a presentation based on liquidity

provides information that is reliable and is more relevant. The mission recommends revising the presentation of the balance sheet.

38. **The GoI present changes in net assets/equity as part of the note disclosure on equity.** IPSAS 1 requires presenting a Statement of Changes in Net Assets/Equity as one of the primary financial statements rather than as a note disclosure. Accumulated surplus/deficit should be shown as a separate component of equity.

39. **In accordance with IPSAS, the GoI provides a classification of expenses by nature as a note disclosure (Note 25).** An allowed alternative under IPSAS would be to provide this information on the face of the operating statement (IPSAS 1, paragraphs 109, 115). This would facilitate consolidation since this classification is common to all agencies. The GoI operating statement shows expenses organized by ministry or other major administrative categories and financing costs.

40. **The GoI operating statement does not distinguish between revenue from non-exchange transactions (taxes and transfers) and revenue from exchange transactions for some items.**[5] IPSAS 1 requires a distinction between the two in the statement of financial performance. This may apply to fines and compensation (Note 21), where fines seem to be revenues from non-exchange transactions and compensations relate to revenues from exchange transactions. Alternatively, if the amounts in this do not include compensation revenue, the note title should be revised. The 2011 financial statements do not appear to include any amounts that may be considered in the nature of compensation.

K. Offsetting

41. **Some revenues and expenditure of government entities are not reported on a gross basis in the financial statements.** Expenditures are recognized net of institutions' independent revenues. This treatment is mandated by the Act (Art. 12) and is consistent with budget presentation. However, this presentation is inconsistent with IPSAS 1, paragraphs 48-50. The amounts are material—ISK 35,104 million or over 6 percent of total expenditure (ISK 575,950 million) and over 12 percent of total operating expenditure (ISK 277,349 million). Note 1.2.2 in the 2011 financial statements states: "In the operating statement for class A expenditures are recognized net of institutions' independent revenues, cf. Art. 12 of the Act, in the same manner as is done in the presentation of Art. 1 and breakdown 2 in the budget and supplementary budget." IPSAS, however, requires all revenues and expenses to be included in the financial statements on a gross basis and does

[5] Exchange transactions are transactions in which one entity receives assets or services, or has liabilities extinguished, and directly gives approximately equal value (primarily in the form of cash, goods, services, or use of assets) to another entity in exchange. Non-exchange transactions are transactions that are not exchange transactions. Examples of exchange transactions are sales of goods and services, interest, dividend and royalties. Examples of non-exchange transactions are taxes and transfers.

not allow offsetting. In order for a government to be transparent, all revenues should be accounted for, whatever source they originate from and whatever government controlled entity receives them. This logic flows from the accountability objective of IPSAS-based financial reporting.

42. **The notes to the balance sheet items follow the format of reconciliation between the balance at the beginning and closing of the year.** While this is an IPSAS requirement for some assets, for example, property, plant, and equipment, and for some liabilities, for example, provisions, it may cause information overload for many other balance sheet items.

43. **The GoI financial statements do not present comparative information in respect of the previous period for all amounts reported in the financial statements.** IPSAS requires this presentation, except when an IPSAS permits or requires otherwise. This also applies to amounts reported in the financial statements that by themselves are not required by IPSAS, such as the reconciliation between the balance at the beginning and closing of the year mentioned above. So, providing the reconciliation for the year 2011 triggers the requirement to also provide the reconciliation for the year 2010 in the 2011 financial statements. (IPSAS 1, paragraph 53).

L. Cash Flow Statement

44. **The GoI reports the cash flow statement according to the indirect method.** The direct method cash flow statement discloses major classes of gross cash receipts and gross cash payments. In the indirect method, cash flow statement surplus or deficit is adjusted for changes in inventories and operating receivables and payables and for non-cash items such as depreciation and provisions. IPSAS allows both methods but encourages entities to apply the direct method because it is more informative to the users of the financial statements. For entities reporting cash flows from operating activities using the direct method, IPSASB also encourages to provide a reconciliation of the surplus/deficit from ordinary activities with the net cash flow from operating activities. This reconciliation would usually be provided in the notes to the financial statements. The mission supported the GoI in preparing a direct method cash flow statement for the FY 2011. Appendix 4 illustrates the preparation of a direct method cash flow statement using the GoI's 2011 indirect cash flow statement.

45. **The cash flow statement should also be revised in two other respects.** From the cash flow statement in the 2011 financial statements the line item "the translation difference and revaluation of cash and bank accounts (Gengismunur og endurmat sjóðs- og bankareikninga)" under "financing activities" should be removed. The description of the line item "translation difference and revaluation of cash and bank accounts" should be replaced by "effects of exchange rate changes on the balance of cash held in foreign currencies."

46. **The GoI recognizes impact of exchange-rate movements on loan accounts through a revaluation account.**[6] IPSAS 4, paragraph 35, however, requires exchange differences to be recognized in surplus or deficit in the period in which they arise. This applies to exchange differences arising: (a) on the settlement of monetary items; or (b) on translating monetary items at rates different from those at which they were translated on initial recognition during the period or in previous financial statements.

M. Events after the Reporting Date

47. **The GoI does not report on events after the reporting date.** IPSAS 14 *Events after the reporting date* establishes criteria for deciding whether the financial statements should be adjusted for an event occurring after the reporting date. It distinguishes between adjustable events (those that provide evidence of conditions that existed at the reporting date, for example, a lost court case that was pending at the reporting date) and non-adjustable events (those that are indicative of conditions that arose after the reporting date, for example, a decrease in the value of real estate after the reporting date).

N. Segment Reporting

48. **The GoI does not provide segment reporting.** IPSAS requires reporting financial information by segments to achieve several objectives:

- To better understand the entity's past performance;
- To identify the resources allocated to support the major activities of the entity;
- To enhance the transparency of financial reporting; and
- To enable the entity to better discharge its accountability obligations.

An entity normally looks to its organizational structure and internal reporting system for the purpose of identifying its service segments and geographical segments. A primary and secondary segment reporting structure may be adopted with only limited disclosures made about secondary segments. The government should disclose segment revenue and segment expense for each segment. Segment revenue from budget appropriation or similar allocation, segment revenue from other external sources, and segment revenue from transactions with other segments should be separately reported. The government should also disclose the total carrying amount of segment assets and segment liabilities for each segment, and the total cost incurred during the period to acquire segment assets that are expected to be used during more than one period for each segment. In its consolidated financial statements, the GoI should distinguish between the following three segments: general government (class A), public non-financial corporation's (class B), and public financial corporation's (class C).

[6] Note 1.2.3 to the 2011 financial statements.

49. **The GoI financial statements present "next year's installments transferred to short-term receivables" as a negative amount under the long-term receivables.** These are the installments on long-term receivables that are due within 12 months. The mission recommends not including negative amounts in this breakdown on the face of the financial statements because this is not common practice. This also applies to next year's installments transferred to short-term liabilities, which are shown as a negative amount under the long-term liabilities.

O. Provisions, Contingent Liabilities, and Contingent Assets

50. **The GoI's balance sheet does not present any provisions.** IPSAS 19 *Provisions, Contingent Liabilities, and Contingent Assets* requires provisions and prescribes recognition criteria and measurement bases for provisions, so as to ensure that sufficient information is disclosed in the notes to the financial statements to enable users to understand their nature, timing, and amount. Provisions may be required to be made for onerous contracts, restructuring, guaranties, court cases, refunds, and site restoration. In particular, if it is considered that payments are likely to be made in respect of guarantees or court cases and the amounts can be measured reliably, provisions should be included in the balance sheet.

51. **The GoI discloses information about guarantees and long-term agreements as part of the note on equity (Note 45).** A detailed list of long-term agreements is separately disclosed in Special Summary 16 *Binding long-term agreements*. IPSAS 19, however, requires disclosures of contingent liabilities including guarantees and long-term agreements in a separate note. Contingent liabilities typically arise when there is a possible obligation to be confirmed by a future event that is outside the control of the entity. Contingent liabilities require disclosure only; they are not recognized as a liability on the statement of financial position, except when it is considered probable that payments would have to be made. If the possibility of outflow is remote, no disclosure is required. The mission recommends disclosure of contingent liabilities and commitments as separate notes, not as part of the note on equity.

P. Related Party Disclosures

52. **The GoI does not include any information about related parties in its financial statements.** IPSAS 20 *Related Party Disclosures* requires entities to disclose the existence of related-party relationships and transactions between the entity and its related parties. This information is required for accountability purposes and to facilitate a better understanding of the financial position and performance of the reporting entity.

53. **Related parties are parties that control or have significant influence over the reporting entity and parties that are controlled or significantly influenced by the reporting entity.** The former includes controlling entities, owners, major investors, and key management personnel, while the latter includes controlled entities, joint ventures, associates, and postemployment benefit plans. If the reporting entity and another entity are subject to

common control, these entities are also considered related parties. This means that class A, B, and C entities, and any associates would be considered to be related parties. IPSAS requires disclosure of:

- Relationships involving control, even when there have been no transactions;
- Related-party transactions; and
- Remuneration of key management personnel.

Q. Budget Information in Financial Statements

54. **The Althingi approves a budget document which includes appendix tables for both cash flow statement and operating statement.**[7] The GoI therefore applies cash budgeting and a form of modified accrual budgeting—modified, because the operating statement reports capital expenditure rather than depreciation and amortization as an expense. In accordance with IPSAS 24 *Presentation of Budget Information in Financial Statements*, the GoI presents a comparison of the budget amounts and actual amounts both for the cash flow statement and the operating statement. IPSAS 24 offers two alternatives for disclosing the comparison between the actual figures and the budget: either a separate statement ("statement of comparison between budget and actual figures"), or an additional column in the financial statements. The GoI applies the latter alternative which is allowed under IPSAS since budget and financial statements have been prepared on a comparable basis, e.g., the cash flow statement presents the actual increase in cash (the "accounts 2011" column) and compares this to the budgeted increase in cash (the "budget/supplementary budget 2011" column).

55. **The GoI presents a comparison of the final budget amounts (labeled budget/supp. budget) and actual amounts but does not show the original budget.** In accordance with IPSAS this comparison should present both the original and final budget amounts in separate columns.

56. **The GoI does not explain whether the changes between the original and final budget are a consequence of reallocations within the budget, or of other factors.** IPSAS 24 requires such an explanation. Without this requirement the explanation of differences between actual figures and budget could be limited if the entity has revised the budget by the end of the budget year to largely align it with the estimates of the actual figures (outcome). This disclosure should be included in the financial statements, unless such a statement is included in a report that is disclosed prior to, at the same time as, or in conjunction with the financial statements, and the notes to the financial statements refer to such a report. The GoI does not comply with this requirement which is a deviation from IPSAS 24. The mission recommends presenting both original and final budget figures; and providing an explanation

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[7] See http://www.ministryoffinance.is/treasury/nr/15651.

of material differences between actual and budget figures; and providing an explanation as to whether the changes between the original and final budget are a consequence of reallocations within the budget, or of other factors.

57. **The GoI's financial statements do not explain the accounting basis used in the preparation and presentation of the budget.** Budget figures are presented for both the operating statement and cash flow statement. IPSAS 24, paragraph 39 requires an explanation of the budgetary basis (cash, accrual, or some modification thereof) and classification basis adopted in the approved budget. This explanation should be included in the notes to the financial statements. The government should also identify in the notes to the financial statements the entities included in the approved budget.

R. Service Concession Arrangements

58. **The GoI currently does not include in its financial statements any service concession arrangements.** IPSAS, however, requires recognition of the service concession asset and related liability if certain conditions are met. These conditions relate to control over the asset, both during and at the end of the arrangement. The recognition of service concession assets and related liabilities in accordance with IPSAS is likely to have only a limited impact on the statement of financial position (balance sheet) of the GoI at this stage. However, this situation may change if more such contracts are entered into in the future as is currently being contemplated by the Ministry of Finance. The mission therefore recommends the adoption of IPSAS 32 *Service Concession Arrangements: Grantor*, and:

- Analyze existing and future service concession arrangements;
- Recognize service concession assets if required by the standard;
- Recognize liabilities under the financial liability model or grant of a right to the operator model, as appropriate; and
- Account for arrangements that are not within the scope of IPSAS 32 using other IPSASs, as appropriate to their specific terms and conditions.

At the request of the authorities, additional guidance on the accounting for service concession arrangements is provided in Appendix VI to this report.

S. Summary of Recommendations

59. The mission recommends that Fjársýsla should**:**

- Undertake an analysis of entities to identify those that are controlled by the government and those that are more in the nature of associates or joint ventures as defined by IPSAS;
- Determine accounting practices applied by controlled entities, associates and joint ventures, and identify any adjustments needed at consolidation;

- Establish mechanisms to identify, reconcile, and eliminate transactions and balances between the government and controlled entities;
- Identify and determine a value for all assets and liabilities to be recognized on the opening balance sheet in accordance with IPSAS, including:
  - entities accounted for using the equity-method;
  - property, plant, and equipment, including finance leased assets;
  - software;
  - inventories;
  - employee benefits liabilities;
  - financial instruments;
  - public debt; and
  - provisions.

- Revise the presentation of the financial statements, including:
  - balance sheet;
  - changes in net assets/equity as a primary statement rather than a note;
  - classification of expenses by nature;
  - distinguish between revenue from exchange and non-exchange transactions;
  - report revenues and expenses on a gross basis rather than net basis; and
  - previous period comparative information for all amounts.

- Prepare the cash flow statement in accordance with the direct method;
- Prepare segment reporting using the GFS sectors as segments;
- Include related party disclosures;
- Include both the original and final budget in the financial statements and explain the differences between them;
- Explain the accounting basis applied for the preparation of the budget;
- Determine the nature of the service concession arrangements and recognize an asset and a liability if appropriate; and
- Determine transitional provisions to be applied, if any.

The timeline for the implementation of these recommendations is discussed in Chapter VI and set out in more detail in Appendix VII Indicative plan for implementation of IPSAS.

III. General improvements to financial statements

A. Analysis of Expenses

60. **Summary 2 (not part of financial statements) and the operating statement combine administrative and economic classifications.** For example, Summary 2 shows expenditures that are classified partly by administrative units (ministries, state institutions etc.), partly by economic categories (services purchased, contributions and grants, interest etc.) and partly by projects. The operating statement shows expenditures mainly by

administrative classification, but also an extra line, "financing cost," which is not an administrative category. The last table of Note 25 starts with administrative classification (Highest state level and ministries, state institutions), but then introduces economic classification (pension), followed by projects, and reverts back to economic classification (services purchased, transfers, and special expenditures including interest).

61. **These analyses are intended to demonstrate that, among other things, certain overspendings were not caused by administrative units but are the results of legislation and specific government decisions.** The mission understands the need for such analyses and agrees with the authorities that these should be supplemented by a standard analysis of expenditure by functional, economic, and administrative classification.

B. Functional Classification

62. **Functional classification is not entirely consistent with COFOG or GFSM 2001.** At the highest level of the classification, an additional category, irregular expenditure, has been added to the 10 major functions in COFOG. Notes 25 and 33 explain that this category includes 'special state expenditures that fluctuate strongly from one year to the next'. These include expenditures on guarantees, pension liabilities, tax paid on financial income, tax claims written-off, and equalization of invalidity burden of pension funds.

63. **Introducing a new function for these items is not good practice.** The fluctuation in the amounts from one year to the next can be explained in the notes, as is done for other items. These items should be classified under one of the ten main functions under COFOG. The mission supports the introduction of a proposed new structure being considered by the authorities that would provide a clearer mapping of their functions with COFOG.

C. Summary of Recommendations

64. **The mission recommends that:**

- The existing special analyses of expenditures should be supplemented by analyses of expenditure in accordance with standard economic, functional, and administrative classifications.
- MoF and Fjársýsla should develop the economic and functional classifications consistent with GFS/COFOG and avoid any departures from these standards at the high levels of this classification system. In particular, "irregular expenditure" as a highest level function should be discontinued.

IV. Alignment of Budget, Financial Statements, and Statistical Reports

A. Introduction

65. **One of the strengths of the existing budgeting framework is the close alignment between budget and annual accounts.** The financial reforms undertaken in the 1990s particularly the Financial Reporting Act (FRA) of 1997 introduced, among other things, accrual accounting reforms. Remarkably by the standards of those times, Iceland went one step further and also introduced similar concepts for budgeting with a view to achieving a consistent budgetary framework which facilitated comparison of plans and outcomes. Even by today's standards, Iceland is one of the few countries in the world that have implemented accrual concepts in both budgets and accounts and thus have ensured a level of alignment in an accrual accounting environment that is relatively uncommon.

66. **This alignment must be maintained following the implementation of IPSAS.** The proposed OBL stresses the importance of maintaining the alignment between budgets and accounts following the implementation of IPSAS. The main changes required to implement IPSAS have been discussed in Chapter II. The significant changes include the preparation of consolidated financial statements for the central government and its controlled entities and the recognition of nonfinancial assets. The requirement to prepare consolidated financial statements is not expected to impact the budget. However, the requirements related to nonfinancial assets have some implications for budget. Other changes such as valuation policies for assets and liabilities may also have an effect on budgets, particularly in improving transparency of fiscal policy by quantifying the full financial implications of policy decisions.

B. Estimated Financial Statements

67. **The budget documents should include full estimated financial statements for the budget year and preferably the next five years.** The coverage of these statements should be consistent with the budget. In the context of IPSAS these statements would be considered the "separate" financial statements of the central government (budget sector). The estimated financial statements should include an operating statement, a balance sheet, a cash flow statement, and a statement of changes in net assets/equity, and related notes. The estimated statements should be prepared applying the same accounting policies that are used to prepare the ex post financial statements. In particular, the budget should recognize revenues and expenses based on accounting policies that are consistent with the ex post financial statements, subject to the ability to measure items reliably. Notes to the estimated statements should disclose the accounting policies followed, including any cases where estimates were revised due to lack of a reliable measure. For example, some tax estimates on accrual basis for budget and forward years may not be fully reliable, and therefore the estimates may have to be based on numbers that are closer to the cash estimates. These estimates and the nature of uncertainty should be disclosed in the notes to the estimated financial statements.

68. **Full consolidated estimated financial statements for the central government and its controlled entities are not required.** Although fiscal policy should be informed by a comprehensive view of the finances of the public sector, the relevant reports are expected to be produced at a high level by the budget department of the MoF. The consolidated ex post financial statements of the central government will be used as inputs to this process. However, there is no requirement to produce full estimated consolidated financial statements in accordance with IPSAS for the budget and the forward years.

C. Depreciation and the Appropriation Framework

69. **The recognition of nonfinancial assets will have a significant effect on the budget.** Under the existing framework purchase of such assets is treated as an expense both in the budget and the annual accounts. The recognition of nonfinancial assets would mean that these transactions would no longer be treated as an expense but as acquisition of assets, or a balance sheet transaction. Instead a new expense—depreciation—would be recognized in the operating statement. This has important implications for the budget.

70. **Depreciation should be recognized as an expense in the estimated financial statements.** This implies that the purchase of assets would no longer be treated as an expense. This can have a significant effect in the operating result and the total balance in the Treasury operating statement that is included in the current budget documentation. However, under the proposed OBL the GFSM 2001 based net lending/borrowing will be the primary fiscal indicator. As net lending/borrowing is calculated by excluding depreciation and including net acquisition of assets as expenditure, this indicator will be unaffected by the inclusion of depreciation as an expense in the estimated financial statements.

71. **A common harmonized format should be adopted to present estimated and ex post financial statements.** In particular, the operating statement should be presented in a format that enables the generation of both IPSAS and GFSM 2001 based key indicators. This will ensure that there is only one format of the operating statement and no separate reconciliations of the budgets and accounts—particularly between net lending/borrowing and operating result—will be required. The FAD TA Report of January 2012 discussed this issue and provided an example of the presentation.

72. **A number of options exist in respect of the treatment of depreciation for appropriation purposes.**[8] While appropriating depreciation is consistent with the need to maintain alignment between budgets and accounts, appropriation for depreciation is an issue that has been the subject of some debate. In practice, there is no single model for dealing with depreciation in an accrual budgeting framework and different countries have developed different ways of handling this issue. The options include:

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[8] See *Accrual Budgeting: Opportunities and Challenges,* by Abdul Khan, in IMF Publication *Public Financial Management and its Emerging Architecture (2013).*

- Appropriate depreciation and allow agencies to use this appropriation for routine asset replacement, any additional capital expenditure being separately appropriated, New Zealand uses this approach;
- Appropriate depreciation and capital expenditure, but prohibit the use of the appropriation for depreciation for any cash expenditure under other budget items, Switzerland uses this approach;
- Appropriate both accrual based expenses and cash expenditure and impose legal controls on both; the U.K. uses this approach; and
- Appropriate capital expenditure, but not depreciation; estimated financial statements include depreciation as an expense, Australia uses this approach.

73. **In Iceland, depreciation need not be appropriated at this stage.** The first option above maintains the maximum alignment between budget estimates, appropriations, and ex post financial statements. However, it also can result in complexities that are preferably avoided at this stage when the government will be busy implementing IPSAS. The Swiss and the U.K. approach are also consistent with an aligned framework with additional controls on cash, but may again introduce complexities at this stage that are best avoided. Therefore, it is suggested that Iceland adopt a framework under which, while depreciation would be treated as an expense in the estimated financial statements and other relevant budget documents, the appropriation should continue to be for purchase of assets and not depreciation. This approach has the advantage of avoiding a major change to the existing appropriation framework, while ensuring that budgets and annual accounts are fully aligned by treating depreciation as an expense in the estimated financial statements. This approach may be revisited after a few years when adequate experience and data have been accumulated to provide an informed and reliable foundation to move on to a framework that includes appropriation for depreciation.

D. Summary of Recommendations

74. The mission makes the following recommendations:

- MoF should adopt a presentation of the budget (commencing with the 2016 budget) that includes a full set of estimated financial statements—including an operating statement, a balance sheet, a cash flow statement, a statement of changes in net assets/equity, and relevant notes;
- MoF and Fjársýsla should adopt a presentation of the estimated and ex post operating statement that displays on the face of the statement both the net lending/borrowing and the operating result, showing the relationship between these two indicators;
- MoF should include accrual based revenues and expenses, particularly depreciation, in accordance with IPSAS based accounting policies adopted for ex post financial statements; Fjársýsla should provide necessary information to the MoF to facilitate this process; and

- Depreciation need not be appropriated at this stage. MoF should revisit this issue after a few years based on experience of dealing with depreciation—particularly estimating depreciation for future years.

V. AUDIT

A. Auditing Standards

75. **The independent audit of the 2012 financial statements has not been conducted in accordance with internationally accepted auditing standards.** The audit report on the 2012 financial statements issued by the Icelandic National Audit Office (INAO) states that the audit was carried out in accordance with the Act on the National Audit Office and good auditing practices for state entities. This Act does not require compliance with International Standards on Auditing (ISA) or International Standards of Supreme Audit Institutions (ISSAI). The INAO is in the process of implementing ISSAI and plans to carry out the audit of the 2013 financial statements in accordance with ISSAI. INAO, however, may not refer to ISSAI in the audit opinion until it is satisfied that full compliance with the standards has been achieved. Parliament is expected to decide shortly on an updated Act on INAO. Under the proposed new Act it will remain the Auditor General's responsibility to choose the auditing standards applied. The mission recommends applying ISSAIs to ensure high-quality audits.

76. **Consolidated financial statements will expand the scope of work of the Auditor General and the INAO considerably.** This is because the audit opinion will cover the consolidated financial statements of the GoI, including the public nonfinancial enterprises (class B) and public financial enterprises (class C). The Auditor General will effectively conduct a group audit, for which guidance is provided by the ISSAI 1600 *Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors)* and by the related ISSAI Practice Note. ISSAI 1600 deals with special considerations that apply to group audits, in particular those that involve component auditors. In this case the INAO serves as the group auditor and the component auditors are the auditors of the public enterprises and other controlled entities. In accordance with ISSAI 1220 *Quality Control for an Audit of Financial Statements*, the Auditor General (the "group engagement partner") is required to be satisfied that those performing the group audit engagement, including component auditors, collectively have the appropriate competence and capabilities. The group engagement partner is also responsible for the direction, supervision, and performance of the group audit engagement. The mission recommends that the INAO takes steps to prepare for these extended responsibilities in a timely manner.

B. Summary of Recommendations

77. **The mission recommends that the INAO should:**

- Apply the International Standards of Supreme Audit Institutions (ISSAI), commencing 2014 financial statements.

VI. Strategy and Plan for Implementation

78. **A successful implementation of IPSAS will require careful planning and management.** The implementation process should not unduly disrupt the activities of officials and organizations, while making necessary progress in implementation through the resolution of key issues in a timely manner and appropriate sequence. This chapter describes a strategy for implementation developed based on extensive discussions with, and input from, the GoI officials. The strategy takes into account the IT systems and processes, human capacity, and other implications of the planned reforms and proposes a detailed sequenced plan (see Appendix VII) for implementation of IPSAS in respect of key areas, including consolidated reporting, nonfinancial assets, other assets, liabilities, revenues, and expenses.

79. **The implementation strategy recognizes Iceland's specific circumstances.** In particular, the strategy takes the existing accounting framework as a starting point. The GoI has been preparing accrual-based financial statements since 1998. Government entities follow accounting policies that are broadly consistent with internationally accepted standards. This has also led to the development of considerable skills in accounting concepts and practice and related IT systems and processes. The planned implementation of IPSAS is therefore not expected to require extensive changes either in accounting or systems and procedures. The implementation strategy builds on the strengths of the existing framework and is designed to reduce implementation risks further by proposing a phased implementation approach, as discussed in detail in the following sections.

80. **The number of accounting and reporting policies where major efforts would be required immediately is likely to be small.** The gap analysis in Chapter II demonstrates that, while a number of changes would be required, the existing financial statements provide a sound basis for transition to IPSAS. This implementation strategy therefore focuses on two major areas—preparation of consolidated financial statements and reporting of nonfinancial assets—where the existing framework differs from IPSAS and provides detailed suggestions on the approach to, and the sequence in which, the necessary improvements could be made within a phased implementation approach. Other areas where less extensive improvements are likely to be required are also discussed.

81. **The structure of the government and the organization of its accounting arrangements are also likely to limit the operational impact of the move to IPSAS.** The central government comprises 8 ministries and 189 agencies. One hundred and thirty nine of these 197 entities are relatively small (staff of fewer than 70) and only two may be considered large (staff of more than 1,000). Most of the 197 entities have relatively simple operations and few have significant assets. Fjársýsla undertakes the accounting for 91 entities, including all ministries. Approximately 92 percent of the 197 entities use the Oracle E-Business Suite system operated by Fjársýsla, with the rest using their own systems but providing monthly accounting data into the Oracle system.

A. **Phased Approach to Implementation**

82. **In general, an implementation strategy can be based on one of two approaches– a "big bang"approach or a phased approach.** A big bang approach would entail a switch from the pre-IPSAS accounting system to full IPSAS compliance commencing from a particular date. By contrast, a phased approach involves the progressive implementation of improvements in a planned sequence, with the aim of meeting IPSAS requirements to the fullest extent practicable by the end of the final phase.

83. **Existing IPSASs contain several transitional provisions.** Chapter II of this report has indicated some of the transitional provisions available in IPSAS (for elimination of transactions and balances at consolidation and recognition of property, plant, and equipment, and intangible assets) but more exist. The IPSAS Board has issued a draft standard *First-Time Adoption of Accrual Basis IPSASs* which may allow additional transitional provisions.[9] By applying transitional provisions, the government may limit the amount of work needed to prepare the opening balance sheet: some of the work is eliminated altogether; and some work is deferred until after transition date.

84. **However, applying transitional provisions limits the benefits of adoption of IPSAS in the short term.** This is because the desired level of completeness and transparency of the financial statements will not be reached at the begriming of the transition period, but will only be achieved over time. Also, applying some of the provisions including those on property, plant, and equipment, defined benefit plans and other employee entitlements, and financial instruments may affect fair presentation of the financial statements and attract a qualified audit opinion.

85. **The mission recommends a phased approach to the implementation of IPSAS.** A big-bang approach, under which all or most of the requirements of IPSAS would be implemented from a specific date, involves risks and could lead to a significant delay until all preparations are completed for a full implementation. By contrast, a phased approach would allow some IPSAS requirements to be met in the short term, with progressive implementation of IPSAS over the medium term. A phased approach would also allow time to build IPSAS-related skills and expertise in keeping with the pace of implementation. Having regard to current accrual accounting framework, the IT-systems in place, and the capacity of the staff , a phased approach in which the identified gaps compared to IPSAS are closed and the quality of the accounting information is improved progressively during an implementation phase seems to be appropriate.

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[9] The draft standard *First-Time Adoption of Accrual Basis of IPSAS* has not yet been finalized and the existing draft may be revised.

86. **Implementation efforts should focus initially on ex post reporting.** While it is essential that budgets and financial statements are fully aligned, it would be advisable to go through a transitional phase during which the focus is on implementing IPSAS for ex post reporting only. This approach will reduce the implementation risks and avoid undue complexities, cost, and delay. Applying some of the IPSAS-related changes, particularly depreciation to budgeting at this stage would present some difficulties, including the lack of relevant data and practical experience of dealing with these issues. For these reasons the implementation strategy envisages the application of IPSAS to financial statements first, and then subsequently use the experience and the relevant data (e.g., for depreciation) to inform the budget preparation**.** As more fully discussed below (see paragraph 88) budgets and financial statements would be fully aligned in 2016.

87. **IPSAS based financial statements should initially be prepared on a trial basis in parallel with official accounts on the existing basis.** The proposed OBL, which requires the implementation of international standards, is currently expected to be enacted in 2014 with the effective date of implementation being January 1, 2015. This would imply that no changes to official budgeting and reporting systems and procedures can be made until that date. Under the proposed phased approach trial financial statements on an IPSAS basis would be prepared for 2014 and 2015 without making changes to the official systems and procedures.

88. **The suggested phased approach consists of the following:**

- Trial opening balance sheet as at January 1, 2014 – target: September 2014;
- Trial financial statements for 2014 – target: June 2015;
- Formal budget incorporating relevant IPSAS adjustments for 2016 – drafts should be ready for parliament by September 2015;
- Second more refined trial financial statements for 2015 – target: June 2016; and
- Official IPSAS-based financial statements for 2016 including comparisons with budget – target: June 2017.

Table 2 below summarizes the proposed phased approach and each phase is discussed in more detail in the remainder of this chapter.

Table 2. Iceland: Phased Approach to IPSAS Implementation

Trial balance sheet January 2014	• **Trial IPSAS opening balance sheet as at January 1, 2014** • Review report by Auditor-General to Minister of Finance and Fjársýsla • Target: September 2014 • Formal financial statements according to existing accounting practices
Financial Statements 2014	• **First trial IPSAS consolidated financial statements (2014)** • May be made publicly available • Review report by Auditor-General to Minister of Finance and Fjársýsla • Target: 30 June 2015 • Formal financial statements according to existing accounting practices
Budget 2016	• **First budget aligned with IPSAS financial statements (2016)** • Based on trial balance sheet and trial financial statements 2014 • Target: September 2015
Financial Statements 2015	• **Refined trial IPSAS financial statements (2015)** • Refined IPSAS financial statements (complete set of financial statements incl. notes) • May be made publicly available • Review report by Auditor-General to Minister of Finance and Fjársýsla • Target: June 2016
Financial Statements 2016	• **First official IPSAS financial statements aligned with budget (2016)** • Audit by Auditor-General • To be made publicly available • Target: June 2017

89. **INAO should support the Fjársýsla and Ministry of Finance during the implementation period.** The implementation of IPSAS is a complex and time-consuming process that would benefit from close collaboration between Fjársýsla and Ministry of Finance and the INAO. While maintaining its independence, INAO can assist by providing expert advice on accounting and auditing issues, giving feedback on systems and processes and confirming the appropriateness of accounting policies. In particular, it would be important for INAO to issue a review report on the trial opening balance sheets (as at January 1, 2014) and the two trial annual financial statements (for 2014 and 2015) and provide comments identifying issues and areas where improvements are needed. Fjársýsla and the Ministry of Finance should consider the comments systematically and make appropriate improvements to the form and content of financial statements, accounting policies, systems, and processes.

Phase I: Trial opening balance sheet as at January 1, 2014

90. **The implementation starts with the preparation of balance sheets as at January 1, 2014.** This is expected to be completed by September 2014 and will provide the opening balance sheet as at January 1, 2014**.** Two balance sheets would be prepared:

- A balance sheet for the budgetary central government (class A) ("separate balance sheet") including nonfinancial assets and restatements of other assets and liabilities in accordance with IPSAS;
- A balance sheet of the government and its controlled entities (class B and C) ("consolidated balance sheet") eliminating inter-entity balances at least within the A class and between A and B as well as A and C classes, including nonfinancial assets and restatement of assets and liabilities in accordance with IPSAS; and
- The INAO should review these balance sheets and provide a review report to the Fjársýsla and the MoF.

91. **The balance sheets would be prepared in addition to the financial statements according to the existing accounting practices.** A necessary first step in the transition to IPSAS is stocktaking of assets and liabilities and valuation according to IPSAS standards to arrive at an opening balance sheet that is prepared in accordance with IPSAS. This step should contain: (i) a revaluation of already recognized items, if necessary (see Chapter II); (ii) the recognition and initial valuation of nonfinancial assets; and (iii) the consolidation of controlled entities. However, it is recognized that this first balance sheet may not be fully compliant with IPSAS requirements and that further improvements may be required during the preparation of trial financial statements for 2014 and 2015.

92. **The preparation of an opening balance sheet would require several implementation activities.** The main activities are: (i) use the existing databases to provide information for nonfinancial and intangible assets in order to calculate values to be incorporated in the balance sheet; (ii) collect information on inter-entity balances to enable the preparation of the consolidated balance sheet of A, B, and C classes; and (iii) revalue pension liabilities and recognize provisions in the balance sheet. The detailed activities are outlined in Appendix VII. The process of developing the trial opening balance sheet and the outcome should be documented.

93. **The preparation of an opening balance sheet does not require a revision of the IT-system.** The information prepared for the current statements can be combined, and if necessary revalued (e.g., pension liabilities) with additional required information (e.g., non-financial assets) in an Excel spreadsheet. This process would introduce the staff in Fjársýsla and in the MoF to some of the challenges involved with the implementation of IPSAS.

Phase II: First trial financial statements (2014)

94. **The first full set of financial statements in accordance with IPSAS should be prepared for 2014.** Both separate financial statements (for the budgetary central government) and consolidated financial statements (for A, B, and C class of entities) should be prepared[10] according to IPSAS to the extent practicable. They should include a balance sheet, operating statement, cash flow statement, and a statement of changes in net assets/equity. Since the budget and the trial financial statements will not be prepared on the same basis, IPSAS does not allow the operating statement and cash flow statement to include the budget figures (IPSAS 24 *Budget information in the financial statements,* paragraph 21). The official financial statements of 2014 should include a comparison of budget and actuals on a comparable basis (IPSAS 24, paragraph 14). The financial statements should be available by June 30, 2015 as these statements would provide the basis for the development of the budget for 2016. As discussed more fully in Chapter IV, the operating statement should be designed to present key indicators according to IPSAS and GFS. This would require the presentation of both operating result and net lending/borrowing and the reconciliation between the two indicators on the face of the operating statement.[11]

95. **It is recognized that the first set of consolidated statements may not achieve the objective of a full consolidation.** A full consolidation requires the elimination of all transactions and balances among the entities subject to consolidation. This requires the systematic identification and recording of all such transactions and balances in the entities. Changes in systems and procedures required to enable a fully automated collection and elimination of inter-entity transactions and balances would need more time. It is therefore expected that the 2014 consolidated financial statements may, in practice, eliminate only some of the more material transactions and balances, with the objective of achieving full consolidation in the following year. The authorities are considering the option of initially eliminating transactions and balances among A and B, and the A and C class of entities, while aggregating the transactions and balances among the B and C class of entities.

96. **The central government and the consolidated financial statements should be subject to review by the INAO.** The INAO should conduct the review with a view to assessing the extent to which the financial statements are consistent with IPSAS. The INAO should report the departures from IPSAS and make recommendations for addressing the issues. The financial statements along with the report of the INAO could be published, but is not essential provided the existing financial statements and related audit reports are published.

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[10] It is expected that the existing classes B to E would be consolidated by the proposed OBL into B and C class of entities.

[11] See an illustrative format for this type of presentation in Table 5.3 of the FAD TA report of January 2012.

97. **During 2014, requirements for systems and procedures should be assessed to facilitate the recording of transactions and balances in accordance with IPSAS.** In particular the purchase and sale of nonfinancial assets should be recorded as transactions in assets rather than expenses, as is the case under the current system. Similarly, a consolidation system and related procedures should also be developed. These improvements will involve changes to the government's Oracle system and possibly other IT-systems. It would be important to specify the requirements in detail to ensure that the system improvements can be achieved without causing disruptions to normal operations.

Phase III: Budget of 2016

98. **The first budget that is aligned with IPSAS financial statements is expected to be prepared for 2016.** Implementation of IPSAS would require, among other things, the recognition of depreciation as an expense and it is expected this will be a key change in the budget. 2016 is the first year that depreciation can realistically be expected to be estimated for the budget and the forward years. The experience gained and data collected in connection with the preparation of the IPSAS-based financial statements for 2014 would be used to prepare the estimates for 2016 budget and forward years. The 2014 financial statements are expected to be ready by June 2015 giving some time to prepare the estimates to be submitted to the Althingi by September 2015. Close cooperation between the Fjársýsla and the MoF would be required as the MoF may need input from the trial financial statements before its full completion in June to prepare the budget in a timely manner. From this year the budgets and financial statements would be aligned. In particular, the operating statement for both the budget and the financial statements would include comparable revenues and expenses, including depreciation.

Phase IV: Refined trial financial statements (2015)

99. **The financial statements for 2015 should make further progress in meeting the requirements of IPSAS.** The experience gained from the 2014 financial statements preparation process along with the INAO findings should be acted upon with the objective of achieving full compliance with IPSAS. In particular all material nonfinancial assets should be included in the systems and reported in the financial statements. Similarly, material intra-government transactions and balances should be identified and eliminated.

100. **These financial statements should also be subject to a detailed review of the INAO, which should report their findings to the Minister of Finance and Fjársýsla.** The Minister of Finance should give directions to resolve the issues raised by the INAO so that they are avoided in the context of the first official IPSAS based financial statements for 2016. The financial statements along with the INAO report could be published but this is not essential if the traditional financial statements are still being published.

Phase V: First official IPSAS based financial statements (2016)

101. **The financial statements for 2016 should be subject to audit by the INAO.** The traditional financial statements can be discontinued and replaced by the financial statements prepared in accordance with IPSAS and relevant laws and regulations. Any material departures from the standards should be disclosed and explained in the financial statements and where possible the effect of such departures should be quantified. The INAO will provide an audit opinion on the financial statements in accordance with the ISSAI (see Chapter V).

B. System Issues

102. **The implications of the planned move to IPSAS for IT systems are likely to be manageable.** The Fjársýsla has been using an integrated accrual-based financial management system, commonly referred to as Oracle E-Business Suite, for more than ten years. The Fjársýsla carries out the accounting functions for most of the class A entities. Eight percent of the agencies use other systems and transfer their accounting data to Oracle monthly.

103. **An important change to the Oracle system necessitated by the implementation of IPSAS would be in respect of nonfinancial assets.** Currently the system records nonfinancial assets as expenses. However, Oracle has the functionality for recording nonfinancial assets as assets and calculating depreciation, and thus the key requirement is to activate this functionality after any necessary reconfiguration. Some information related to assets (particularly equipment) is recorded in the asset module, but this is currently not integrated with the general ledger module. Important classes of nonfinancial assets are registered in other applications whose data can be transferred to Oracle and used for the preparation of IPSAS-based financial statements. In particular, as more fully discussed in Chapter II, the infrastructure assets (roads, bridges, and tunnels) land and buildings are recorded in registers with detailed information. Furthermore, historical or depreciated replacement cost and/or market value information is available for land and buildings. These systems also have information about depreciation. For these assets, therefore, no immediate major changes to Oracle are expected to be required.

104. **The requirement to produce consolidated financial statements would also have some system implications.** However, the implementation strategy envisages that during the initial stages the consolidation exercise would be undertaken using simple systems, perhaps based on Excel. Consideration should give to other more robust solutions such as applying Oracle E-Business Suite for consolidation or acquiring specialized consolidation software**.**

C. Training and Communication

105. **The training and other capacity development strategies should reflect the strengths of the existing systems and procedures.** Staff have been working with accrual-based accounting, systems, and financial reporting for many years and are familiar with the

relevant concepts and their practical implications. Staff of Fjársýsla, the MoF, the INAO, and some other agencies have developed considerable expertise in preparing and using accrual-based financial statements and would, therefore, require training only on specific IPSAS issues, particularly in areas where improvements or changes are required as identified in Chapters II and III.

106. **Training requirements outside the core government are also expected to be limited.** Officials at significant B and C entities also follow accrual accounting and, in many cases, International Financial Reporting Standards (IFRS) and are not expected to require any significant training. The impact of IPSAS adoption by central government is expected to have limited or no impact on the financial reporting by municipalities. Furthermore, municipalities follow accrual accounting policies that are close to internationally accepted standards, including preparing consolidated financial statements and reporting on nonfinancial assets. It is therefore not expected that the officials of municipalities would require any training. However, the Fjársýsla and the MoF should communicate the implications and reporting requirements that may apply to these entities as a result of central government implementing IPSAS and adopting a greater GFS focus in budgetary reporting. Under the proposed OBL line ministries are expected to be given more responsibilities to manage their portfolios of agencies and programs and would require to be trained, including on budgetary and financial reporting issues, to enable them to perform this role effectively.

107. **A target-group specific training process should be initiated.** Training can concentrate on IPSAS-related issues and on specific implementation requirements, but different target groups have different requirements:

- A core team of the Fjársýsla preparing the financial statements and the INAO auditing the statements need to be trained to acquire a broad and general knowledge of IPSAS and GFS. More specialist expertise on these standards can be sought from accounting firms or other sources as appropriate. These training activities should be initiated as soon as possible;
- Budget analysts in the MoF should be trained in understanding the reports prepared which enables them to prepare the budget in the new format and to use the information for overseeing the budget. A core staff in the MoF should be trained also on the IPSAS standards in a comprehensive way;
- Accounting and budget/finance staff (in ministries and agencies) would need specific training on the system changes and related conceptual issues;
- Staff in the B and C class of entities preparing information for the consolidated financial statements would have to be provided with documentation of requirements. Some training may also be necessary on specific government related issues. However, as many of these officials are likely to be familiar with IFRS or comparable requirements, the training requirements are not expected to be extensive; and
- Relevant staff in line ministries should be specifically trained to develop an understanding of the information in IPSAS-based statements.

108. **Effective communication is essential for securing support of key stockholders and should be given high priority.** The risk of the reforms being seen as a technical exercise and ignored by policy makers and legislators should be addressed by developing a communications strategy and faithfully executing it. The members of Althingi and their key advisors should be provided with explanations of the information provided in the IPSAS-based financial statements and how this can help them in carrying out their functions of oversight of the public finances. The MoF, INOA, and key officials in ministries should be briefed on the objectives and progress of the reforms with a focus on explaining how the reforms can help them perform their functions better. An early start of the communication effort during the preparatory phase can pay rich dividends in terms of acceptance of the reforms and addressing any initial reservations among key stakeholders.

D. Other Implementation Issues

109. **Legal requirements have to be identified and amended accordingly.** The new OBL foresees an accounting standards board with the function to decide whether a standard should be applied or not. Thus, before the implementation of the financial statements in 2016, the board has to formally approve the standards. In a first step, a draft of the accounting policy should be approved by June 2014 to guide the further implementation. The full accounting policy should be approved well in advance before the formal implementation. In addition, Fjársýsla should develop the necessary guidelines so that both trial financial statements and financial statements as of 2016 can be prepared. Furthermore, other legal requirements should be identified and amended accordingly.

110. **Further technical assistance may be helpful during the implementation process.** In particular, further assistance could be provided in respect of IPSAS-related issues including developing the form and content of financial statements that meet the relevant requirements of standards such as IPSAS and GFS. Any need for TA would be considered by FAD management.

E. Summary of Recommendations

111. The mission recommends that:

- Fjársýsla should develop a detailed implementation plan by March 2014.
- Fjársýsla should develop, by September 2014, a balance sheet as at January 1, 2014 based on IPSAS.
- Fjársýsla should analyze IT-requirements by the end of 2014.
- Fjársýsla should issue the necessary guidelines by September 2014 in connection with the preparation of the trial financial statements for 2014. These instructions should be updated and reissued by September 2015 for the 2015 financial statements.
- Fjársýsla should prepare, by June 2015, full sets of separate financial statements of the government and consolidated financial statements for 2014.

- Fjársýsla should prepare, by June 2016, full sets of separate financial statements of the government and consolidated financial statements for 2015.
- Fjársýsla should prepare, by June 2017, the first official full sets of separate financial statements of the government and consolidated financial statements for 2016.
- Fjársýsla and the MoF should include comparison of budget and actual results in the operating statement showing both net lending/borrowing and operating result.
- Fjársýsla should develop a communication and training strategy by June 2014.
- INAO should review the opening IPSAS balance sheet as at January 1, 2014 and the trial IPSAS financial statements for 2014 and 2015.
- INAO should commence auditing the official IPSAS financial statements and issuing audit opinions from 2016.

Appendix I. IPSAS Standards Considered Relevant for the Government of Iceland

IPSAS 1 Presentation of Financial Statements
IPSAS 2 Cash Flow Statements
IPSAS 3 Accounting Policies, Changes in Accounting Estimates and Errors
IPSAS 4 The Effects of Changes in Foreign Exchange Rates
IPSAS 5 Borrowing Costs
IPSAS 6 Consolidated and Separate Financial Statements
IPSAS 7 Investments in Associates
IPSAS 8 Financial Reporting of Interests in Joint Ventures
IPSAS 9 Revenue from Exchange Transactions
IPSAS 12 Inventories
IPSAS 13 Leases
IPSAS 14 Events After the Reporting Date
IPSAS 17 Property, Plant and Equipment
IPSAS 18 Segment Reporting
IPSAS 19 Provisions, Contingent Liabilities, and Contingent Assets
IPSAS 20 Related Party Disclosures
IPSAS 21 Impairment of Non-Cash-Generating Assets
IPSAS 23 Revenue from Non-Exchange Revenues (Taxes and Transfers)
IPSAS 24 Budget Information in the Financial Statements
IPSAS 25 Employee Benefits
IPSAS 22 Disclosure of Financial Information about the General Government Sector
IPSAS 26 Impairment of Cash-Generating Assets
IPSAS 28 Financial Instruments: Presentation
IPSAS 29 Financial Instruments: Recognition and Measurement
IPSAS 30 Financial Instruments: Disclosures
IPSAS 31 Intangible Assets
IPSAS 32 Service Concession Arrangements: Grantor

Appendix II. IPSAS Standards *Not* Considered Relevant for the Government of Iceland

IPSAS 10 Financial Reporting in Hyperinflationary Economies
IPSAS 11 Construction Contracts
IPSAS 15 Financial Instruments: Disclosure and Presentation (withdrawn, refer to IPSAS 28, 29 and 30)
IPSAS 16 Investment Property
IPSAS 27 Agriculture

Appendix III. Example of Certification by the Minister of Finance of New Zealand

I accept responsibility for the integrity of these financial statements, the information they contain and their compliance with the Public Finance Act 1989.

In my opinion, these financial statements fairly reflect the financial position of the Crown as at 30 June 2013 and its operations for the year ended on that date.

Hon Bill English
Minister of Finance
30 September 2013

Appendix IV. Preparation of Direct Method Cash Flow Statement (2011)

	Income Statement	*Cash flow statement - Indirect method as included in 2011 financial statements*	*Cash flow statement - Direct method*
	(ISK million)	(ISK million)	(ISK million)
Cash flows from operating activities			
Surpus/(deficit)		(89,424)	
Receipts			
Tax revenues and social security contributions	441,397	(15,715)	425,682
Contributions	1,642		1,642
Total other revenues	35,611	10,570	46,181
Sale of tangible assets	4,341		4,341
Revenue from monetary assets	3,535	314	3,849
Payments			
Operating expenditure excl. financing cost	(211,761)	29,711	(182,050)
Operating and consumption transfers	(241,896)	14,409	(227,487)
Financing cost	(65,588)		(65,588)
Maintenance	(9,159)		(9,159)
Capital transfers	(35,329)		(35,329)
Net cash flows from operating activities		(50,135)	(37,918)
Cash flows from investing activities			
Capital expenditure	(12,217)		(12,217)
Long-term loans granted		(11,162)	(11,162)
Instalments on long-term loans granted		121,176	121,176
Payment in advance towards long-term cost		(1,138)	(1,138)
Purchase of equities and capital contributions		(1,446)	(1,446)
Sale of equities and holdings		765	765
Net cash flows from investing activities		108,195	95,978
Cash surplus/deficit (GFS)		58,060	58,060
Cash flows from financing activities			
Net short-term loans taken		(13,170)	(13,170)
New loans this year		386,392	386,392
Loan instalments		(226,753)	(226,753)
Net cash flows from financing activities		146,469	146,469
Surpus/(deficit)	(89,424)		
Net increase/(decrease) in cash and cash equivalents		204,529	204,529
Cash and cash equivalents at the beginning of the period		317,486	317,486
Effects of exchange rate changes on the balance of cash held in foreign currencies		11,870	11,870
Cash and cash equivalents at the end of the period		533,885	533,885
			-

Capital expenditure amounted to 12.217. These are included in the net cash flows from operating activities in the cash flow statement as included in the 2011 financial statements. In the cash flow statement according to the direct method (right-hand column), these are presented as investing activities.

Appendix V. Accounting for Service Concession Arrangements

A. Introduction

At the request of the authorities, this appendix provides some guidance on the accounting treatment of one type of public-private partnerships: service concession arrangements. The GoI has currently only few service concession arrangements in place but is considering entering into more such arrangements in the near future. IPSAS 32 *Service Concession Arrangements: Grantor* prescribes the accounting for service concession arrangements by the grantor. Service concession arrangements are arrangements in which:

- The operator uses the service concession asset to provide a public service on behalf of the grantor for a specified period of time; and
- The operator is compensated for its services over the period of the service concession arrangement.

A grantor (the government) is the entity that grants the right to use the service concession asset to the operator. An operator (the company) is the entity that uses the service concession asset to provide public services subject to the government's control of the asset.

B. Typical Features of Service Concession Arrangements

A typical type of service concession arrangement that falls within the scope of IPSAS 32 is a "build-operate-transfer" arrangement. Under this type of arrangement, an operator constructs the infrastructure to be used to provide a public service, and it operates and maintains that infrastructure for a specified period of time. The operator is paid for its services over the period of the arrangement. A contract sets out performance standards, pricing mechanisms, and arrangements for arbitrating disputes. In some cases, the operator may upgrade the existing infrastructure and maintain and operate the upgraded infrastructure. This second type of arrangement is sometimes referred to as a "rehabilitate-operate-transfer" arrangement. Outsourcing the operation of an entity's internal services (e.g., employee restaurant, building maintenance, accounting, or IT functions) does not constitute a service concession arrangement.

Some common features of service concession arrangements are described below.

- The grantor is a public sector entity;
- The operator is responsible for at least some of the management of the service concession asset and related services and does not merely act as an agent on behalf of the government;
- The arrangement sets the initial prices to be levied by the operator and regulates price revisions over the period of the service concession arrangement;
- The operator is obliged to hand over the service concession asset to the government in a specified condition at the end of the period of the arrangement, for little or no incremental consideration, irrespective of which party initially financed it; and

- The arrangement is governed by a binding arrangement that sets out performance standards, mechanisms for adjusting prices, and arrangements for arbitrating disputes.

IPSAS 32 applies to a broad range of concession arrangements. Road and water treatment concession arrangements are two common examples, but other types of arrangements may meet the scope criteria, such as contracts for the:

- Provision of transport services;
- Construction and operation of waste treatment plants;
- Provision of public airport services;
- Construction and maintenance of hospitals;
- Generation of renewable energy;
- Production of electricity; and
- Construction and operation of public transport systems, schools, prisons etc.

There are many different types of concession arrangements, and the detailed structure and arrangements are often specific to jurisdictions. Therefore, in order to determine the appropriate accounting for an arrangement, the details of the arrangement should be analyzed based on the specific facts and circumstances.

C. When Should the Government Recognize a Service Concession Asset?

IPSAS 32 requires the government to recognize an asset as a service concession asset if the following conditions are met:

- The government controls or regulates what services the operator must provide with the asset, to whom it must provide them, and at what price; and
- The government controls—through ownership, beneficial entitlement or otherwise—any significant residual interest in the asset at the end of the term of the arrangement.

For a "whole-of-life" asset, only the conditions in the first bullet need to be met.

Only assets provided by the operator (existing asset of the operator, constructed or developed, purchased or an upgrade to an existing asset of the government) are recognized. Existing assets of the government (other than upgrades thereto) used in a service concession arrangement are reclassified as service concession assets—no additional asset and related liability are recognized in such cases.

IPSAS 32 does not create new principles for timing of recognition of the service concession asset, or its measurement. It refers to the IPSAS standards where those principles are set out, and provides relevant application guidance. One area on which guidance was provided related to assets that were constructed or developed by the operator to illustrate how the service concession asset are be recognized in accordance with IPSAS 17 *Property, Plant, and Equipment* or IPSAS 31 *Intangible Assets*.

Under IPSAS 32, the government must recognize the service concession asset and related liability if the conditions for asset recognition in IPSAS 17 or IPSAS 31, are also met.

D. Treatment of the Liability

The type of liability the government recognizes under IPSAS 32 depends on how the government compensates the operator.

Financial liability model

The government compensates the operator for the construction, development, acquisition, or upgrade of a service concession asset and service provision by making a predetermined series of payments to the operator.

The transaction meets the definition of a financial liability and is accounted for in accordance with IPSAS 28, Financial Instruments: Presentation, the derecognition requirements in IPSAS 29, Financial Instruments: Recognition and Measurement, and IPSAS 30, Financial Instruments: Disclosures, except as required by IPSAS 32.

Grant of a right to the operator model

The government compensates the operator for the construction, development, acquisition, or upgrade of a service concession asset by granting the operator the right to earn revenue from third-party users of the service concession asset or another revenue-generating asset.

The transaction is an exchange transaction involving dissimilar assets (a service concession asset for the government and an intangible asset for the operator) that gives rise to revenue for the government.

However, as the service concession arrangement covers a period of time, the government does not recognize the revenue immediately.

The government recognizes a liability for any portion of the revenue that is not yet earned.

E. Treatment of Revenues and Expenses

Financial liability model

Payments to the operator are allocated and accounted for according to their substance as a reduction in the liability, a finance charge, and charges for services provided by the operator.

If the asset and service components of a service concession arrangement are separately identifiable, the amount allocated to each component is determined by reference to their relative fair values.

If they are not, the components are determined using estimation techniques.

The finance charge and charges for services provided by the operator are accounted for as expenses.

Grant of a right to the operator model

The government earns the benefit associated with the assets received in the service concession arrangement in exchange for the right granted to the operator over the period of the arrangement.

A liability is recognized for any portion of the revenue that is not yet earned. Revenue related to the recognition of the service concession asset is recognized according to the economic substance of the service concession arrangement, and the liability is reduced as revenue is recognized.

Appendix VI. Indicative Plan for Implementation of IPSAS

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
1a. Consolidation within class A, between A and B classes and A and C class (Transactions and balances between B and C classes aggregated)	- Identify relevant B and C entities - Inform accountants in agencies and line ministries - Agree method of capturing inter-entity transactions - Train staff who consolidate	- Develop form and content of separate (A entities) and consolidated financial statements - Document procedures for consolidation - Issue instructions to B and C entities to submit financial statements and supplementary information for 2014 by March 31, 2015; also other information requirements (e.g., for quarterly reporting) - Consolidate balance sheet as at January 1, 2014	- Prepare first trial consolidated financial statements for 2014 including notes according to IPSAS - Issue instructions to B and C entities to submit financial statements and supplementary information for 2014 by March 31, 2016	-		Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
1b. Consolidation within class A, between A and B classes, A and C classes, and B and C classes			- Refine and improve accounting policies, processes, and data quality and completeness based on experience and comments of INAO	- Prepare second trial consolidated financial statements for 2015 including notes		Fjársýsla
1c. Consolidation within class A, between A and B classes, A and C classes, and B and C classes				- Refine and improve accounting policies, processes, and data quality and completeness based on experience and comments of INAO	- Prepare official consolidated financial statements for 2016 including notes and submit for audit	Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
2a. Land and buildings, roads and other infrastructure, other equipment (OBL effective 1.1 2015)	- Review quality and completeness of data in registers - Review existing valuation policies - Prepare technical requirements for Oracle - Specify useful lives for assets other than land - Establish cost or values - Impairment test	- Adapt Oracle asset module - Data transfer to Oracle (recording assets as both assets and expense in two parallel systems) - Prepare template for notes - Complete identification, recording, and valuation of any missing items	- Prepare information for IPSAS financial statements for 2014 - Calculate estimated depreciation for budget 2016 and future years, based on investment plans	- Refine and improve data for financial statements and estimates for budget and future years	-Record assets and related transactions in official system -Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla, Real Estate Agency, Road Administrative Agency
2b. Finance and operating leases	- Identify and review leases and classify as finance or operating leases - Prepare technical requirements for Oracle	- Adapt Oracle in a parallel system - Data transfer to Oracle - Prepare template for notes - Register in the system	- Prepare information for IPSAS statement for 2014 - Calculate amortization, depreciation for budget 2016 and subsequent years	- Refine and improve data for financial statements and estimates for budget and future years	- Record assets and related transactions in official system - Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
2c. Public-private partnerships	- Identify and review public-private partnerships arrangements - Treat as assets under appropriate categories and liabilities	- Adapt Oracle in a parallel system - Data transfer to Oracle (record transactions as assets) - Prepare of template for notes - Register within the system	- Prepare information for IPSAS statement for 2014 - Calculate depreciations under appropriate asset categories for budget 2016 and future years	- Refine and improve data for financial statements and estimates for budget and future years	- Record assets and related transactions in official system - Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla Statistics Iceland
2d. Software and databases	- Collect and review any available data - Transfer data to Oracle (for available data) - Estimate useful lives	- Adapt Oracle in a parallel system - Transfer data to Oracle (record transactions as assets) - Prepare template for notes - Impairment test	- Prepare information for IPSAS statement for 2014 - Calculate depreciation for budget 2016 and future years	- Refine and improve data for financial statements and estimates for budget and future years	- Record assets and related transactions in official system - Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla
2e. Inventories	- Review available data - In case of significant data gaps, register material inventories	- Adapt Oracle in a parallel system - Data transfer to Oracle (record transactions as assets) - Prepare template for notes	- Prepare information for IPSAS statements for 2014 and for budget 2016 and future years	- Refine and improve data for financial statements and estimates for budget and future years	- Record assets and related transactions in official system -Refine financial statements and estimates for budget and future years	Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
2f. Accounting for associates	- Identify relevant entities - Develop methodology for equity accounting - Continue to account for associates at cost in separate financial statements of class A entities	- Identify missing entities - Include associates on equity basis in consolidated balance sheet as at January 1, 2014	- Include associates in first trial consolidated financial statements for 2014 including notes - Refine and improve accounting policies, processes, and data quality and completeness of associates based on experience and comments of INAO	- Include associates in second trial consolidated financial statements for 2015 including notes - Refine and improve accounting policies, processes, and data quality and completeness of associates based on experience and comments of INAO	- Include associates official consolidated financial statements for 2016 including notes and submit for audit	Fjársýsla
3a. Pension liabilities	- Specify accounting policy and new methodology for calculation - Recalculate according to new methodology	- Data transfer to Oracle - Record transactions as assets - Prepare template for notes	- Prepare information for IPSAS financial statements for 2014 - Prepare estimates for budget 2016 and future years	- Refine and improve data for financial statements and estimates for budget and future years	-Record revised liabilities and related transactions in official system - Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
3b. Other provisions	- Identify need for other provisions (e.g. leave entitlements, guarantees) - Analyze circumstances - Develop methodology	- Prepare template for notes - Recognize in opening balance sheet	- Improve methodologies - Supplement with additional material provisions not identified in opening balance sheet - Prepare input for budget 2016	- Refine and improve data for financial statements and estimates for budget and future years	-Record revised liabilities and related transactions in official system -Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla
3c. Contingent liabilities	- Review completeness and quality of existing data	- Review probability of payments related to guarantees and other contingent liabilities, and if payments are probable, estimate provisions	- Recognize provisions as estimated - Revise presentation and disclose all contingent liabilities as a separate note, not as part of equity	- Continue to recognize and disclose according to IPSAS 19		Fjársýsla
3d. Commitments	- Review completeness and quality of existing data		-Revise presentation and disclose significant commitments as a separate note, not as part of equity	- Continue to disclose as a separate note, not as part of equity		Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
4a. Financial assets and debt	- Categorization of financial assets according to IPSAS 28 - Analysis of arrangements - Develop accounting policy - Prepare revaluation - Analyze new requirements in the LIBRA debt management system	- Develop accounting policy - Prepare revaluation - Analyze new requirements in the LIBRA debt management system - Prepare template for notes	- Prepare information for IPSAS financial statements for 2014 - Prepare estimates for budget 2016 and future years	- Refine and improve data for financial statements and estimates for budget and future years - Prepare input for budget 2016	-Record revised assets and liabilities and related transactions in official system - Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla, Central Bank
4b. Receivables and doubtful debts	- Analyze receivables to identify doubtful items - Revaluate receivables	- Prepare template for notes	- Prepare information for IPSAS financial statements for 2014 - Prepare estimates for budget 2016 and future years	- Refine and improve data for financial statements and estimates for budget and future years - Prepare input for budget 2016	-Record revised assets and provisions and related transactions in official system - Refine and improve data for financial statements and estimates for budget and future years	Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
5a. Presentation of financial statements		- Develop template for revised statements - Develop statement of changes in net assets/equity - Develop template for direct method cash flow statement - Implement necessary IT-changes	- Use revised presentation for 2016 budget - Use revised budget for IPSAS 2014 financial statements	- Refine and improve presentation	- Prepare official IPSAS financial statements using new presentation	Fjársýsla
5b. Harmonized presentation of budget and accounts		- Develop common template for budget and ex-post operating statement, showing net lending/borrowings and operating result - Review other needs for harmonization	- Prepare 2016 budget using harmonized presentation - Prepare trial financial statement for 2014 using harmonized presentation	- Prepare 2017 budget using harmonized presentation - Prepare trial financial statement for 2015 using harmonized presentation	- Prepare official IPSAS financial statements using harmonized presentation and compare budget and actual	Statistics Iceland, Ministry of Finance, Fjársýsla

Action	Phase I Jan – June 2014	Phase II July – Dec 2014	Phase II/Phase III 2015	Phase IV 2016	Phase V 2017	Responsible Agency
6a. Audit		- review and comment on trial balance sheet as at January 1, 2014	- Review and report on first trial IPSAS financial statements for 2014	- Review and report on second trial IPSAS financial statements for 2014	- Audit official financial statements for 2016 and issue formal audit opinion and recommendations for improvements	INAO