Public Governance Directorate
Senior Budget Officials

Financial Reporting in the Faroe Islands

Benchmarking of the accounting and financial reporting framework against the OECD Recommendation of the Council on Budgetary Governance
Faroe Islands

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1. Introduction

The OECD Benchmarking of the accounting and financial reporting framework of the Faroe Islands was conducted at the request of the Faroese Government. The aim of this work is to assist the Faroese Government in assessing the strengths and weaknesses of its framework against the relevant principles of the OECD Recommendation of the Council on Budgetary Governance\(^1\) and to provide recommendations to address any gap.

In requiring this work, the Faroese Government recognises the relationship between good accounting and financial reporting and better public governance. Reliable, comprehensive and timely accounting data allows for external stakeholders, including the Parliament, citizens and investors, to understand and monitor the full range of the Government financial operations. As noted in a recent OECD study, a sound accounting and financial reporting has both direct benefits in terms of transparency and indirect benefits in terms of confidence in the reliability of the Government fiscal policy formulation and implementation.\(^2\)

The findings and recommendations of this benchmark build on the experience and knowledge of good practices acquired by the Budgeting and Public Expenditures Division of the OECD Directorate for Public Governance over past decades through the meetings and workings of its Senior Budget Officials Working Party and Network of Financial Management and Reporting Officials.

This note was written by Delphine Moretti, Senior Policy Analyst in the Public Management and Budgeting division within the Public Governance directorate of the OECD, following two missions in Tórshavn in December 2019 and February 2020. Interviews were held with key stakeholders of the Faroese fiscal reporting ecosystem: representatives from the Government, including agencies, funds and municipalities; the Parliament; Economic Council; Statistics Office and Auditor General.

The OECD would like to thank the Faroese stakeholders, in particular Bjarni Askham Bjarnason and Leif Abrahamsen, for their availability and openness to recommendations.

2. Institutional, economic and fiscal context

The Faroe Islands are an autonomous and self-governing nation under Danish sovereignty since 1948. They are a parliamentary democracy, with the Faroese Government holding executive power on all matters except police, defence and foreign affairs. The Parliament (Løgting) comprises 33 members that serve a four-year term. Following legislative elections, the incumbent Prime Minister (Logmaður) is generally given the initiative to establish a new coalition by the Faroese Parliament and becomes the head of the Government unless a majority of the Parliament demands a new political leader.

The Faroe Islands are an archipelago of 18 islands, and one of which is not inhabited. They are one of the smallest countries of the world, with around fifty thousand inhabitants. Administratively, the islands are divided into 29 municipalities (kommunar) within which there are 120 or so settlements. Around 22,000 (40%) of the country’s inhabitants are based in the larger municipality, Tórshavn, the country’s capital.

Fluctuation in GDP per capita in the Faroe Islands are primarily a function of the performance of the salmon farming industry, which accounts for around 80% of the exports of goods and services. This makes the economy highly dependent on fish stocks, fish prices,


oil prices and exchange rates. Recently, however, successive governments have actively promoted the broadening of the economic base by developing other economic activities, including tourism.

The Faroe Islands have historically had a GDP per capita close to the OECD average, but with considerable fluctuations in performance over time. In particular, the country suffered a significant fiscal, financial and economic crises in the early 1990s, due to declining fish stocks and prices. Due to defaults on private borrowing, a large stock of government guarantees were called and public spending increased, leading to a sovereign-debt crisis.

In the wake of the 1990s crisis, ambitious fiscal reforms were rolled out to prevent any future solvency or sustainability problem. In particular, the process for the issuance of government guarantees was strengthened and the State required to hold at any point in time liquidities (cash, bonds or shares) equivalent to about 15% of the GDP.

Another striking feature of the Faroese economy is the large public sector, which is responsible for around 35% of employment, plays a key role in delivering welfare as well as developing infrastructure and provides both public and commercial services to the population.

Figure 1 describes the composition of the Faroe Islands’ public sector according to statistical concepts. The budgetary central government comprises the Prime Minister Office and the ministries. Administratively independent agencies and authorities implement certain State policies (e.g. the road and building agency, Landsverk) and funds have been set up to manage revenue or assets in relation to certain sectors or activities (e.g. the farmers fund, Búnahargrunnurin or Unemployment Fund). In addition, public institutions deliver a range of public services, such as hospitals or schools.

Within the central government, the social security sector comprises funds that deliver universal social benefits. The benefits are funded by contributions paid by all citizens along their income tax. General government comprises the Municipalities, which are administratively fully independent from the central government. They collaborate together to deliver elderly care, the main local public service, through so-called municipalities collaborative entities.

Finally, both ministries and municipalities own shares in enterprises (state-owned enterprise, or SOEs) created under public or private law and delivering commercial services (e.g. Faroese Telecom, Vágar Airport, Atlantic Airways and the Faroese Post) or building infrastructure such as undersea tunnels (e.g. Norðoya Tunnilin, Vága Tunnilin and Eystur og Sandoyartunlar).

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3https://www.oecd.org/governance/regional-policy/oecdterritorialreviewsnoraregionthefaroeislandsgreenlandicelandandcoastalnorway.htm

Figure 1. Faroe Islands: Composition of public sector according to GFSM concepts

<table>
<thead>
<tr>
<th>Public Sector</th>
<th>General Government</th>
<th>Central Government</th>
<th>Local Government</th>
<th>Enterprises</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>State-owned (8)</td>
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<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Municipalities-owned (3)</td>
</tr>
<tr>
<td>PM Office</td>
<td></td>
<td>Fund for occupational diseases (1)</td>
<td>Municipalities (29)</td>
<td></td>
</tr>
<tr>
<td>Ministries (7)</td>
<td></td>
<td>Labour market supplementary pension fund (1)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Agencies and authorities (27)</td>
<td></td>
<td>Unemployment fund (1)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Institutions (71)</td>
<td></td>
<td>Other fund (1)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Funds (7)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: The classification of public entities above uses the concepts of the Government Finance Statistics (GFS) Manual. It however differs from the classification currently used by Statistics Faroe Islands, which comprises an additional sector and classifies two institutions as state-owned enterprises due to their commercial activities.

Source: OECD, based on information from Gjaldstovan.

In recent years, the Faroese economy has experienced a period of significant growth due to higher fish quotas and prices, as well as buoyant salmon farming. Consequently, since 2016, the State experienced fiscal surpluses between 2 to 2.5% of GDP. These surpluses have been used to reduce the State debt and fund additional public spending (excluding SOEs), which reached 47.7 percent of GDP in 2017.

Public investment has been particularly dynamic (Figure 2). In 2018, for the whole of the public sector, it totaled kr. 3 billion (approx. 15 per cent of GDP), with half of the investment done in central and local government (e.g. hospitals) and the other half done by publicly owned corporations (e.g. undersea tunnels). As some of the most significant investment projects are only in their preliminary stages, investment is likely to remain a significant part of public sector spending in coming years.

3. Accounting and Financial Reporting Framework

For the State, broad principles for financial management, accounting and financial reporting are laid out in the three laws: the Law on the State budget, Law on State Accounts, Law on the audit of the State Accounts (Table 1). The legislation does not define the accounting basis to be used for the accounts (cash or accrual), but requires that loans and grants that have not been paid to third-parties at the end of the fiscal year shall be reported as liabilities in the accounts.

In addition, importantly, the legislation requires that the State budget and accounts be aligned and specifies their institutional scope. The Law on State Accounts lays out an important principle, which is that the State accounting and financial reporting rules should be applied by all public entities that receive funding from the State, in any form (e.g. earmarked revenue, loan and transfer or capital contribution).

However, the legislation authorises exceptions to that general principle and some large funds established prior to 1994 have not yet acknowledged this requirement in their legal statutes. Therefore, as can be seen on Figure 3, in practice, the institutional coverage of the State Accounts is close to the statistical concept of central government as shown in Figure 1, but not fully similar. In addition, municipalities, which receive transfers from the State budget, have remained outside of the State Accounts.

To prepare the State Accounts, any intra-governmental transactions and balances are reconciled and eliminated and the State Accounts could be considered, in practice, to be consolidated accounts for the central government, with however some limitations detailed in the following section.
Figure 3. Faroe Islands: Institutional coverage of the State Accounts

<table>
<thead>
<tr>
<th>Public Sector</th>
<th>General Government</th>
<th>Enterprises</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central Government</td>
<td>Social Security</td>
<td></td>
</tr>
<tr>
<td>Budgetary Central Government</td>
<td></td>
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</tbody>
</table>

**State accounts**
- PM Office Ministries (7)
- Agencies and authorities (27)
- Institutions (71)
- Funds (4)

**Outside of the State accounts**
- Other funds (3)
- Labour market supplementary pension fund (1)
- Unemployment fund (1)
- Other fund (1)
- Municipalities (29)
- State-owned (8)

Source: OECD Accruals Survey (2016).

The broad principles laid out in legislation are further detailed in Ministerial orders, as follows:

The *Order on State Accounts* requires that entities use a shared chart of accounts. It specifies that expenditures shall be recorded at the delivery stage and liabilities and assets reported in the annual accounts, subject to some exceptions (for example, provisions and infrastructure assets are not mentioned). It does not, however, define the accounting policies to be applied (e.g. depreciation periods for specific categories of assets), which are decided at entity-level;

The *Order on the Submission of Accounts for Transparency, Management and Control* requires that the entities that are not part of the State account submit their financial data monthly to Gjaldstovan. Once a quality control is done, this data is made available on a public website at a fairly detailed level.

The *Law on the Audit of State Accounts* (Table 1) stipulates that the Parliament approves the State Accounts. Within the Parliament, the Audit Committee, comprising four members, reviews the annual State Accounts as well as the accounts of other public entities submitted to Parliament. An independent Auditor General supports the work of the Parliament and more specifically the Audit Committee. It realises the annual audit of the State Accounts, but does not have any responsibility in relation to the annual audit of the accounts for public entities other than the State, which is carried out by accountancy firms.

Concerning municipalities, the *Law on Municipalities* (Table 1), stipulates that they shall follow the rules established by the Ministry of finance for their financial management and reporting. These rules, defined in the *Order on Municipal Accounts*, are largely similar to

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6 *Gjaldstovan* is an authority operating under the auspices of the Ministry of Finance. It is tasked with defining rules and principles for financial management, accounting and financial reporting; preparing the State accounts for; and managing the State accounting and payment systems.
those applying for the State Accounts concerning the chart of accounts, accounting principles and requirement to submit monthly budget execution data. However, according to Gjaldstovan, municipalities’ accounting frameworks have not been fully harmonised yet and small municipalities face serious capacity constraints. Therefore, challenges still exist with the quality of their financial data although their accounts are audited by private audit firms.

Concerning SOEs, private law applies, including the obligation to prepare accounts based on the national accounting standards on accrual basis and to publish their accounts annually along with the audit opinion of their auditor. One the question raised during the OECD visit to the Faroe Islands was whether SOEs, being recipients of State funding (often in the form of issuance of guarantees or capital contributions) should be required to provide their monthly financial data.

Table 1. Faroe Islands: Key legal requirements for accounting and financial reporting

<table>
<thead>
<tr>
<th>Key dispositions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Law on State Budget (2009)</strong></td>
</tr>
<tr>
<td>- Section 3: State budget and accounts shall be aligned.</td>
</tr>
<tr>
<td>- Section 5: State budget should cover all entities whose expenditures are funded by tax or State grants, but exceptions may be granted in other legislation.</td>
</tr>
<tr>
<td>- Section 8: A report is laid out before Parliament alongside the State budget proposal, describing the whole of the public sector finances situation.</td>
</tr>
<tr>
<td>- Section 24: loans and grants that are granted but not paid yet shall be reported as liabilities in the accounts.</td>
</tr>
<tr>
<td><strong>Law on State Accounts (1994)</strong></td>
</tr>
<tr>
<td>- Section 1: State Accounts shall be laid before Parliament by end of May.</td>
</tr>
<tr>
<td>- Section 2: State accounting rules shall be applied by all entities within the State budget/ by entities that receive loans, capital or any other financial support from the State.</td>
</tr>
<tr>
<td>- Section 3: the State defines rules and principles applying to financial management and reporting for all entities within the State budget.</td>
</tr>
<tr>
<td>- Section 5: the rules and principles shall be detailed in a guidance by each entity.</td>
</tr>
<tr>
<td><strong>Law on the Audit of State Accounts (1999)</strong></td>
</tr>
<tr>
<td>- Section 4: The Parliament’s Audit Committee reviews the annual State Accounts and other public entities’ accounts.</td>
</tr>
<tr>
<td>- Section 5: The Auditor General is appointed by the Parliament Presidency and is independent.</td>
</tr>
<tr>
<td>- Section 7: The Auditor General functions’ include the audit of the annual State Accounts and other public entities’ accounts.</td>
</tr>
<tr>
<td>- Section 8: The audits will be procured by the Auditor General, certified auditors and registered auditors.</td>
</tr>
<tr>
<td>- Section 19: The PAC presents to the Parliament a proposed resolution for approval of the State Accounts.</td>
</tr>
<tr>
<td>- Section 45: municipalities should undergo an independent audit of their accounts, to be done by an accountancy firm.</td>
</tr>
<tr>
<td>- Section 47: the minister of finance determines the rules applying to financial management and reporting of municipalities (chart of accounts, bookkeeping, etc.).</td>
</tr>
</tbody>
</table>

Source: OECD, based on information from Gjaldstovan.
4. Benchmarking with international best practices and standards

The benchmarking of the Faroese accounting and financial reporting framework against the three principles of the *OECD Recommendation of the Council on Budgetary Governance* (Annex A) relevant to the present report is presented below. It shows that although the accounting and financial reporting framework has some obvious strengths, significant deviations can be observed in some areas.

**Principle #4: “budget documents [i.e. the budget and accounts] are open, transparent and accessible”**

The framework appears to be compliant with the requirements of principle #4 above, as the State budget and accounts are fully aligned and all entities within general government (Figure 1) is available on a monthly basis on Gjaldstovan’s website.

In addition, the State Accounts are published within 5 months within the end of the fiscal year, as required by legislation and consistent with the *OECD Best Practices for Budget Transparency*.

**Principle #6: “present a comprehensive, accurate and reliable accounts of public finances”**

The requirements of principle #6 are only partially met as of today. Although the accounting and financial reporting framework has been harmonised for the bulk of public entities and the legislation requires that the State Accounts cover all entities receiving State funding, the State Accounts prepared by Gjaldstovan have a limited institutional coverage (Figure 3). The grounds for the exclusion of certain funds from the State Accounts are in addition unclear.

To provide a comprehensive overview of public finances, and although it has no legal obligation and authority to do so, Gjaldstovan is preparing at year-end a set of accounts that aggregates the State Accounts, the individual accounts of those funds that have remained outside of the State Accounts as well as the municipalities’ accounts. It however faces technical difficulties in doing so, and these “aggregated” accounts are not submitted to a financial audit, raising uncertainties over their reliability.

As of today, therefore, the overall financial situation of the general government and public sector is available only in the statistics prepared independently by Statistics Faroe Islands. These statistics are however published with considerable delays, e.g. the 2018 fiscal statistics were published on 30 October 2019.7

Concerning the completeness of the financial operations reported in the accounts, although the *Order on State Accounts* requires that liabilities and assets be registered in the accounts, the accounting policies cannot be said to be fully compliant with generally accepted accrual accounting principles. Financial assets and liabilities are reported, but, as mentioned above, provisions and infrastructure assets are not.

Moreover, accounting rules are not always complied with. The reports of the Auditor General identify, for example, regular and significant problems with the recording of some fixed assets (e.g. land or infrastructure), as well as with the value for certain assets and

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7 In any case, as underlined during the discussions conducted for preparing this note, statistics are not similar to accounts in that they use specific measurement methods and rely significantly on estimates, etc. Therefore, they should not be considered a substitute to consolidated accounts. Rather, it was underlined that harmonised and accurate accounting data would be a prerequisite for more reliable and timely fiscal statistics.
liabilities (e.g. equity shareholdings that are not measured at their present value but at historical cost).

Interviews held within the frame of this benchmark have highlighted that these assets could represent very significant value on the State balance sheet, due to the particular circumstances of the Faroe Islands, where the State owns around a half of the country’s land and holds shares in SOEs delivering large infrastructure programmes.

Compared to OECD countries, the bulk of which report their land, buildings, infrastructure assets, etc., the Faroe Islands can therefore be said to have significant gaps in their balance sheet (Figure 4).

**Figure 4. OECD countries: Reporting of selected assets and liabilities**

![Diagram showing the reporting of selected assets and liabilities in OECD countries.]

Source: OECD Accruals Survey (2016).

**Principle #10: “promote the integrity and quality of (…) budgetary implementation through rigorous quality assurance”**

Concerning external audit, the requirements of principle #10 listed above appear to be met overall. The Auditor General Office is tasked with auditing annually the State Accounts. Legislation or statuses of the other public bodies specify what are the requirements for the annual audit of their accounts, e.g. local governments must have their accounts audited by local audit firms. The Parliament is presented with a summary of all audit opinions by the Audit Committee. However, the lack of centralisation, or at least coordination, of the audit function for public entities may prevent the identification of any potential widespread or general issue or challenge.

**State-Owned Enterprises**

Concerning SOEs, although their accounts are published and audited annually, as noted above, their financial data is not communicated to the Ministry of Finance in-year and no aggregation or consolidation is performed that would inform policy-makers about the total level of their spending and investment, and the resulting aggregated net worth. It is noted, however, that the authorities are currently revising their framework for SOEs, which could allow strengthening reporting requirements over the short-term.
5. OECD Findings and Recommendations

Findings

The Faroe Islands have made very significant steps towards modernising their accounting and financial reporting framework, as shown in the previous section, with the main achievements being i) the reporting of financial assets and liabilities in public entities’ balance sheets; ii) the harmonisation of the frameworks for a large number of public entities and iii) the provision of monthly disaggregated financial data on line. The latter, in particular, is remarkable and not yet achieved in most OECD countries.

Building on these achievements, the Faroe Islands should now consider completing its accounting and financial reporting reforms by bringing its framework fully in line with international best practices and standards. To do so, a number of weaknesses need to be addressed, as described below.

Legislation and orders, despite being revised and improved over the last decade, should be clearer and more rigorous in defining the principles and rules to be applied for accounting and financial reporting. In particular, the legislations and orders allow interpretations as to what should be the institutional coverage of the State Accounts; authorise “exceptions”, which created uncertainties as to whether all funds should comply with its principles; and do not provide accounting rules that are clear and detailed enough to allow for a full harmonisation of accounting principles and rules applied by entities for their book keeping.

Significant assets and liabilities are not reported and/or not measured at their present value. This creates a number of challenges for understanding the financial situation of each entity and for good public management. It is questionable, indeed, whether the liabilities and assets that are not reported in the accounts can be properly monitored and managed.

The State Accounts, the main financial report, provide only a partial view of public finances. A comprehensive overview of the financial situation of the general government, or even the whole of the public sector, would be useful against the background of an increasing share of public spending and investment being undertaken by municipalities and State owned companies.

The limited institutional coverage of the State Accounts and lack of reporting on some significant assets and liabilities limits the understanding and scrutiny by both the Government and Parliament of the extent to which land, loans, guarantees, as well as extra-budgetary spending are used to support certain policies and sectors of the economy and the potential fiscal risks associated with these.

Recommendations

1. **Gjaldstovan** should be granted the responsibility to not only collect but also control the quality of the monthly accounting data transferred by public entities.

2. Public entities should be required to use accrual-basis accounting standards compliant with generally accepted accounting principles and taking into account size and resources constraints in the Faroe Islands' public sector (see following section below).

3. Accounting principles for (all) funds and municipalities should be aligned with those of the State, including by abolishing all exceptions to the principles laid out in the legislation and orders and imposing penalties in case of no compliance.

4. Building on existing informal practices, consolidated financial statements according should be prepared according to clear specifications laid out in an
accounting standard (e.g. statistical concept of general government). These consolidated accounts should be published within 5 months after the end of the year.

5. Requirement for agencies and authorities, institutions and funds to communicate to the Auditor General a copy of the audit opinion on their annual accounts and requirement that the Auditor General realise a financial audit of the consolidated financial statements in accordance with international audit standards.

6. For SOEs, obligation to transfer their accounting data in-year to the Ministry of Finance, in addition to the annual communication of their audited year-end financial statements. Ideally, the Government should prepare an annual report on the financial situation and performance of the state owned companies, as recommended in the *OECD SOE Guidelines*.8

The target financial reporting framework resulting from the above recommendations is presented in Annex B. Should the Government of the Faroe Islands decide to implement these recommendations, they would have been implemented according to a roadmap taking into account the time need for revising the legislation and orders, addressing any technical challenges and building up capacities.

**Which accounting standards for the Faroe Islands?**

The governance and leadership for defining accounting standards will be among the most important tasks to advance the recommendations above. When considering potential institutional models for standards setting, the Faroe Islands will have two main options available.

The **first option would be to establish in the legislation an independent standard setter or advisory body.** OECD countries such as France, Portugal and the United Kingdom (Box 1) have adopted done so using different governance models that could be considered in the Faroe Islands – e.g., accounting standards and policies are established by the government and reviewed by the advisory body (United Kingdom) or the standards setter establishes standards and submits them to government for endorsement (France and Portugal).

Irrespective of the governance model, for safeguarding the standards setter or advisory body’s independence, the standards setter would need a clear legal mandate; appropriate composition of members (e.g. cross section of people comprising academics and representatives of the accounting profession and potentially the user community); and transparency on activities (e.g. due process, activity report).

In the Faroe Islands, this standard setter or advisory body could be tasked with developing national standards based on International Public Sector Accounting Standards (IPSAS), produced by the International Public Sector Accounting Standards Board (IPSASB).9 When considering IPSAS, the standard setter or advisory body would examine three possible approaches: firstly, to simply “adopt” the standard; secondly, to “adapt” the standard when certain operational or resources constraints need to be accommodated; thirdly, to “remove” the standard for financial transactions that are not relevant to the Faroese national circumstances. The choice to “adopt”, “adapt” or “remove” standards

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9 The most recent OECD survey on financial reporting (OECD, 2017) shows that a third of OECD countries are using IPSAS directly or as a primary reference for setting their national standards. The number of countries using IPSAS is expected to increase, as the framework develops.
would have to be formally identified and justified for the information of key stakeholders (the Parliament and Auditor General), and potentially revised at later stages.

However, in the context of the limited resources, adopting an existing framework may be necessary for being able to deliver quickly a consistent and comprehensive set of standards. A second option would be that the legislation requires that entities use directly an existing set of accounting standards. For example, the Faroe Islands could consider using IPSASs, which has standards prescribing the accounting treatment for all major assets and liabilities, including land and a variety of natural resources, two important components of the State’s wealth in the Faroe Islands.

### Box 1. IPSAS standards: Accounting treatment of land and biological assets

The accounting treatment of Property, Plant and Equipment is regulated by IPSAS 17, which defines the recognition, the determination of the carrying amounts and the depreciation charges and impairment losses of these assets. In particular, for each class of property, plant and equipment, (PP&E) the financial statements of an entity shall disclose: the measurement basis used for determining the carrying amount; the depreciation method used; the useful lives or the depreciation rates used; the gross carrying amount and the accumulated depreciation at the beginning and end of the period; and a reconciliation of the carrying amount at the beginning and end of the period, showing additions, disposals, increases or decreases resulting from revaluations and impairment losses, etc.

Land is an example of a class of a PP&E item, and it has generally unlimited useful life, i.e. it is not depreciated. Buildings, on the other hand, have a limited useful life and are thus depreciable assets, even when they are acquired together with land. Indeed, land and buildings are accounted for separately, so that an increase in the value of the land on which a building stands does not affect how the depreciable amount of the building is determined. The Standard specifies also how to determine the useful life of an asset, the frequency of revaluations, and how to manage de-recognition of an item.

The accounting treatment and disclosures for agricultural activity (including aquaculture, i.e. fish farming) and biological assets is regulated by IPSAS 27, which prescribes that a biological asset shall be measured at its fair value less costs to sell. An entity shall distinguish between consumable biological assets (animals and plants for one-time use, including fish in farms) and bearer biological assets (used repeatedly for more than one year, such as breeding stocks), but also between mature and immature biological assets. Additionally, an entity shall describe the nature of its activities involving biological assets and an estimation of the physical quantities of both each group of biological assets and the output of agricultural produce.

*Source:* Author, based on IPSAS.

However, due to size and resources constraints, the Faroe Islands could consider adopting other frameworks or standards. For example, the United Kingdom’s Financial Reporting Standard (FRS) 102 issued by the Financial Reporting Council is a standard aimed at ‘small and medium-sized’ entities, which requires only succinct financial reporting requirements but remains however aligned with generally accepted accounting principles. Outside of the United Kingdom, Ireland, for example, has been using FRS 102 as the mandatory standard used for local governments’ accounts for a number of years.

Box 2. Selected OECD Countries: advisory body role and responsibilities

**France**

Accrual accounting standards are enacted by the Ministry of Finance, after receiving advice from an independent advisory council (“Conseil de Normalisation des Comptes Publics”, or CNoCP). The CNoCP is tasked with proposing standards to the Ministry of Finance for three separate sectors: the State and its agencies, the Social security and the Local Governments. The CNoCP has a Standing Committee (“College”) comprising a Chair and 18 members, including 9 ex officio members and 9 technical experts, who are appointed by the Minister of Finance for a three-year fixed term period, with the possibility of renewal. For each sector, a Sectoral Committee, working under the leadership of a Chair, composed of qualified professionals is in charge of establishing sectoral standards. Each sectoral committee comprises members with sectoral knowledge, with some members taking part in all committees.

**Portugal**

In Portugal, the accounting standard-setter role was redesigned following a major reform of the organisational structure of the Ministry of Finance in 2012. The accounting standard-setting commission (Comissão de Normalização Contabilística – CNC) was created by Law-decree 134/2012. It is an independent body under the Ministry of Finance comprising stakeholders from both the private and the public sector. CNC comprises two committees: one for business accounting, and another for public sector accounting (Comité de Normalização Contabilística Pública – CNCP). According to article 18, the main task of CNCP is to issue public sector accounting standards and interpretations taking IPSASs as reference, as well as to contribute to its development, implementation and improvement. CNCP comprises 9 members, including representatives of the accountants and auditors institutes, the Budget General Department, Local Government General Department, Finance Inspection Directorate, National Institute of Statistics; Universities teaching accounting, and an independent member acknowledged as expert (article 16).

**The United Kingdom**

The accounts of central government Departments and agencies are prepared in accordance with the Government Resources and Accounts Act 2000 (GRAA) and the Government Financial Reporting Manual (FReM) which applies International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector by HM Treasury, and sets out the framework by which Government Departments should prepare their resource accounts. To prepare the FReM, HMT is advised by an independent advisory board (Financial Reporting Advisory Board - FRAB). The FRAB is composed of representatives from the accountancy profession in the private and public sectors, academia and government bodies.

Annex A. OECD best practices and standards on accounting and financial reporting

Concerning accounting and financial reporting, the OECD Recommendation of the Council on Budgetary Governance recommends that “budget documents [i.e. the budget and accounts] are open, transparent and accessible” (principle #4) by:

- “the presentation of budgetary information in comparable format [through the budget cycle]” meaning that the budget and accounts should be prepared according to the same nomenclature and accounting basis;
- “the publication of all budget documents [i.e., budget and accounts] fully, promptly and routinely, in a way that is accessible to citizens, civil society stakeholders and other stakeholders”, meaning that financial data should be made available ideally on a monthly basis.

In addition, governments should “present a comprehensive, accurate and reliable accounts of public finances” (principle #6) by:

- “presenting a full national view of the public finances”, meaning that information should be provided in the accounts on the financial situation of, ideally, the whole of the public sector or, at least, for the central government; and
- “accounting in a manner that shows the full financial cost (…) of budget decisions, including the impact upon financial assets and liabilities”, meaning that accrual accounting financial statements should be established, eventually as a complementary information to the cash budget outturn.

Moreover, governments should “promote the integrity and quality of (…) budgetary implementation through rigorous quality assurance” (principle #10) by “supporting the supreme audit institution in its role of dealing authoritatively with all aspects of financial accountability”.

Finally, the OECD Guidelines on Corporate Governance of State-Owned Enterprises (“SOE Guidelines”) call for the state as an owner of commercial enterprises to “set up reporting systems that allow the ownership entity to regularly monitor, audit and assess SOE performance” and “develop consistent reporting on SOEs and publish annually an aggregate report on SOEs”.

Annex B. Faroe Islands: Recommended financial reporting framework