Written evidence from Organisation for Economic Co-operation and Development (IGA 21)

Public Administration and Constitutional Affairs Committee
Inquiry into Government Accounts

This submission draws on recent surveys undertaken by the OECD, and aims at presenting an overview of OECD countries’ practices with regards to in-year and year-end financial reporting, as well as the best practices identified in the OECD’s Recommendations on Budgetary Governance and Best Practices for Budget Transparency.

This submission notes that:

- The United Kingdom (UK) Government’s practices with regards to in-year and year-end reporting are among the most advanced in OECD countries.
- Currently use of Monthly Management Accounts in the public sector is not a widespread practice. However, virtually all OECD countries publish monthly budget execution reports that allow comparison between planned and actual results.
- Among the group of OECD countries that implement accrual accounting and publish yearly audited financial statements, satisfaction with the usefulness of financial reports is mixed, and number of remediation measures have been implemented or considered.
- The UK Government’s practices with regards to setting the format of financial reports are similar to those of a majority of OECD countries.
- International frameworks, so far, do not define how public sector financial reports should bring together financial, accountability, and performance information, hence the need for guidance and practices to be developed at the national level.

Monthly Accounts

1. In the private sector, Monthly Management Accounts (MMA) contain information that allows management to gauge regularly its performance against set budgets and expected forecasts. In most private sector entities, the board or senior management will therefore require the management accountant or chief accountant to produce at least a monthly profit and loss account/income statement, but the MMA may also include a range of other key metrics (e.g., sales figures).

2. The publication of MMA is not a widespread practice in the public sector. MMA are internal documents aimed at informing the management’s decisions, while, in the public sector, financial reporting (in-year or at year-end) traditionally is aimed at assessing the compliance of actual spending against the approved budget, and holding public officials to account for the use of public money.

3. Therefore, most governments only publish Budget Execution Reports that follow the presentation and classification of the annual budget and aim at comparing outturn values for revenue, expenditure, and other fiscal aggregates with the levels approved by the legislature in the budget. Based on an OECD Survey, governments’ practices with regards to budget execution reports are as follows:

---

Virtually all jurisdictions reported that governments publish interim financial statements on the same basis of reporting as their budgets (i.e. comparable accounting method, allowing comparison between planned and actual results);

Almost two thirds of countries indicated monthly updates. Of these, almost half indicated that the reports are issued within three weeks of the reporting period’s end;

Approximately one-quarter of the jurisdictions reported that only aggregate-level expenditure information is released. Among the remainder, approximately half reported that expenditure data are presented for each ministry (or department), while the other half indicated that even greater levels of detail are made available at the programme level;

Only one-third of respondents indicated that the interim reports contain non-financial performance information;

Most countries do not have a formal process for consideration of the interim reports by legislatures. Rather, the reports are considered on an ad hoc basis. Among the minority of countries that do have established review processes, approximately one third indicated that the reports are used for in-year resource allocation or reallocation.

4. The OECD Best Practices for Budget Transparency provides guidance regarding timing and content of interim reports. The OECD recommends mainly that:

- Governments (Finance Ministries or Departments) release monthly budget reports within four weeks of the end of each month;
- Reports contain the amount of revenue and expenditure in each month and year-to-date. A comparison should be made with the forecast amounts of monthly revenue and expenditure for the same period;
- A brief commentary accompanies the numerical data. If a significant divergence between actual and forecast amounts occurs, an intelligible and relevant explanation should be made.

5. The OECD Recommendations on Budgetary Governance also advise governments to prepare, publish, and scrutinize interim financial reports that should yield information on spending and performance. It recommends in particular governments use a small number of performance indicators for each policy program (outputs and outcomes), which allow the tracking of results against targets.

Format and Utility of Year-End Financial Reports (Departmental Accounts and WGAs)

6. Based on an OECD Survey, the United Kingdom’s financial reporting practices are among the most advanced in OECD countries: it implements accrual accounting (72% of OECD countries); produces complete financial statements including management commentaries (42% of OECD countries); consolidates the financial statements of all public sector entities (15% of OECD countries); and uses accounting standards based on IPSAS or IFRS (41 % of OECD countries).

---


7. In all OECD countries, financial statements are subject to independent external control or audit, but only 62% of respondents, incl. the UK, indicated that their supreme audit institutions (SAIs) provide an opinion on the year-end financial report according to international auditing standards. Among this group of countries, a high proportion of the audit opinions are qualified.

8. Overall, OECD countries’ financial reporting practices are consistent with the OECD Recommendations on Budgetary Governance, which advise governments to present a comprehensive, accurate, and reliable account of public finances annually that is submitted to independent audit. Accordingly, a majority of OECD countries express satisfaction that recent reforms have allowed objectives with regards to transparency and accountability to be fully achieved.

9. However, Finance Ministries recognize that parliamentarians, and the public at large, still have limited interest in available financial information, and stakeholders express regular concerns about financial reports not meeting their needs. Concerns are generated in particular by uncertainties over i) the exact purpose and content of financial reports, ii) their alignment and comparability, iii) the completeness and usefulness of the financial information for oversight and decision making purpose, iv) the understandability of the reports, and v) the linkage to non-financial performance information.

10. A number of initiatives are on-going to address these issues. They include:

- Aligning the presentation, accounting basis of financial reports;
- Using new technologies to give full access to detailed data to the public on public spending, contracts, grants, and other financial operations, as a complement to the “aggregated” information provided in financial reports;
- Enhancing the understandability of financial reports by including management commentaries, or limiting the volume of disclosures;
- Developing financial analysis tools and information (for example benchmarks for certain costs, such as salaries, and standardized valuation methods for overhead costs; fiscal ratios for analysing the impact of fiscal policies in the financial statements; information on the management of assets and liabilities).

11. Governments also recognize the need to rationalize financial reporting further, as, despite the increasing quantity of financial data available to the public, there seems to be no clear and shared understanding of what information the set of documents as a whole should provide and the exact content of each document.

12. These concerns are not unique to the public sector. The International Accounting Standards Board (IASB) launched a project in 2013 to address ongoing concerns about the quality and quantity of financial reporting disclosure. The IASB underscored that it was trying to deal with a general concern that, on the one hand, bigger and bigger financial reports were getting overly costly for preparers, and, on the other hand, investors were saying that the reports were not giving them the information that they needed.

**Improvements to the Format of Financial Reports**

13. Similarly to the practice in UK, finance ministries are the standard-setting authorities in about a half of OECD countries. The need for objectivity, independence, and integrity in defining the government financial reporting standards is however acknowledged by

---

5 See reference above.
governments, which increasingly consult their supreme audit institutions before enacting new accounting standards, or establish an independent advisory board. A quarter of countries have taken a step further and set up national standard setting boards independent from the government.

14. Also, similar to the practice in UK, nearly all countries develop national accounting standards but use international frameworks as a reference. Reasons for favouring national standards include i) accommodating a number of specific deviations, such as limiting the quantity of disclosures, ii) defining boundaries for the financial statements that are aligned with the ones used in the budget and the fiscal statistics, or iii) reflecting the specificities of national legal frameworks and public policies.

15. It is worth noting that international frameworks (IFRS and IPSAS) define high-level, principle-based guidance, and focus on the accounting treatment of financial transactions. Where governments want to define more detailed financial reporting guidance, and bring together financial, accountability, and performance information, setting the format of the financial reports at the national level, as done in the UK, appears necessary.

* * *

16. The above messages are based on OECD analysis of the experiences of other countries with financial reporting. We would be pleased to elaborate on any of these points, including providing specific examples of experiences in our Member countries.

July 2016