

# Issues on Public Sector Accounting Reform in Jordan

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This study reviews recent articles discussing the benefits of International Public Sector Accounting Standards (IPSAS) implementation in reforming public sector accounting, specifically in developing countries. These benefits are among others better transparency, accountability, and decision making in public sector financial transactions. The purpose of this study is to examine the role of IPSAS in addressing some critical financial issues, including financial aids, budget deficit, taxes, and corruption, which may hinder the progress of Jordanian public sector and the country's economic growth. This study concludes that IPSAS has an effective role in addressing these thorny issues and its implementation would therefore allow the Jordanian public sector to reach its development goals. The unique contribution of this study is that it enriches the body of knowledge regarding the benefits of IPSAS implementation in a more holistic manner and in a new context, Jordan.

*Keywords:* budget deficit, corruption, financial aids, IPSAS, Jordan, taxes

## Introduction

As a developing Middle Eastern country, Jordan is marred by poor economic development and limited sources of income, depending primarily on international financial aids (Abushamsieh, López-Hernández, & Ortiz-Rodríguez, 2014). Though faced with a very challenging regional environment, Jordan has been progressing within the past few years in terms of fiscal strength and external positions. But critical challenges remain a part of Jordan's economy. These include low economic growth, high unemployment, high level of public debt, budget deficit, and current account deficit (Jordanian Ministry of Finance [JMOF], 2016). In addition, the presentation of public sector accounting information in Jordan remains an issue. Jordanian public sector reports its accounting information based on "Accounting principles and practices, and Budget Law No. 39/1962) issued by the Ministry of Finance in 1994". This Law guides many practices to ensure the events (incomes and outcomes) of public sector budgets (Abushamsieh, 2014). However, Jordanian public sector needs to adopt more effective standards to enhance accounting information transparency due to its high reliance on international financial aids and tax revenues (Ouda, 2016). The accounting information of Jordanian public sector is also weak compared to other Middle Eastern countries such as Kuwait, Saudi Arabia, and Bahrain. These countries are rich in natural resources, allowing them to develop their public sectors services independently without the need of international aids (Brautigam, Fjeldstad, & Moore, 2008). Thus, one of the recommendations for Jordanian public sector is to seriously consider the implementation of the International

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Public Sector Accounting Standards (IPSAS) in order to standardize and improve accounting information as well as to reform the public sector (Ouda, 2016).

In recent years, the International Arab Society of Certified Accountants (IASCA), located in Amman, Jordan, has exerted its efforts to generalize the experience of other countries in the implementation of the IPSAS to Jordan, where it has conducted many courses and seminars regarding the implementation of these standards and to promote the benefits that Jordan will receive from applying these standards to the country's public sector (IASCA, 2014). As a part of Jordan's Fiscal Reform Project, the JMOF, the entity responsible for the implementation of IPSAS in Jordan, has officially endorsed the adoption and implementation of IPSAS in 2015. A five-year implementation road map was put in place, with implementation assistance coming from the United States Agency for International Development (USAID). The five-year plan is expected to entail a gradual transformation from cash accounting to accrual accounting (IFAC, 2016; Alghizzawi & Masruki, 2019a) aimed at to be completed by year 2021 (Alghizzawi & Masruki, 2019b). This step is aimed at improving the quality of financial reports and the transparency of government financial accounts. In addition, it is expected to enhance control and accountability as well as simplify the decision-making process in a timely manner and an optimal use of financial resources (JMOF, 2015).

Many studies have described the benefits of IPSAS implementation. Obara and Nangih (2017) revealed that the implementation of IPSAS in Nigeria results in financial transparency and accountability, strengthened internal controls, improved financial and resource stewardship, and increased efficiency in decision making and good governance in Nigeria. Similarly, Brusca, Gómez-villegas, and Montesinos (2016) found that IPSAS improves the transparency, accountability, decision making, and quality of accounting information in Colombia and Peru. Opanyi (2016) discovered that IPSAS provides better quality financial reports compared to the traditional reports of Kenyan ministries. Biancone and Secinaro (2015) concluded that accounting information under IPSAS has many advantages over other financial reports (e.g. Generally Accepted Accounting Principles (GAAP) and traditional reports) in non-profit companies in Italy. IPSAS governs and presents more details of economic entities than other standards. Therefore, the transparency and accountability of accounting information can be enhanced using IPSAS. In the context of the Middle East, Alshujairi (2014) found that the implementation of IPSAS is critical in order to improve the transparency, quality of accounting system, and accountability of the Iraqi public sector.

Importantly, the implementation of IPSAS is driven by the need to find appropriate solutions for the financial problems that hinder the work of public sectors. In reality, as it is apparent from the New Zealand experience, the economic crisis was the main financial problem behind the economic and public sector reform. However, unlike New Zealand, globalization, financial crisis and scandal, corruption, and fraud are/were the main driving forces for the public sector reform in some countries such as USA, UK, and Spain (Ouda, 2004). Moreover, Godfrey, Sophal, Kato, Piseth, Dorina, Saravy, Savora, and Sovannarith (2002) added another driving force, which is the impact of international organizations such as International Monetary Fund (IMF), World Bank (WB), and other aid donors. These organizations require public sector reform as a *sine qua non* of assistance. This can be seen particularly in underdeveloped and transitional economies. Thus, the awareness about these financial problems (driving forces) will speed up the process of transition to IPSAS (Azmi & Mohamed, 2014).

This study is motivated by the dearth of literature pertaining to the implementation of IPSAS in developing countries, especially those in the Middle East like Jordan, and the lack of empirical studies on the benefit of

IPSAS implementation in Jordan. Moreover, the abovementioned studies that conclude the benefits of IPSAS (transparency, accountability, and better decision making) provide no clear argument on how the implementation of IPSAS can be employed to address financial problems in the public sector. Therefore, this gap encouraged the authors to explain the current financial issues in Jordanian public sector and how the implementation of IPSAS could address them.

### Literature Review

Over the recent years, a number of governments around the world have moved from traditional cash accounting to full accrual accounting as part of public sector accounting reform, while many others are moving toward this direction (OECD/IFAC, 2017). The main reason for this switch is to enable more effective and efficient fiscal management (Irvine, 2011). According to Cavanagh, Flynn, and Moretti (2016), from the governments' point of view regarding transparency, accountability, and integrity, accrual accounting offers a number of significant benefits over traditional cash accounting, such as: (1) it provides a comprehensive scene of the cost of government activities and financial and government performance; (2) increases the concentration of decision makers in governments and making them more capable to manage assets and liabilities effectively; (3) provides a more complete picture of governments financial position as a whole; and (4) improves the reliability and integrity of government financial data. Figure 1 next shows the countries that have fully implemented accrual accounting and a number of countries that are in moving towards the full implementation.

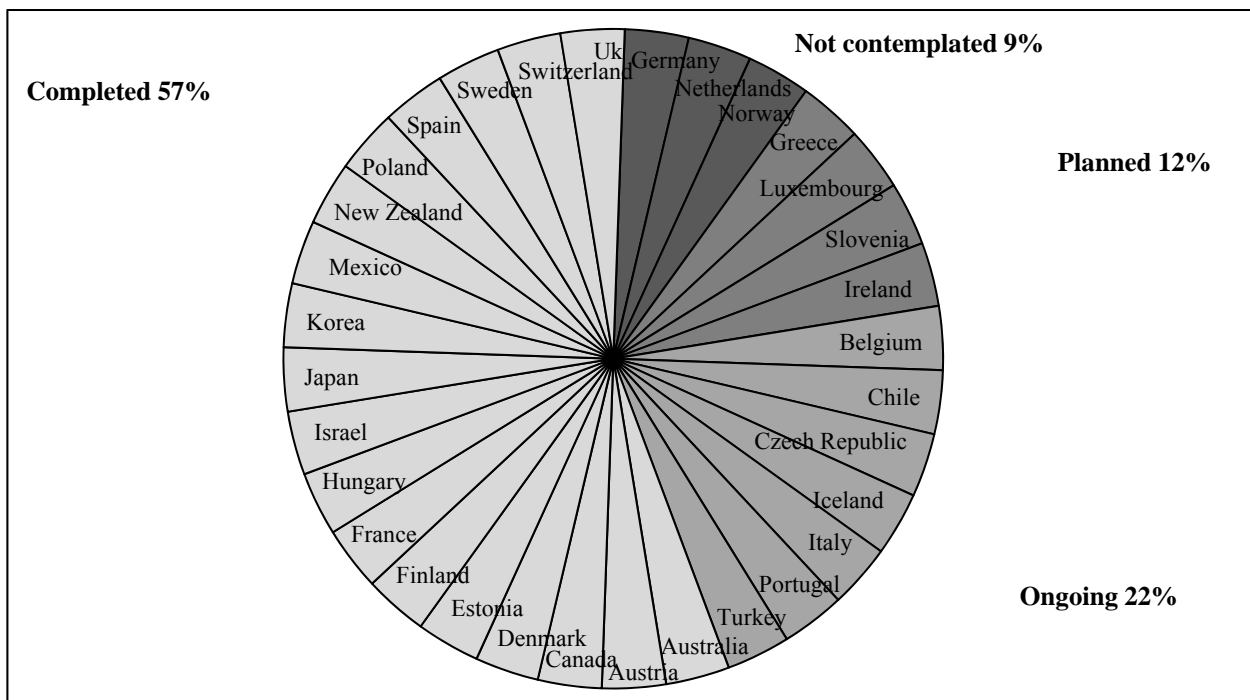


Figure 1. OECD countries: Status of accrual reform. Source: OECD (2017); Accruals survey.

Accrual accounting records accounting transactions and activities when they arise (i.e. not when cash is paid), hence the accounting records are documented in the financial statement depending on the period in which they need to be received or paid (IFAC, 2008, p. 3233). Meanwhile, cash accounting documents accounting transactions and activities based on immediately received or paid cash (IFAC, 2008, p. 926). According to

Hepworth (2003) and Sour (2012), accrual accounting is more suitable for governments than cash accounting. Most government transactions are accomplished based on accrual accounting and they are not paid immediately. For example, if a government rents a building, the transaction is recorded in the accounting report, but the payment will be made later e.g. end of year. Thus, the fundamental justification for the change from cash to accrual accounting system by governments is the drawbacks of cash accounting. Cash accounting fails to recognize future commitments, guarantees and other contingent liabilities (Ball, Dale, William, & Sacco, 1999). Table 1 shows the difference between the two methods in terms of financial statement preparation in governments.

Table 1

*Cash Accounting VS Accrual Accounting*

Method	Balance sheet		Operating statement			Institutions
	Assets	Liabilities	Revenues	Expenses	Other flows	
Cash accounting	Cash balances	Bank overdrafts debt	Cash receipts	Cash payments	None	Budgetary central government
Accrual accounting	Fixed and intangible assets Inventories Tax receivables	Monetary financial instruments	Accrued receivables	Depreciation	Valuation changes in nonfinancial assets	Public sector

Source: Cavanagh et al., 2016.

For these reasons, the International Federation of Accountants (IFAC) began to urge governments around the world to move towards accrual accounting. And for this purpose, IFAC released IPSAS and called for the provision of high-quality government accounting reports at the end of the year in order to promote transparency, accountability, and decision making (Christiaens, Reyniers, & Rollé, 2010). According to Masruki, Hussainey, and Aly (2018), the implementation of IPSAS by the public sector promotes significant qualitative characteristics in terms of financial information disclosure, such as relevance, faithful representation, understandability, comparability, and timeliness. IPSAS mainly focuses on accrual accounting rather than cash accounting. The final version of IPSAS consists of one standard for cash accounting and 40 standards for accrual accounting (IFAC, 2018). Chan (2006) mentioned that IPSAS tends to be adopted by developing countries that have weak economies, taking into consideration that the majority of the developed countries (strong economies) have accounting standards that are either comparable to or more rigorous than IPSAS. Even if their accounting standards are not equivalent to IPSAS, the strong economies are under less pressure to adopt it.

### **The Need of IPSAS Implementation in Jordan**

#### **Financial Aid**

Countries in the Middle East such as Jordan still have weak economic development and are reliant on foreign aid (Abushamsieh et al., 2014; Oliorilanto, 2008). The international financial aids are important to Jordan due to its limited economic resources. Other countries e.g. Kuwait, Saudi Arabia, Bahrain, and Qatar have rich resources, such as gas and oil, which allow them to develop their public sectors services independently without the need of international financial aids (Brautigam et al., 2008). Table 2 presents the amount of international development aids received by Jordan in 2010 (Abushamsieh et al., 2014; Klugman, 2011).

Jordan has received a large amount of aids (\$955.41 Millions) and its human capital development ranking

is low (95). Therefore, international aids are important to enhance the development of Jordanian public sector. However, regarding Jordan's financial situation and its dependency on international aids, the public sector should present adequate quality and amount of accounting information for international agencies such as WB and IMF to assure that the provided international aids are allocated effectively to develop the services of the public sector (Ouda, 2016; Abushamsieh, 2014). Therefore, the implementation of IPSAS will create the avenue to provide the needed accounting information since the primary objective of IPSAS is to present clear and comprehensive accounting information (transparency) about the financial operations of the public sector.

Table 2

*Indicators for the Official Development Aid (ODA) of Jordan*

Indicator	Jordan
Human development index ranking (2011)	95
ODA received in 2010 (\$ millions)	\$955.41
GDP (2010) (\$ millions)	\$27,454

Source: Abushamsieh et al., 2014; Klugman, 2011.

**Budget Deficit**

One of the main financial problems in Jordan is budget deficit, which means that the expenses of the public sector exceed its revenues. According to Trading Economics (2019a), Jordan recorded a government budget deficit equal to 2.40% of the country's Gross Domestic Product (GDP) in 2018. The budget balance averaged -1.22 % of GDP from 1990 until 2018, reaching an all-time high of 10.11% of GDP in 1992 and a record low of -8.90% of GDP in 2009. Figure 2 represents Jordan government budget in terms of budget deficit over the years of 2007-2018.



Figure 1. Jordan government budget. Source: Trading-Economics; Central Bank of Jordan.

IPSAS implementation will improve the quality of governmental decision-making for various activities (Oulasvirta, 2014). Government budgets should be managed and allocated effectively to achieve the highest possible performance of overall services provided by the public sector in the country. A budget in public sector accounting is a plan that shows how government plans its spending. This requires accurate decisions of how to manage the allocated budgets in the right way. IPSAS implementation would reduce the ambiguity of accounting information and consequently improve financial decisions. This in turn will reduce the budget

deficit in Jordanian public sector.

### Taxes

One of the main revenues in Jordan is taxes collected from its citizens in order to develop the services of the public sector, which is considered as one of the axioms in response to reducing the budget deficit in the country. OECD (2013) showed that tax revenue in Jordan represented 33% of GDP. According to Doing Business Project [DBP] (2020), which is supported by the WB, the taxes in Jordan are high compared to other countries in the Middle East. Table 3 presents the type and amount of taxes in Jordan in 2020 (DBP, 2020).

Table 3

#### *Taxes Types and Amount in Jordan in the Year 2020*

Tax type	Statutory tax rate	Tax base	Total tax rate (% of profit)
Social security contribution on employee	7.5%	Gross salaries and any amount paid as a fixed monthly amount	8.46 (not included)
Social security contribution	14.25%	Gross salaries and any amount paid as a fixed monthly amount	16.07
Corporate income tax	14%	Taxable income	10.48
Property transfer tax	4%	Estimated property value	1.21
Property tax	10%	Assessed annual rental value	0.45
Vehicle tax	Fixed fee (JOD 500)	-----	0.24
Tax on interest	5%	Interest income	0.13
Municipal business tax	Fixed fee (JOD 200)	-----	0.10
GST (VAT)	16%	Value added	0.00
Stamp duty	0.3% to 0.6%	Contract value	0.00
Fuel tax	-----	-----	0.00
Totals	-----	-----	28.6

\* This information was collected as part of the *Doing Business Project (DBP)*, which measures and compares regulations relevant to the life cycle of a small- to medium-sized domestic business in 190 economies.

It could be concluded that, the citizens and companies in Jordan pay high taxes (e.g. GST is 16% on all services). Thus, the Jordan's citizens or taxpayers considered as one from the main sources to support the public services development. This highlights the importance of using a rigorous reform project such as IPSAS implementation in order to provide transparent accounting information for taxpayers in order to enhance trust between citizens and the government that taxes paid is properly allocated to support public services in the country to activate the accountability.

### Corruption

Another issue necessitating IPSAS implementation in Jordan is corruption. According to Siame (2002), "as a result of a lack of accountability and transparency on the part of public integrity systems, corruption in developing countries is reportedly higher and more severe than it is in developed countries" (p. 7). Tanjeh (2016) stated that corruption steps in to understate the government's revenue and assets or to overstate government's expenses and liabilities. As reported by Rasheed (2017) on Jordan, corruption is a serious problem in Jordan and the government must address it as soon as possible. Table 4 shows Jordan's ranking in terms of corruption over the period of 2007-2015.

Nweze (2013) observed that the proper implementation of IPSAS would reduce cases of financial resources manipulation in the public sector, since one of the main objectives of IPSAS is to engender

transparency and accountability in the operations of public entities. Full and proper implementation of IPSAS paves way for Related Party Disclosure which by extension checks cases of corruption through effective, efficient, and transparent financial reporting in the public sector (Khan et al., 2014). Considering the fact that corruption is a threat to government legitimacy and authority and reduces the amount of public money available to fund public services, the implementation of IPSAS is a giant step in the global fight against government corruption (Chan, 2006). Thus, the implementation of IPSAS will play an important role in the fight against corruption in Jordanian public sector, which will lead to a positive impact on the Jordanian economy.

Table 4

*Jordan's Corruption Perception Rank*

Year	2007	2008	2009	2010	2011	2012	2013	2014	2015
Countries under rating	180	180	180	178	183	176	177	175	168
Grade	47	51	50	47	45	48	45	49	53
Rank	53	47	49	50	56	58	66	55	45

Source: Rasheed, 2017.

## Theoretical Perspective

### Agency Theory

According to the agency theory, an “agency relationship” refers to a contractual agreement that involves the appointment of another party (denoted as the agent) with the capacity to make certain decisions by an individual or organization (denoted as the principal) to deliver the stipulated services in the benefit of the principal (Jensen & Meckling, 1972). A public organization is typically autonomous and often involves various relationships between the principal and the agent with respect to the agency theory (Lane, 2003). The conflict of interest between the management and stakeholders adversely affects the quality of financial reporting.

The dissimilar interests and knowledge of the public and private sectors in a country, especially in a relationship between the principal (e.g., the owner of an organization) and the agent (e.g., the manager) (Donaldson & Davis, 1991; Guangdi & Fulwood, 2013), with respect to this theory, inevitably result in an “agency dilemma” or in other words problems of steering the agent to operate in the interest of the principal (Lucian & Jesse, 2004). On a similar note, the public (taxpayers) is regarded as the principal, who is entitled to the public resources, in this exclusive relationship with the government (uses the tax revenue) as the agent, who is expected to serve the public interest. However, certain appointed individuals in an inequitable government may only act based on their own interest instead of the public interest. They may be involved in fraudulent cases, such as offensive tax proposals or uncontrolled expenditures, resulting in financial predicaments, such as national debt crisis (Guangdi & Fulwood, 2013). In this case, the answerability and openness of how the government manages these financial resources are deemed obligatory to the public.

After all, the government is trusted by the public with the capacity to manage the limited resources in the public interest, which justifies the significance of authentic and conclusive financial reporting from the government, as the agent, to the public, as the principal. In return, the government is remunerated with allowance, bonus, and salary. Meanwhile, the unauthorized agents of the government mainly operate for their personal interest. Hence, it is imperative that the principal considers a financial information system (Kathleen, 1989) that requires revised or restructured public sector accounting system or practice to deliver authentic and conclusive financial reporting. With that, the public is adequately informed about their efficiency and the

effectiveness of their services.

Consequently, the agency theory used in this study explains the relationship between the government of Jordan (agent) and holders of interests (principals) in the management of such public resources as: (1) Donors who provide financial aids to Jordan in order to develop the public services; (2) Who have an interest in reducing budget deficit; (2) Taxpayers who pay the taxes for the public services; (3) Who have an interest in reducing corruption. IPSAS implementation aims at disclosing financial information that is useful for evaluating the financial position of the country as a whole and at the departmental level, as well as its financial performance, in a manner that facilitates the enhancement of the value of its usefulness for the purpose of supporting accountability and decision-making. Thus, the government of Jordan is concerned with the implementation of IPSAS in order to provide a full and clear presentation about its financial operations to prove that the financial aids and taxes are allocated effectively for the development of Jordanian public sector. In addition, its implementation holds the government of Jordan accountable for their financial decisions and therefore reduces corruption cases within the public sector, which in turn will increase the trust between the principals and the agent. Moreover, the IPSAS system will enable the government of Jordan to manage its budget effectively and hence reduce the budget deficit.

### **Conclusions and Suggested Future Work**

Based on the Agency Theory, the present study addresses the benefits of IPSAS implementation on public sector accounting reform in the context of Jordan. Specifically, its implementation may be useful to remedy several financial issues in the country, which include the dependency on financial aids and taxes, budget deficit, and corruption. These issues play significant roles in Jordan's economic growth and legitimacy of its public sector. It has been demonstrated in this study that Jordan has been unable to address these financial issues. More precisely, the accounting system of Jordanian public sector has not been able to address these critical issues. Thus, the implementation of the IPSAS system by the public sector will produce more transparent information, promote government accountability, and encourage better and more comprehensive decision-making process.

The unique contribution of this study is that it enriches the body of knowledge regarding the benefits of IPSAS implementation in a more holistic manner and in a new context. This is currently very limited. Thus, this study is expected to be beneficial to such various parties as the decision-makers, public sector accountants, JMOF, and Jordanian public sector. In terms of theory, the present study contributes significantly to Jensen and Meckling (1972) agency theory by employing it to explain the necessity of IPSAS for better public sector accounting reform in a new context, Jordan.

However, this study has at least two limitations. First, it is not conducted based on empirical evidence. Future research may test the role of IPSAS implementation in addressing the abovementioned financial issues empirically. Second, the financial issues may not be generalized to the public sectors of other countries because they may face different issues altogether. Therefore, future research should consider the financial issues in the country under study. Moreover, in the context of Jordan, future research may address the role of IPSAS implementation on the credit rating of Jordan, considering that Jordan's credit rating is fluctuating and sometimes even negative (Trading Economics, 2019b).



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