

Financial Information on the States of Mexico and Inflation a Reference to the Case of Baja California Surⁱ

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Abstract

The international government accounting system has required Mexico's federal government to change the way it presents accountability information. Government accounting standards impose the obligation to recognize the effects of inflation on financial information. The purpose of this study is to assess the efficacy of preparing financial information on the accounting basis of accumulation or accrual, in financial statements presented in currencies of legal tender within inflationary contexts that entail a significant loss of purchasing power of that currency. This paper studies the accounting records presented by the government of Baja California Sur, and finds that the financial and budget information provided by agencies of the centralized state government and state-owned enterprises do not conform to international and national financial reporting standards regarding the recognition of inflation in those financial statements.

Keywords: Government accounting, restated financial information, public administration, inflation

1. Introduction

Inflationary crises in many countries during the 1990s revealed that governments' accounting and budget (fiscal) positions were lacking, given the abrupt deterioration of standards that had previously allowed governments to engage in practices that tended to obscure the true state of their finances. In response, the International Monetary Fund proposed creating a global architecture of transparency standards, preparing a code of good fiscal transparency practices that clearly defined duties and responsibilities under a legal, regulatory and administrative framework established for public finance management, obliging governments to be clear and transparent in rendering their accounts.

According to the International Federation of Accountants (IFAC)ⁱⁱ International Public Sector Accounting Standards Board (IPSASB), government assets and liabilities should be managed on the basis of explicit legal standards and within an accounting system that provides a reliable basis for tracking revenues, commitments, payments, assets and liabilities (IFAC, 2008). Financial and budget information should indicate the accounting method used, following accepted accounting standards (IMF, 2007b).

Having defined governmental accounting (IMF, 2012) as the set of concepts, standards, rules and systems used to generate financial information contained in government financial statements, for publishing and disclosing the state of public finances to citizens, and prepared in accordance with accounting standards, the IMF provides guidance on codes and guidelines for governments and urges them to improve the transparency of their financial information for international, regional and national accountability.

On this order of ideas, and considering that there are three levels of government in Mexico with the authority to both levy taxes and expend public funds, there is a clear need to prepare consistent financial information that reveals the reality of government finances. To this end, Mexico's Ministry of Finance and Public Credit (SHCP) and Ministry of Public Function have worked to establish standards for recognizing the effects of inflation on financial information.

The Mexican Financial Reporting Standards Board (CINIF) issued Financial Standard B-10 “Inflation Effects,” which sets rules for recognizing the effects of inflation on financial information. The Ministry of Finance also issued standards for state-owned and centralized government agencies to apply to their financial statements in order to reflect inflation effects, in keeping with national and international accounting standards (SHCP, 2012), which facilitates the comparability of government accounts. The financial statements of any government agency that produce information in the currency of an inflationary economy should be presented in terms of a constant unit of measure as of the date of their presentation.

Mexico’s process of accounting harmonizationⁱⁱⁱ involved a restructuring and homogenization of accounting standards and procedures for accounting registry, for the purpose of accountability. Authors such as Olais (2013) point out that a registry of the transactions and financial information generated by government accounting systems under specific applicable standards, with the expectation of aligning all public sector assets, obligations and equity under a single accounting system based on accounting standards, is useful for complying with transparency and accountability obligations.

Government financial information standards should be applied at the federal, state and government agency level, and represent a substantial advance toward transparency and accountability (IPSASB, 2000). More work must still be done on their application, however, because budget information, particularly the recognition of inflation effects on that information, still requires more and better efforts in the areas of transparency and accountability.

2. Accounting Theory as the Foundation of Governmental Accounting

Accounting is considered by various authors (Panario and Farfán, 2012) as an applied social science that focuses on how and why things are done. Governmental accounting standards have their origins in the general theory of accountability (Mejía, 1981) which can explain all economic transactions by government entities, and which in turn gives rise to entity theory, which can be applied to social accounting by governments, companies or both. The essence of accounting theory lies in the standard, and it is therefore descriptive, because it prescribes what must be done and how to do it. The theory is used to “evaluate current practices” ... and “may be used to develop new procedures.” Accounting theory also “attempts to explain current practice or rationalize the use of certain procedures” (Hendriksen, 1970), a theory useful as a model for transparency and accountability.

The interests of financial information users involve specific, socially beneficial purposes, whose ultimate purpose is to facilitate decision-making. Along this order of ideas, accounting standards are the foundation for financial analysis and involve inductive reasoning that incorporates “the formulation of general or specific objectives of financial reporting; a statement of postulates of the social, economic, political environment in which accounting operates [...] and finally, the application of principles to specific situations and the development of procedural rules.” (Hendriksen, 1970).

The financial reports of government agencies are designed according to the needs of the users of that information (Mejía, 1981), which follow specific and precise objectives. Government assets should be used to optimize budget and financial resources for the benefit of society, and to best distribute their benefits.

To account for the government’s functions and activities, Mejía (1981) applies command theory, which is applicable to major corporations. He also uses fund theory, which can be applied to any set of assets dedicated to specific purpose, producing objective information. Command reports stress the responsibility of the administrator. “The concept of fund is associated with the concept of money. [...], denotes a separation of resources for use toward a specific given purpose, usually for settling a debt” (p. 27), for example. Fund theory uses eight types of funds, classified into “three groups: a) government funds; b) proprietary funds; and c) trust funds; and two account groups: fixed assets and long-term debt” (p. 25). The definition of the funds does not nor cannot be applied to all government agencies; it depends on the many variables in the concept of current account and capital expenditure.

3. Accounting Standards as Governmental Accounting Principles

Governmental accounting standards are also established in Statement No. 14, by the Government Accounting Standards Board (GASB, 1994, paragraph 9), “The Financial Reporting Entity,” describing how the other components of the government apparatus should be integrated into the primary governmental sector. The central system (government ministries and administrative governmental organizations) and other government entities like hospitals, schools and universities, should be added to the primary sector.

Mexican standards use international models “with an accrual basis, harmonized accounting and issuing bodies” supervised by public government organizations (Zárate, 2013) that create governmental financial standards for the purpose of harmonizing accountancy for all three orders of government (Esquivel, 2013). This means, as some authors have pointed out (López, 2013), that government financial information should incorporate at least a minimum of standardized elements in order to ensure a harmonization of its standards, and thus to guarantee that the accounting system is grounded in concepts that permit governments to provide financial information on similar public entities in real time.

According to this conceptual framework, the most appropriate way to prepare financial information is on an accrual basis, meaning accounting for income or expenditure transactions as of the date they are effected, and regardless of the date of collection or payment (Mancilla, 2014); accounting for revenue when it is effectively realized and/or the corresponding assets recorded when there is a legal right to collect them, in other words, as of the moment the taxes or fees are levied (*Postulados Básicos de Contabilidad Gubernamental*, 2009). It is also best to financially recognize all quantifiable transactions or changes in equity by government entities on an accumulated basis. The focus on accrual enables administrators of public funds and users of financial information to better estimate the economic impact of government fiscal policy by recognizing the change in the ownership of goods and services actually rendered.

Expense transactions should be entered on the accounting records according to the date the expenditure is formalized, which is the moment, in accounting terms, at which a payment obligation to another party is recognized for the receipt of goods, services or contracted public works, as well as the obligations stemming from the laws, treaties, decrees, resolutions and binding sentences, regardless of their payment; revenue transactions should be entered on the accounting records when they are effectively formalized and/or recorded within the corresponding assets, when the legal right exists to collect the taxes, fees, products, and usage of the public entities (*Postulados Básicos de Contabilidad Gubernamental*, 2009).

Central governmental and state-controlled entities must introduce an accounting data system that permits the harmonious, well-defined and specific registry of budget and financial transactions relating to public administration, revenues and expenditures, so that the accounting system can generate reliable, prompt, understandable and comparable information for all users of that information, and which is consistent with the budget information (Olais, 2013). This information should be prepared based on the conceptual framework, so that it can be interpreted by the users of that information. The reconciliation of budget and financial information, presented in constant pesos, should be based on budget records, i.e., the execution of revenue and the exercise of expenditure in public entities, in order to reflect the impact on equity including the effect of inflation on the accounting information. “Budget accounting, like equity accounting, should follow the methodology of balancing statements, with transactions represented through budget ledger account that reflect the execution of revenue and exercise of expenditure; as well as their effect on the financial position and on results” (*Postulados Básicos de Contabilidad Gubernamental*, 2009).

Federal and state government agencies should present information about their financial situation and changes in equity to the public financial and fiscal authorities (Article 45 of the General Law on Governmental Accounting), and their financial information should recognize the effects of inflation and indicators of their fiscal standing, investment programs and projects (Domínguez, 2013).

The established standards oblige government entities to prepare their financial and budget statements on the accounting basis of accumulation and accrual, and also to recognize the effects of inflation. According to international standards (IFAC, 2011), any entity that prepares and presents its financial statements on the accrual basis of accounting must apply the standard to its primary financial statements, including the consolidated financial statements of any entity that prepares its information a hyperinflationary economy, in accordance with International Public Sector Accounting Standard 10 (IPSAS 10); the results of operations and financial position are not useful unless they are restated. In an inflationary economy, financial statements are only useful when expressed in terms of constant units of measure. Information must not be presented without restatement (SHCP, 2012), and this includes budget information.

In an inflationary climate, central accounting areas must recognize the effects of inflation on the financial statements by applying the comprehensive method to determine monetary and non-monetary entries, and the impact on their purchasing power (IFAC, 2011).

The most common assets of a government entity are cash, government funding instruments, accounts receivable, contractor advances (in cases in which goods and services have not been received, in given amounts and characteristics, and for which purchase-sale prices have not been guaranteed). The most common monetary liabilities are bank loans, accounts payable to suppliers, wages and salaries payable, taxes payable, advances from clients (on the same principle as contractor advances). In the case of a cost or expense derived from a non-monetary asset, the base figure must include all the restatement effects (CINIF 2014)^{iv} established in the financial information.

4. Study Methodology

The inductive exploratory method was applied, in an interpretative-descriptive frame of reference (Alvarez, 2003), to the financial information of central and government-controlled administrative entities of Mexico's thirty-two states (including Mexico City, the Federal District). Each of the states was reviewed in consideration of its municipal geographic distribution and the financial information it prepares, in order to choose a non-probabilistic unit of analysis, which would be the state with the fewest municipalities, in order to more precisely review the restated financial and budget information.

Tabla 1: Municipalities by State

State	No. municipalities	State	No. municipalities	State	No.
Aguascalientes	11	Baja California	5	Baja California Sur	5
Campeche	11	Chiapas	118	Chihuahua	67
Coahuila	38	Colima	10	Mexico City	16
Durango	39	Guanajuato	46	Guerrero	81
Hidalgo	84	Jalisco	126	Mexico	125
Michoacán	113	Morelos	33	Nayarit	20
Nuevo León	51	Oaxaca	570	Puebla	217
Querétaro	18	Quintana Roo	19	San Luis Potosí	58
Sinaloa	18	Sonora	72	Tabasco	17
Tamaulipas	43	Tlaxcala	60	Veracruz	212
Yucatán	106	Zacatecas	58		

Source: <http://www.municipios.mx/>

Search date: November 18, 2013

The purpose of this study is to examine the financial information prepared by the central and government-controlled administrative entities of the state government of Baja California Sur, based on the central hypothesis that the state of Baja California Sur and its central and government-controlled administrative entities report financial and budget information with recognition of inflation effects, in other words, restated. The design of the research was adapted to the collection of data for analysis, in a transactional study of a non-probabilistic sample (Hernández, 2006). We reviewed the financial and budget information for fiscal year 2013, and the accompanying notes to the financial information, which were prepared under the framework of governmental accounting. The purpose of studying the financial information was to determine whether the central and government-controlled administrative entities of the state government were reporting financial and budget information in restated terms, in compliance with the transparency and accountability principles established in the Law on Government Accounting.

5. Results

The central and government-controlled administrative entities of the state government consist of the Executive branch (governor's office), General Secretary of Government, Secretary of Tourism, Secretary of Health, Secretary of Urban Planning and Infrastructure, Secretary of Economic Promotion and Development, The State Treasury Office, Secretary of Fishing and Fisheries, Secretary of Public Education, Secretary of Finance, State Civil Registrar's Office, State Attorney General's Office, Office of Integral Family Development.

Secretary of Labor and Social Planning. It also includes the Under Secretary of Public Security, the State Water Commission, the State Electoral Institute, the Institute for Transparency and Access to Public Information. We revised the budget and financial information for each of these entities, including the Income Statement; Statement of Changes in Public Finance; Statement of Changes in Financial Position; and the notes to the financial statements of the state government and other agencies and entities of the state government whose information is made public. Our findings indicate that the central and government-controlled administrative entities of the state government do not publish financial information as established in the applicable standards, in other words, recognizing the effect of inflation on the financial statements. The financial and budget information published as of the months of September and November 2013 is presented at historic values. There were also cases in which no financial information was available, such as the judicial branch, which is not report any financial information at all. The following table shows the degree of compliance with standards on the preparation of financial and budget information in restated terms, for the central and government-controlled administrative entities of the state government. We found that only the Ministry of Finance prepares financial and budget information, but it is not restated.

Table 2: Accounting Information Basis: Government Accounting Law Year 2013

	Statement of financial position	Statement of public finance results	Statement of changes in financial situation	State of changes to equity	Note to the financial statements	Budget information	Restated financial statements
Judicial branch	ND	ND	ND	ND	ND	ND	ND
Legislative Branch	N	X	N	N	N	N	ND
Secretary of Tourism	N	N	N	N	N	N	ND
Secretary of Health	X	X	N	N	N	X	ND
Secretary of Urban Planning and Infrastructure	ND	ND	ND	ND	N	ND	ND
Secretary of Economic Promotion and Development	ND	ND	ND	ND	N	ND	ND
State Treasury Office	N	N	N	N	N	ND	ND
Secretary of Fishing and Fisheries	N	N	N	N	N	N	ND
Secretary of Public Education	N	N	N	N	N	N	ND
Secretary of Finance	S	S	S	S	S	S	ND
State Government Clerks Office	X	X	X	X	X	X	ND
State Civil Registrar's Office	ND	ND	ND	ND	ND	ND	ND
Office of Integral Family Development,	ND	ND	ND	ND	ND	ND	ND
Secretary of Labor and Social Planning							
Under Secretary of Public Security	X	X	X	X	ND	ND	ND
State Water Commission	X	X	X	X	N	N	ND
State Electoral Institute	X	X	X	X	X	N	ND
Institute for Transparency and Access to Public Information (1)							

Source: In-house calculations based on information published on the official websites of the state public administration. Article 51, General Law on Government Accounting.

Y: published

N: not published

X: financial information published late

N/D: not available

(1): Publishes information, but difficult to understand because information is insufficient and/or too general.

Note: The financial information was recovered in January 2014. The budget information was recovered in April 2014.

Despite the obligations imposed by the Law on Government Accounting, the General Government Financial Information Standard for State-Controlled Entities NIFGG SP 04 (SHCP, 2012) and NIFG 010, Recognition of Inflation in Financial Statements (SHCP, 2011), the central and government-controlled administrative entities of the state government of the State of Baja California Sur do not publish restated financial and budget information, so we were unable to prove this hypothesis.

6. Final Considerations

Empirical investigation in accounting sciences seeks the significant relationships between the use of public funding and the decisions made by government and legislative agencies. It is unlikely that the empirical studies can provide a complete platform for finding variables that may be related to and at the same time based on accounting theory, in fact, empirical investigation can only be used to test the theoretical hypotheses.

From the focus of government standards, financial and budget information prepared on the accrual basis of accounting, in combination with the recognition of inflation's effects on financial statements (restated financial information) enables an entity to show the annual results of public resources. It also presents the government's financial resources as well as its obligations; the net state debt; and its non-financial assets. It also takes into account cash flow, investments in fixed assets or financial instruments and obligations in constant pesos. In other words, restatement recognizes the effect of inflation on monetary and non-monetary items, the result of which reflects purchasing power as of the closing date of the financial information.

With fund theory and command theory, which are descriptive in nature, notes to the financial statements and budget information should provide information on the matters determined by the budget laws themselves, which must comply with the objectives proposed in the governments' development plan. These actions are expected by citizens and users of financial information; by investors, public finance analysts, and high-level officials interested in the correct distribution of public resources.

It is essential that government agencies concatenate their financial and budget information presented in historic values with the recognition of inflation in the financial statements, to create a homogeneous accounting system that is functional with economic activity, and obviously, for transparency and accountability proposed as a good practice by the International Monetary Fund.

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7.1 Legislation

- "Political Constitution of the United Mexican States", *Official Gazette*, Mexico, February 5, 1917, Wednesday April 13, 2011, latest reform, first section, p. 1.
- "General Law of Government Accounting", *Official Gazette*, Mexico, December 31, 2008, first section, n/p. New Law. Saturday December 31, 2011, first section, p. 36-50, latest reform.
- "Basic Law of Public Administration for the State of Baja California Sur", *Official Gazette from the Government of the State of Baja California Sur*, July 14, 2005.
- "Agreement for Issuing the Government Accounting Manual", *Official Gazette*, Mexico, November 22, 2010, second section, n/p.
- "Agreement for Issuing the Basic Postulates of Government Accounting", *Official Gazette*, Mexico, Thursday August 20, 2009, first section, n/p.

7.2 Web Resources

<http://www.conac.gob.mx/>

<http://secfin.bcs.gob.mx/finanzas/index.php>

<http://www.oficialiamayorbcs.gob.mx/>

<http://contraloria.bcs.gob.mx/>

<http://www.saludbcs.gob.mx/>

<http://lapmedia.mx/sepesca/>

<http://www.sspbcs.gob.mx/ssp/>

<http://www.sepbcs.gob.mx/index.php>

<http://www.spyde.bcs.gob.mx/>

<http://secturbcs.gob.mx/>

<http://www.difbcs.gob.mx/v2/index.php>

<http://cea.bcs.gob.mx/>

<http://www.pgjbcs.gob.mx/>

<http://www.ieebcs.org.mx/noticias/noticia.php>

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<https://spc.conanp.gob.mx/capacitacion/nociones/index.htm>

<http://www.gasb.org/st/summary/gstsm14.html>

http://imt.mx/images/files/SPC/Curso%20Nociones/contenidos/modulo1/mod_1_1.htm

End Notes

ⁱ This study is part of an institutional research project by Universidad La Salle Registry number CA01215, Comparative study of government accounting.

ⁱⁱ The IPSASB is an independent standards issuing committee within the IFAC that focuses on the accounting and financial information needs of national, regional and local governments, related government organizations, and the territories they serve.

ⁱⁱⁱ The General Law on Government Accounting establishes the general criteria on government accounting and the preparation of financial information by public entities, in order to properly standardize the information. It is mandatory for the federal executive, legislative and judicial branches, state governments and Mexico City; municipal governments; political/administrative agencies of the territorial divisions of Mexico City; state-controlled government agencies, whether federal, state or municipal, and federal and state autonomous organizations. State governments must coordinate with the municipalities so that they could harmonize their accounting based on the provisions of this Law, and the government of Mexico City with its political-administrative divisions.

^{iv} Restatement is the method by which inflation effects are recognized in basic financial statements as a whole, or, when applicable, as an individual entry.