The Switch: Cash to Accrual Accounting

Interview with the immediate former Public Sector Accounting Standards Board (PSASB) CEO Fredrick Riaga (23rd Nov 2023)

Four very critical observation become certain once you interact with FCPA Fredrick Riaga. One, He is a stickler for time, two; He's very impatient and, he's not as young as one would think; his words not ours and lastly; if the adage, the clothe maketh a man is to be true, Riaga gives meaning to this.

Fredrick Riaga is a man on a mission; to help transition the country from the cash to accrual accounting. A difficult task by any measure, but one which he relishes. Mr Riaga is the immediate former Chief Executive Officer of the Public Sector Accounting Standards Board, a government agency mandated to prescribe and promote adoption of financial reporting, internal auditing, and risk management standards in the public sector.

Fredrick Riaga began his career at NIC bank (Now NCBA) as a cashier in 2003. He says he was lucky and fortunate to land a job just a week after leaving campus. Jim, a she calls him, was his first Boss at the Bank, A man who Riaga speaks fondly of, reminiscing on his indelible impact that helped shape his professional career.

"He was a leader. A transformative leader for that matter. One thing then which he also made known to us, he told us, guys, we are here to make money and we do anything so that we make the money.

So if you are a cashier and you see an opportunity that you can help me make money for the shareholders, make it. Then seek approval later on". Riaga says.

A change in leadership at NIC saw Jim leave the Company. According to Riaga, a change in leadership after the exit of Jim changed the 'culture 'of the bank. This sudden shift gave him the conviction that it was time to seek new challenges elsewhere.

" I get impatient pretty fast , Jim left and they brought us a new MD, the general culture kind of changed , I got bored , I got bored because I was doing cashiering, cashiering with a bit of enhancement in terms of the quality of the job, but I still got bored. So I left."

They say when an opportunity presents itself, don't be afraid to go after it, Riaga found himself in the Academia

"My friend joined the University of Nairobi and he informed me that once I enrolled into the university then, one would get 60% discount on the fees". He enrolled in the University for his masters, while at the same time working at the institution, eventually graduating in 2008. He immediately left the University for PricewaterhouseCoopers (PWC) working for two years before his University Lecturer back at UoN, who happened to be the chairperson of the Institute of Certified Public Accountants of Kenya (ICPAK), recruited him to lead the Public Policy Department at ICPAK.

One can deduce that Riaga's Journey to lead the Public Sector Accounting Standards Board may have commenced from his decision to ditch the private sector for Public Service at ICPAK. But it wasn't as straightforward as it seems, he unsuccessfully applied and interviewed twice for the Chief Executive officer role. The third time was however different, he told no one except his wife.

"No, for this job I did not speak. I only spoke to my wife. I told her, "By the way there is a job I'm going to apply for." and she told me," Okay let's go for it". And I applied. With this affirmation, Riaga began his leadership journey at the Public Sector Accounting Standards Board.

Transition from Cash to Accrual Accounting.

Since the adoption of International Public Sector Accounting Standards (IPSAS) and the subsequent application of the same, transitioning to accrual accounting is now a key PFM reform target spearheaded by the National treasury and the Public Sector Accounting Standards Board. Accrual accounting requires revenues and expenditures to be recorded in the financial statements when they are earned and incurred respectively, while Cash accounting is a method that requires transactions to be recorded only when a cash flow has occurred.

The main difference between them lies in the timing of when revenue and expenses are recognized. The cash method is a more immediate recognition of revenue and expenses, while the accrual method focuses on anticipated revenues and expenditures.

We sat down for an in-depth discussion with the PSASB CEO Fredrick Riaga, to learn more about this transition and why it matters for sustainable public finance management.

Tell us what is accrual accounting from a simplified perspective?

I would define accrual accounting as a basis of reporting that a mama mboga who wakes up in the morning, goes to Marikiti, and on this particular day, she finds herself with less cash. she has to pick the same volume of supplies for her grocery store back in the estate. So she picks stock worth Ksh. 3000 shillings, but she only has Ksh. 2000 shillings.

Now she has created an expectation worth Ksh. 3000 bob. But she can only fund that expectation up to Ksh. 2000. Now accrual accounting therefore implies that this mama mboga has created an expectation of Ksh. 3000. So she's then booking her cost of sales not at Ksh. 2000 shillings which she has paid, but at the Ksh. 3000

So accrual accounting is essentially the basis of comprehensive accounting that captures the transactions in its totality.

Now when she goes back to sell. She sells her stock for a figure of Ksh. 4500. Accrual accounting would then compel her not to recognize that she has 2500 bob because, remember she has only spent 2000 shillings, but to only recognize that she has made ksh.1500.

That is accrual accounting in a simplified manner.

Why is it important for the country to make this transition?

The distinction between cash accounting and accrual accounting is purely on the comprehensiveness of one against the limitations of the other.

In the public sector, accrual accounting helps us manage asset management risks. When the new Constitution came into bear, we were transitioning from local authorities to Counties, In some conversations, you did hear that a local authority had just bought a set of vehicles, but because it is not recorded anywhere, the exiting local councilors just drove them off when their term ended, because there was no record of it. So there are risks attendant to asset management that is not addressed well under cash accounting, which accrual accounting would help us deal with.

Remember the story I gave about this mama mboga, with accrual accounting, the mama mboga has an elaborate system to make future decisions. She has Ksh. 4500 bob in sales, but because she has knowledge of Ksh.1000 bob that is pending, she is then able to project into the future. Assuming that she has made a decision to close her business, so then she would only be spending the Ksh. 3500 knowing that Ksh. 1000 is not hers but is owned by somebody else or to somebody. So consequently, the significant differences between cash accounting and accrual accounting, cash accounting looks at today, accrual accounting looks into the future,

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What role will PSASB play in this transition from cash to Accrual?

Yes, a very good question. The law mandates PSASB to set frameworks that would guide financial reporting. The process must be guided by: one, international best practice, point number two, ability of the public sector to adopt.

Now when you look at the international best practices, the only available set of international best practices is the accrual based reporting standard. Under that very performance objective, As a board , we had to ask ourselves, how do we plug into the international ecosystem informing financial reporting to the public sector and around that, consequently , IPSAS comes around as the major player .

The Board has now adopted International Public Sector Accounting Standards as the basis of reporting. And within the confines of IPSAS reporting framework, accrual accounting is at the core.

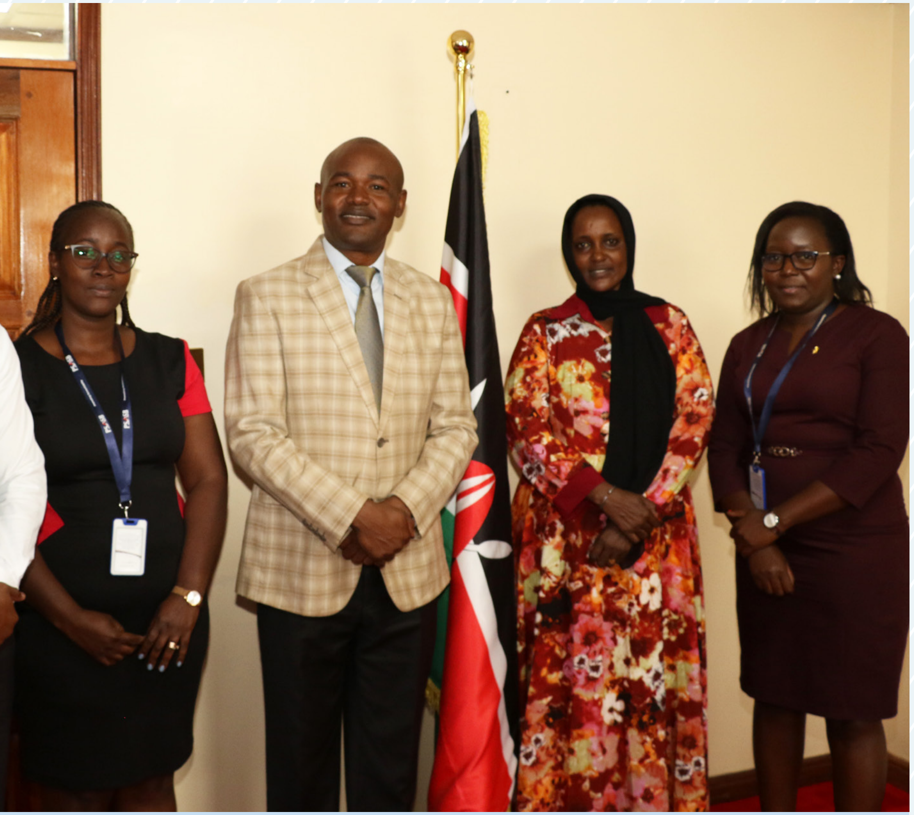
So beyond the benefits that we have then described, we are also plugging within the international landscape where accounting and accrual basis is now the current norm.

What other critical players will be involved in this transition?

In delivering any project, you cannot go single-handedly. You must create teams, create collaborations, you must establish who the stakeholders are.

The transition to accrual accounting is a major project, it touches everybody. It's going to consume significant resources.

Financial reporting is a shared responsibility, there are roles that are played by the National Treasury, the Accountant General's department. There are



FCPA Fredrick Riaga (Centre), the immediate former Chief Executive Officer of the Public Sector Accounting Standards Board (PSASB) with PSASB staff: Linda Njeru (right), Stephanie Dida (second right), Mercylyne Opiyo (second left). With them is the Communications Specialist, Oliver Mwenda, from the Public Financial Management Reforms Secretariat.

roles that are played by the Controller of Budget.

The roles played by the Auditor General might come at the very tail end of the transition but they are still critical roles that will inform the general financial reporting landscape that we adopt as a country.

Some of the critical stakeholders that we then must, work with is now the National Treasury, and more so the Accountant General's department. The office of the Auditor General, Office of Controller of Budget, the reporting accountants themselves.

When you move now to the counties, you're talking about the County Executive committee, the County Executive Committee Member for Finance, the audit committees and internal auditors, they will be critical stakeholders that we've got to work with in driving this agenda through.

Finally, Parliament, as the ultimate oversight institution, is a critical stakeholder that we must engage with because: one, they will avail the resources to fund this process and two, they are the principle consumers of the ultimate financial reports that are generated out of accrual based system.

What are the crucial steps involved in this transition?

We started off with scoping the project and we have been through that. Getting to know the volume of work that we have to deliver. We have mapped out various stakeholders identifying the key roles to be played by each agency. The board has approved a road map, within that road map, we have identified some critical steps.

IFMIS has been identified as a critical system that would need to be relooked and reconfigured. You may be aware that IFMIS is originally configured to anticipate accrual accounting. There is need for us to reconstruct and align it to accrual accounting so there are steps around that currently underway at the National Treasury, Department of IFMIS is working closely to ensure that happens.

What are some of the risks you anticipate during this transition period?

Risk management becomes crucial in ensuring a successful delivery of this project. One of the critical risks that one would come across will emanate from a fiscal policy point of view. There are more pressing and more urgent issues that would consume resources. Remember I've said the full transition is fairly expensive. So, it's then competing with other more pressing funding needs.

Then, point number 2, there exists massive expectation gaps. I've just defined one. From a technical point of view, we are clear that the benefits are massive but we must as well convince the political side of the benefit of this transition. The political buy-in remains critical.

Fortunately, we are now getting the right leadership, or the right focus from the leadership at the National Treasury, the PS is really focused, Parliament is now focused. So, the political support is yet another risk that we must then bring in.

The other risk will emanated in regards to technical capacity of Finance officers in Government institutions. In Kenya accountants train on the basis of accrual. When you're certified, you go through CPA, all the examinations are based on accrual, then they come into the markets they settle back to cash accounting and everybody does not want to think of accrual accounting, so capacity challenges becomes yet another risk that we must think of.

What timeline do you think as a country, we are looking at in terms of complete transition? Are you looking at one term? Are you looking at five years? Are you looking at 10 years? Are you looking at two years? What would be your ideal timeline if all that matters remain constant?

I will break that question into two. One, and there is the bit that is non-discretionary. What does the standard provide for? We've got a standard called IPSAS, IPSAS 33. First time adoption of accrual standards - accrual-based standards.

It provides that at the point you take the decision, then you have a transition period of three years. So, at the point at which a decision is taken, that as a country, we're moving into accrual accounting. You have three years to prepare fully

Consequently, like when you go back to the road map, we've also anticipated that, yet it will take us three years and now to create an expectation. Remember, I've emphasized on the dangers of setting expectations of accrual based financial statements. That is what the standards provides. But practically, is it achievable? I will tell you no. There are jurisdictions that went ahead of us.

Empirical evidence suggest that a country is able to fine tune accrual-based financial reporting between periods of eight to 10 years of trials. But I'm not saying that as Kenya, we cannot achieve a paradigm shift, so that we are able to achieve this transition within five years. Remember what we said, if we have the right resources and the political will, we are going to achieve this.

Which countries have made successful transitions that we , as a country , can learn from ?

There have been quite a number of countries that have gone IPSAS accrual. Let me start with the outliers. The best performers. New Zealand.

New Zealand has actually achieved a feat that no region has. A government that reports on the same basis as the private sector. They apply international financial reporting standards that apply to the private sector. They have perfected it, but it took quite a bit of time.

Moving closer home, the likes of Malaysia have done a fairly good job in terms of doing accrual accounting. Singapore are on accrual accounting. You move to Europe, EU is on accrual accounting. The US, they're not on IPSAS but they've created their own sets of standards. Like now Europe are not on IPSAS but they have EPSAS (European Public Sector Accounting Standards), that are accrual based and which are for universal application by all European or government agents within the EU.

Coming closer now to this region, the saddest part is Kenya is the biggest economy but we are lagging behind in this reform agenda. Rwanda is ahead of us, Uganda is ahead of us, Tanzania is ahead of us. So that means we are only ahead of Burundi, South Sudan and now DRC and Somalia.

We're not doing very well compared to the countries I have mentioned. So, we don't have to go very far to New Zealand. New Zealand is an outlier. I think if we did move around, went to Rwanda, Tanzania, Uganda we will manage to consume local based practices. What is shocking is that the Rwandan case which is, Rwanda is ahead of the east. It is fast. What is shocking is that Rwanda was helped by Kenyans. It was the Kenyans who help them establish the accrual based reporting system and they took ownership of it.

Lastly, why should this transition matter to PFM stakeholders?

I will give a very simplistic answer. A former Permanent Secretary in the previous administration was quizzed on how many vehicles the Ministry owned. Unfortunately, He could not give a definitive answer to this question. So assuming this PS, as the accounting officer, receives a request to purchase 100 vehicles. Would he know whether there is need for the 100 vehicles or 20 vehicles? He wouldn't. And if he would, is there a justifying need for 100 vehicles because those vehicles consume resources.

Accrual accounting would have enabled him to just have a look at the request; inquire from his officials on the exact number of vehicles in the ministry? How many of them are in usable form? How many are not in usable form? Then he would then tell these guys;you want 100 vehicles but from my records , I see that with a 1/5 of this budget you have allocated for the 100 vehicles, we can recondition the vehicles that we have and put them into use, save these resources for a more pressing need. So from that point of view, I think accrual accounting is the silver bullet to smart and future based decision making for government officers to avoid unnecessary wastage.

Career advice

In my personal opinion, I would recommend that somebody starts in the private sector then land in the public sector. In the public sector, I would say there is just about 25% of people who are committed and they're doing their job as expected. But there is a 75% that kind of messes up the image of the public sector. Because one will need to deal with

PFMRS Communications Specialist (Left) Oliver Mwenda, FCPA Fredrick Riaga (Right), the immediate former Chief Executive Officer of the Public Sector Accounting Standards Board

the 75%, the anchoring under the private sector would be good foundation.

On Parental influence

There are two things that have left an indelible mark on my personal and professional growth as far as the influence my parents had on me.

I mention my mother, she sacrificed everything to see us through with our education.

For my dad, my dad once told us when he was ailing, he is now deceased, he called us and said, "my sons, unfortunately, I am not leaving you with much. Some parents would bequeath their children quite a bit, in terms of earthly possessions. But there is one thing that I'm leaving you with, that if you use it well , it will open doors anywhere.'

'And that is the name Riaka. I have lived a life of integrity.'

My father was, you know, those councilors wa kitambo, So one time we asked him, 'how comes you don't even get a single plot?' He said, 'you know every single thing that I got people would come crying and I would give them out. I would give them and I would give them. So, I have created a name that would open doors for you.'

And truth to this, that name has opened doors for some of us. You're in a fix and you mention that my name is Riaka. 'Oh so and so?' Mara moja the thing is then signed.

So that taught me the value of a name and I aspire that I will do everything that I can to bequeath my children a credible character, a credible name that will open doors for them.

I think that was profound from my father.

Before he died he told us 'guys, you may not know, he apologized before he died. That I must apologies before I die, that I'm going to put you guys in a lot of trouble'

And he indeed put us in a lot of trouble because of this business of forgetting himself and giving out. A friend of mine, the current cabinet secretary in charge of Sports and youth Affairs Hon. Ababu Namwamba, told me that he had never witnessed a funeral as big as my dad's.

It is the name that he bequeathed us, which is the name and the values that came with that that I hold dear to.

On family

The wife that I got married to has also been you know you chase you chase, then one day you just say okay this one looks to be a good mate. Let me stick with this one. She has proved to be at the center of every success. Of course, God first. Then you have people that God works through to help support me as we scale the ladder of leadership in this country. The woman that you get married to will determine how ratchet you're going to be or how happy you want to be. And I thank God that He sent me a good woman.

On his upbringing

Unfortunately, the observation that you have made, because our parents often sacrifice quite a bit and we are forgotten them through these discussions. But there are two things, about my mom. She sacrificed everything to see us through education. For my dad, my dad once told us when he was ailing, he is now deceased he then called us and said, my sons, unfortunately, I am not leaving you with much. Some parents would bequeath their children quite a bit, in terms of earthly possessions. But there is one thing that I'm leaving you with, that if you roe t it will open doors anywhere. And that is the name Riaka. I have lived a life of integrity. My father was you know those councillors wa kitambo, before the county councils that would then... if you talked of Nyeri county council, then it would take care of up to Kiambu. He was in those realms. So one time we asked him, how comes you don't even get a single plot? He said, you know every single thing that I got people would come crying and I would give them out. I would give them and I would give them. So, I have created a name that would open doors for you. And truth to this is that that name has opened doors for some of us. You're in a fix and you mention that my name is Riaka. 'Oh so and so?' Mara moja the thing is then signed. So the value of a name and I aspire that I will do everything that I can. That I will bequeath my children a credible character. A credible name that will open doors for them. I think that was profound from my father. Before he died he told us guys, you may not know, he apologised before he died. That I must apologies before I die, that I'm going to put you guys in a lot of trouble. And indeed he put us in a lot of trouble because of this business of forgetting himself and giving out. A friend of mine, Ababu Namwamba told me that he had never witnessed a funeral as big as my dad's. It is the name that he bequeathed us, which is the name and the values that came with that that I hold dear to.