Written evidence from HM Treasury (IGA 06)

Public Administration and Constitutional Affairs Committee inquiry: Government accounts

Questions to consider
The format of monthly management accounts

Monthly management accounts, usually in the format of departmental board reports, are prepared in all departments for ministers, the board and the Permanent Secretary. Departmental boards regularly review reports that cover performance, money and major programmes/policy objectives. As such, they integrate inputs, outputs and outcomes.

1. What is the purpose of monthly management accounts?

Monthly management accounts provide senior leaders with the information they need to make considered, evidence-based decisions. Following the recommendations in the 2013 review of financial management, HM Treasury (HMT) and the Chartered Institute of Management Accountants (CIMA) co-developed Global Management Accounting Principles, and outlined how these would be applied to HM Government. HMT have disseminated these principles across departments, encouraging them to prepare their monthly management accounts and other reports for their boards, ministers and Permanent Secretaries in line with these principles. Specifically, they enable a department to:

- Drive better decisions about strategy and its execution;
- Analyse impact and value for money;
- Manage the resources so that financial and non-financial assets, reputation and value of the department are protected.

2. How far do monthly management accounts currently meet this objective? Is their quality consistent?

Departmental management accounts enable better decision making. There remains some variability in structure between departments, which reflects the different operating models and individual needs of each department. HMT has piloted a set of central government management accounts, in line with CIMA standards, in order to provide decision makers and senior officials in HMT with the information they need.

HMT are also working with Cabinet Office to roll out a new planning and performance framework for all central government departments, and Single Departmental Plans (SDPs) are at the core of this framework. Guidance and ongoing support has been provided by the centre to increase standardisation and raise the quality of planning across government. Departments will report regularly to HMT and Cabinet Office on progress against their SDP, as well as publishing updates against key output and outcome metrics online.

Management accounts play a key role in achieving value for money, and HMT has been working to assist departments to raise the quality and consistency of their reports even further. This includes sharing best practice, driving discussion and
accountability through the Finance Leadership Group (comprised of Finance Directors General) and a coordinated cross-departmental effort to improve departmental board reporting, which was a specific strand of work under the implementation of the Financial Management Review (FMR).

3. **How can the monthly management accounts be improved to ensure they are more useful to decision makers, particularly Permanent Secretaries, Departmental Boards and Ministers?**

Government has made progress towards improving management accounts. HMT has played a role in driving up standards, but the quality of departmental reports is ultimately the responsibility of departments themselves.

As part of the FMR, HM Treasury has led a process to improve the standard of departmental board reports across Whitehall. HMT have collected and disseminated reporting best practice, developed and shared principles of good board reporting, and established a Board Reporting Knowledge Network to connect departmental experts across Whitehall.

The FMR programme is also developing other tools to help ensure management information is more useful for decision makers, such as a data visualisation training that is being developed as part of the new Government Finance Academy. It also produces a set of government management accounts, which summarise the financial performance and current risks for each department for HMT leadership in a concise, readable way.

In addition, HMT, and government more broadly, has actively leveraged private sector experience to help improve the quality of management accounts. Non-executive directors continue to play an important role within departmental reporting, bringing new perspectives and best practice examples. The FMR Board, which oversees and steers the implementation of the FMR programme, has 3 CFOs of major companies as members.

4. **How could outcomes be integrated into the monthly management accounts, such as proposed by the MINIS system promoted by Lord Heseltine?**

HMT continue to learn lessons and take best practice from former management information regimes. When reviewing the government’s performance management framework in 2015, with a view to establishing new SDPs, HMT worked closely with Cabinet Office colleagues to draw lessons from former frameworks, including Public Service Agreements and Business Plans. Key recommendations from this exercise included ensuring that any new performance framework was underpinned by outcome metrics, and that the new framework should mirror existing departmental management accounts where possible, to avoid duplication. This system is now being rolled out across 17 government departments.

5. **How far can the monthly management accounts be made public?**

HMT have made progress in making management information transparent, but it is not always appropriate to publish all internal information on a monthly basis.
In February 2016 every department published a summary of their SDP. Each SDP lays out the department’s objectives, the political commitments it has made, its business-as-usual activity, and headline indicators to demonstrate progress. Data against each of these indicators is being regularly updated with the latest management information. Departments will also report in full on progress against their SDP through their annual reports and accounts.

There is also a variety of other data and information already in the public domain. A Memorandum for the Supplementary Estimates is issued by each department to provide additional information about supplementary estimates, and how it will be applied to achieve departmental objectives. A variety of civil service people statistics are available via the Office for National Statistics (ONS) or via the data.gov.uk website. Public spending statistics are available on gov.uk, presenting analyses of public spending against budgets and expenditure on service frameworks. The statistics are updated quarterly with a full report annually.

However, HMT does not deem it appropriate to publish all monthly management information, and indeed this is not what routinely happens or is considered best practice in the private sector. Some data is sensitive or classified, and publication could affect national security. Often, data is used to inform policy development, where decisions have not yet been taken. Other data is commercially sensitive, and could affect ongoing negotiations or the UK economy if released without appropriate context. It is important that management information is approved before publication, which can take time.

**The current utility of departmental accounts**

1. **How useful are the accounts as a tool to scrutinise the Government?**

Until the introduction of Resource Accounting and Budgeting (RAB) in the late 1990s, central government departments planned and reported their expenditure on a cash basis. Since the 1999-2000 financial year all departments have produced audited accounts on an accruals basis. These are produced according to Generally Accepted Accounting Practice (GAAP) to the extent that it is meaningful and appropriate in the public sector context. Combined Annual Report and Accounts (ARAs) are consolidated to include all agencies and arm’s length bodies (ALBs) within the departmental boundary.

The accounts give a true and fair view of the state of affairs as at 31 March and of the net resource outturn, the application of resources, changes in taxpayers’ equity and cash flows for the financial year then ended. They also provide disclosure of any material expenditure or income that has not been applied to the purposes intended by Parliament or material transactions that have not conformed to the authorities which govern them. Accountability is the primary objective of financial reporting in central government.

Departmental accounts are one of several tools produced to provide reassurance that resources granted by Parliament have been used in a regular and proper way and that relevant controls have been adhered to. They give relevant information on the management of both the balance sheet and income and expenditure, as well as relevant disclosures on longer term risks and liabilities.
Since the 2009-2010 financial year HM Treasury have produced the Whole of Government Accounts (WGA) which, in 2013-14, consolidated the audited accounts of around 5,500 organisations across the public sector in order to produce a comprehensive, accounts-based picture of the financial position of the UK public sector. WGA provides some broad context and a sense of materiality across government, alongside other tools such as Public Expenditure Statistical Analyses (PESA), fiscal event documents and information produced by the Office of Budget Responsibility (OBR).

2. Which part of the accounts are used by those scrutinising the Government? Which parts are not?

WGA is a major step forward in transparency and accountability as it supports the government’s agenda to make more public data available. It enables the direct comparability of financial data across public sector entities and produces trend data that will help to inform future analysis and decision making. WGA is independently audited giving both Parliament and the outside world greater confidence in the figures, and supports effective scrutiny by Parliament. The Public Accounts Committee has welcomed the publication of the WGA as an improvement in transparency and accountability.

The introduction of accruals accounting and budgeting for central government departments has led to significant improvements in financial management and external accountability, particularly with the further reforms introduced under the Clear Line of Sight project. The National Audit Office (NAO) note that the project has brought greater alignment and coherence to its key financial data and the processes supporting the management of public finances.

Reforms to the format of departmental accounts

1. How could Departmental Accounts be improved to meet the needs of Parliament and the public?

HM Treasury launched the Simplifying and Streamlining Accounts project in 2013 with the aim of restructuring the presentation of the statutory ARAs produced by central government entities so as to better meet the needs of users. The project recommended a restructuring of the traditional “front half” annual report and “back half” financial statements into three more integrated reporting requirements; performance i.e. “telling the story”; accountability; and financial statements. The Accountability section will contain a Parliamentary Accountability and Audit report which will bring together the key parliamentary accountability documents in one place within the ARAs. These improvements are being implemented in departmental ARAs from the 2015-16 financial year.

a. What is best practice in public sector accounts across the world and why is it best practice?

The IMF observe that accruals accounting in accordance with internationally recognised standards of best practice is seen as a vast improvement on cash accounting as it provides better information about the use of resources and promotes accountability and transparency. In addition, public sector entities should prepare a full set of financial statements and a management commentary which should be independently audited.
In 2015 the IMF estimated that 21% of countries had adopted accruals accounting. The UK is seen as a proponent of best practice in public sector accounting and budgeting along with New Zealand, Canada, Australia and the USA. A 2013 EU report noted that the UK’s adoption of IFRS as adapted for the public sector appeared to be those closest to International Public Sector Accounting Standards (IPSAS) amongst member states. The NAO report that the WGA is the largest consolidation of public sector accounts in the world.

b. What is best practice in the private sector and why?

Accruals accounting is fully established in the private sector. The Financial Reporting Council (FRC) is empowered by law to set UK accounting standards for the private sector and collaborates with other countries and the International Standards Board (IASB) in the development of international standards for their application in financial reporting. The FRC produces guidance to promote high quality corporate governance and reporting and cohesiveness to enable related information within the annual report to be linked together. International Financial Reporting Standards (IFRS) are set by the IASB and adopted in the UK for consolidated financial statements of all companies whose securities trade in a regulated market but are also permitted for companies whose securities do not trade in a public market.

The FRC has a programme of activities under the “Clear and Concise” initiative aimed at ensuring that annual reports provide relevant and accessible information for users. It reinforces the importance of materiality and encourages the streamlining of information to better meet the needs of users.

The public sector seeks to apply the principle of the Corporate Governance Code and from 2015-16 the Accounting Officer must confirm that the annual report and accounts as a whole are “fair, balanced and understandable”. Departments and their ALBs apply EU adopted IFRS and relevant interpretations for the public sector.

2. What if anything is missing from the Treasury 2014 Command Paper which laid out the new accounting procedures for 2015–16?

The 2014 Command Paper outlines the Simplifying and Streamlining Accounts project which recommended a restructuring of the annual report and financial statements into three more integrated reporting requirements; performance; accountability; and financial statements. The performance reporting requirement includes a clear statement of the purpose and activities of the organisation, high level financial information with cross references to the audited accounts and trend information with commentary against trends and performance against policy. The accountability requirement contains a Governance Statement and information on strategic risks to the entity, the Remuneration Report and information on parliamentary accountability, including the Statement of Parliamentary Supply. The final requirement shows the set of financial statements and disclosure notes that the NAO has audited to International Standards of Audit.

The aim of the new accounting procedures is to ensure that the ARAs provide information about the reporting entity that is useful to Parliament and the wider user community for accountability and decision making purposes. By giving reporting entities greater freedom to focus on what matters to them and how they define success in their ARAs, the information provided in those reports should become
more output and outcome focused. This will not only allow Parliament to better hold those charged with governance to account but it will also hopefully ensure entities are themselves more focused on delivering what adds real value in their operations.

3. How far should other government accounts (for NDPBs and Agencies) reflect the format of Departmental accounts?
   a. How much more should government accounts be standardised?

Government departments, NDPBs and Executive Agencies prepare accounts in accordance with the Government Financial Reporting Manual (FReM) which is the technical accounting guide to the preparation of financial statements and is updated annually. Accounts are prepared on an accruals basis in order to present the entity’s financial position and performance in accordance with IFRS as adapted and interpreted for the public sector in accordance with the Government Resources and Accounts Act 2000 (GRAA).

The specific accounting arrangements for an entity will depend on how an entity has been classified by the Office for National Statistics (ONS). Agencies and ALBs should prepare accounts in accordance with their governing documents, relevant legislation and the directions given by sponsor departments. However, entities will need to provide the additional disclosures required by the FReM where these go beyond the requirements of the relevant legislation. All government accounts are therefore prepared following the same principles and entities do not need to develop accounting policies, or provide disclosure notes, in relation to accounting standards that do not apply to their circumstances or are immaterial. Whilst the FReM contains illustrative accounts as a guide to departments, these are not templates and departments have flexibility in how they meet the mandatory reporting requirements and to include additional content.

Future improvements to accounts

1. Who should have control over the format of Departmental Accounts and Whole of Government Accounts?

HM Treasury has statutory powers under the GRAA to determine the reporting framework under which departments operate, and also prepares the WGA for the whole of the UK public sector (central government, local government and public corporations) under section 9 of the same legislation. This follows commercial practice but provides flexibility to meet the unique context of the public sector. The Financial Reporting Advisory Board (FRAB) provide independent advice to HM Treasury. The accounting framework controlled by HM Treasury enables departments to have flexibility to organise their reports in a way that makes most sense in terms of their objectives, organisation, business processes and Select Committees’ needs.

2. What independent body should advise on the format of Departmental accounts in the future?

The GRAA set out that the Treasury shall consult a group of appropriate people to advise on financial reporting and standards. This role is fulfilled by the FRAB in order to ensure that government financial reporting meets the best possible standards of financial reporting by following GAAP as far as possible. It is fully independent and includes senior representatives from the accountancy profession in the private and
public sectors, the NAO, academia and government bodies, as well as a parliamentary observer. The Board meets regularly to consider proposed changes to policy and practice. Where changes to the accounting guides are made, the Treasury is responsible for publishing them via the FReM. Each year the board produces a report of their activities throughout the year, which is laid before Parliament.

3. How can we judge the success of Departmental Accounts as disclosures of information to the public?

Departmental accounts are laid before Parliament each year and also available online on the gov.uk website where they can be easily accessed by members of the public. From 2015-16, a key disclosure is the performance section of the accounts whereby entities will be able to “tell the story” in a way that is more relevant and understandable. It provides information on the entity, its main objectives and strategies and the principal risks that it faces. It will complement, supplement and provide context for the financial statements, with the intention that the information in the overall ARAs will be integrated to provide a cohesive document.

Improving scrutiny of financial information from the Government

1. How can financial scrutiny of departments in both Parliament and outside be improved?

HM Treasury sets guidance and direction to ensure that departmental ARAs present a clear picture of the aims, activities, functions and performance, linking performance and services delivered over the reporting period with expenditure and other financial information. Departments and their ALBs are required to prepare ARAs in accordance with the FReM, other related guidance and Managing Public Money (MPM) and should be produced in a timely manner in order to meet the administrative deadline for laying these publications in Parliament. The format and content should meet the needs of users and the consistent application of the relevant reporting requirements make their scrutiny and comparability easier. By laying ARAs in a timely manner, the information offers better accountability and provides information which can be acted upon for decision making purposes. HM Treasury continues to work with departments to reduce the time taken to lay their consolidated annual reports and accounts.

HM Treasury has introduced the simplification and streamlining agenda from 2015-16 to improve the quality and presentation of both financial and non-financial information, and is currently looking at the potential for further opportunities to reduce disclosure requirements where appropriate.