

Study visit

PEMPAL Treasury Community of Practice (TCOP)

“Implementing Accounting Reform in the UK Government”

London, United Kingdom



From September 23 to 25, eleven TCOP members from nine countries participated in a visit to the United Kingdom to meet with officials from the UK Treasury. The focus of the visit was to find out how the United Kingdom is dealing with the challenges of public sector accounting reform, in particular, implementation of accrual accounting. During the visit attendees also took the opportunity to explore possibilities for cooperation with the

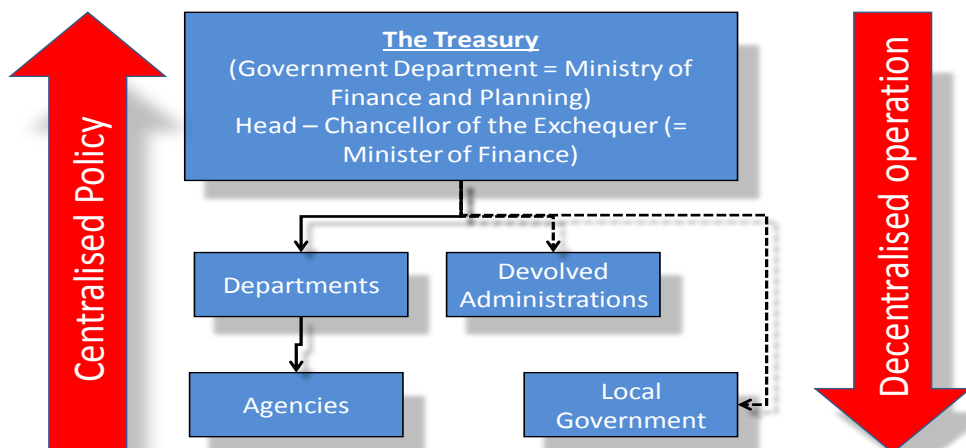
International Federation of Accountants (IFAC) and The Chartered Institute of Public Finance and Accountancy (CIPFA). The visit was supported technically by a World Bank Team and administratively by officials from the Slovenian Centre of Excellence in Finance.

In preparation for the visit, **Michael Parry**, TCOP expert, delivered a presentation on Public Financial Management in the UK to attendees via video conference.



General approach to UK PFM

Very centralised control of financial policy
Very decentralised operation of PFM



The UK system is very different from that operating in TCOP Member countries and it was therefore considered important to provide participants with a general understanding prior to

the visit, particularly to ensure some of the unique terminology and processes were more familiar and understandable. Concepts such as the UK supply estimates and resource budgets, would be new to most participants, as would the fact that the UK does not have a written constitution.

The visits commenced Monday morning 23 September, with a welcome address by the Chair of the TCOP, **Angela Voronin**, who thanked the UK Treasury for agreeing to the visit and hosting the delegation. **Karen Sanderson**, Head of the Public Expenditure Group of Her Majesty's (HM) Treasury, officially welcomed the visitors and gave a brief introduction on the UK public financial management system. Attendees were interested to learn



that the UK government had adapted International Financial Reporting Standards rather than International Public Sector Accounting Standards (IPSAS), as the model in the UK, due to the fact that IPSAs were not in place at the time the UK commenced its accounting reform. Participants were particularly interested to understand the role of the Office of Budget Responsibility in relation to the Treasury. Karen informed the delegation that this independent organisation develops independent fiscal forecasts, which are used by the Treasury in formulating the budget.

Emily Curtis, from HM Treasury delivered the first formal presentation where she provided



an overview of the UK system for spending control. The UK undertakes a three year spending review for its departments similar to what might be termed a medium term expenditure framework in other countries. However, something which may be unique in the world is that while the budget is formally presented to the Parliament, HM Treasury separately submits supply estimates, which represent the request for the authority to spend public money for the

government. Emily also indicated that the UK had moved from cash to what it terms resource budgeting, which the UK government's approach to accrual is budgeting. This was further expanded upon during day two and three.

Next **Gary Hansman** provided more detail on the Supply Estimates which have a strong historical base in the UK system, where government seeks the approval for its annual resource requirements from the Parliament. The much devolved nature of public finance in the UK means that the Treasury does not have a system based control over the estimates, such as an integrated government financial management system. If a department overspends its estimates,



its Head will be called before the Parliamentary Public Accounts Committee (PAC) to answer for this breach. In practice overspends are rare, with the trend in more recent years to be for spending to be less than the estimates, in part due to a tightening fiscal position. The supply estimates are broken down in to three major components: a request for accrual resources; capital; and the cash requirement of the department¹. Gary pointed the group to an online publication titled *Supply Estimates: A Guidance Manual*² for more detail on the arrangements and procedures.

Both Emily and Gary received extensive questions from the group, particularly in relation to how central control over the estimates was maintained. It was of interest for the group to note the high level of devolution of control and authority operating in the UK compared to their own countries. Despite this, compliance levels in budget controls was reported to generally be very high, in part due to the perceived negative consequences of being scrutinized by Parliament.

The afternoon of day one was devoted to a working session, where the World Bank team facilitated a discussion of key issues identified thus far, and highlighted some of the differences between the participants' country systems and that operating in the UK. Key areas discussed included:

Whether the UK has government programmes – While the answer was yes, these are not the typical budget and reporting structure seen in many other countries. Programme guidelines state that programmes are only required where it would be strategically beneficial to have a layer of management and control between projects and organisational entities – in other words programmes are not universal.

¹ In the UK, a department is the equivalent of a ministry

² www.gov.uk/government/publications/supply-estimates-guidance-manual

Thus programmes are a special additional reporting structure rather than an integrated component of government budget planning and execution.

The Treasury indicated that the full year's appropriation is released at the beginning of the year and the group wanted to understand if that meant the cash was also released.

The expert group indicated that this was unlikely to be actual cash, rather it was probably the authority to spend. Departments would normally be expected to also provide an indication of actual cash disbursement requirements to assist with liquidity management. The UK Debt Management Office which is an Executive Agency of HM Treasury, undertakes regular cash operations during the day, suggesting it has good quality information on planned cash flows and a degree of central control over the cash balances.



The group indicated that the consultative budget process in the UK was particularly interesting, and noted that it suggested the UK had less prescription and rules to guide processes than many of the countries attending the event. It also appeared that a significant incentive for good management was the knowledge that you could be criticised by an external body such as the Public Accounts' Committee. The World Bank team noted that internationally,

there were two general themes in way legislation was drafted for government: the highly prescriptive approach versus the trend in many OECD countries for principle based legislation. Notwithstanding this, they also noted that even in countries where principle based laws applied, and where devolution was the norm, there were cycles in PFM reforms with periods of high devolution followed by periods of increased central scrutiny, particularly when the budget was under fiscal pressure. UK has recently seen such a process, with the most recent spending review occurring within just 12 months of the previous review (normally three yearly).

Day two commenced with a presentation by **Thomas Zimmerman**, on IFAC and Public Sector Financial Management. Thomas explained that the goal of IFAC was to improve the quality of accounting across the globe so that the profession would be recognised as a valued leader. Thomas went on to explain the various Boards and structures in IFAC and the Statement of Member's Obligations.



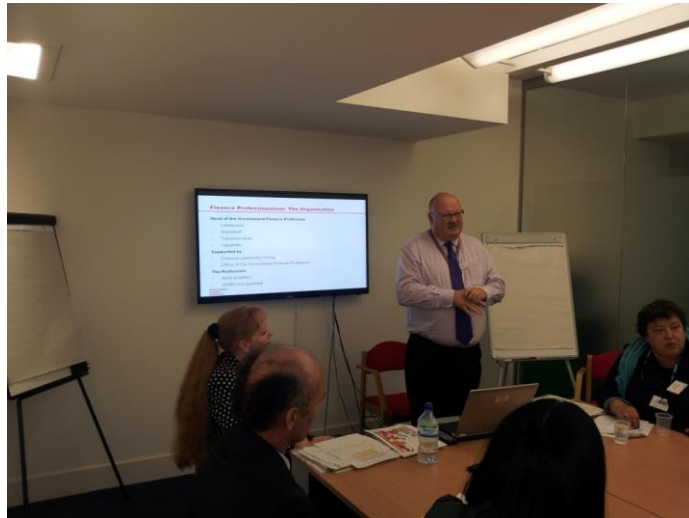
He also briefly described the status of the adoption of IPSAS across the world and in the nine countries attending.

Thomas was asked whether in the absence of a national accounting body, a government could become a member. He indicated that at present, only professional accounting bodies were eligible to be members, but acknowledged that this did present an issue in some jurisdictions.

The group next met with **Sue Davidson** and **Madeleine Smith** from HM Treasury, who presented on the topic of Public Money and Accountability to Parliament. Sue and Madeleine explained many different aspects in relation to accountability including the select committee process in Parliament which covered each department. Typically they would review the budget and annual accounts of each department each year, including what the department achieved in terms of results with its public money. Treasury has also been given the authority to issue instructions to departments. This includes the budget process and controls over budget execution. The Treasury appoints Accounting Officers (AO), usually the executive head of a department or agency. Each accounting officer is responsible for the performance of his/her department and for ensuring control and accountability of the autonomous agencies, termed Arm's Length Bodies (ALB). The departmental AO also appoints an AO in each ALB under the department's jurisdiction. Sue and Madeleine also directed attendees to a number of publications on PFM including "Managing Public Money", which was described as a publication to guide Parliament's expectations regarding the use of public money. Through a question from the group it was clarified that the publications or guidance from the Treasury did not have the force of law, but in general it was expected that departments and agencies would follow the guidelines unless it could be demonstrated it was in the public interest to not do so. In relation to local governments and independent territories the guidelines were available but these governments had their own authority in relation to governance.



The penultimate presentation for day two was by **Mike Buckley** (Department of Work and Pensions) and Gillian Crooks, (HM Revenue and Customs) on finance professionalism in Government. This is an organisation created to provide leadership for the development of the financial profession in the UK government. The profession goes beyond formal accountants to all officials with a financial role. In fact, of the 29,000 officials involved in



financial roles, only 9000 have a professional qualification in the UK public service. The Office of the Government Finance Profession is led by the Finance Leadership Group. However, the office and team is a virtual unit, formed from resources provided by different government departments through secondments, as demonstrated by both Mike and Gillian's home departments. Gillian is the Human Resource Advisor to Finance Leadership Group and has been developing its capabilities framework after undertaking a similar role with HR Revenue and Customs. One participant indicated that the concept of a virtual team was somewhat difficult to fully comprehend as no similar structures exist in their countries. In addition to looking at training opportunities in the market place for its members, the group is also focussing on getting the right people recruited to the public service.

The final presentation of day two was by **Phil Trotter**, HM Treasury, on the *Introduction of Accrual Accounting in UK Central Government*. Phil indicated that local government in the UK had been accounting on an accrual basis since the nineteenth century, while for central government, it has been a relatively recent development occurring in the 1990s. Phil indicated that accrual accounting and budgeting in the UK was introduced for four main reasons:



modernising government; cash did not provide sufficient information for decision making; improved accountability; and because of the positive experiences in a number of other countries. For the introduction, a small dedicated team was set up with a planning time horizon of eight years. While Phil indicated that this was a long timeframe, it is worth noting that few countries have successfully implemented full accrual budgeting in a shorter timeframe. Phil also indicated that there were a range of challenges including: culture; the

need to establish a common vision; the costs and the benefits of implementation; effective communication; and of course managing the actual implementation.

For implementation there were four major deliverables or milestones:

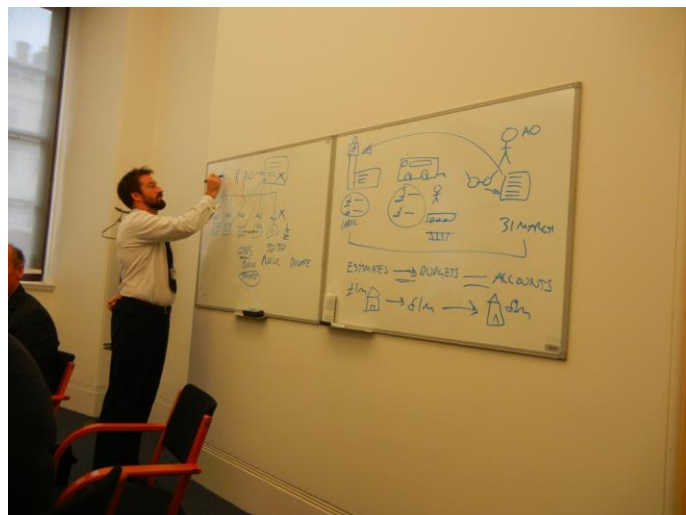
- Departments and Arms Length Bodies (ALBs) had the human and other capacity to produce accounts;
- Establishing the opening balance sheets –migration from cash to accrual and the correctness of opening balances;
- Undertaking an audit of a dry-run of the accounts; and
- Ensuring Parliament was happy with the information that was presented to it.

The eight year timeframe was also needed to absorb and allow changes to existing accounting systems. Many of them had to be replaced. UK did not make a specific system mandatory, with each department determining its own solution - this is now a problem with many different systems in operation that cannot properly communicate. Training also took time. Stakeholder management was another big issue, particularly engagement with Parliament. The implementation of accrual budgeting was the biggest change to the PFM system in 130 years

A further issue with consolidation has been the absence of a uniform chart of accounts (CoA). The history of strong devolution in the UK has made it challenging to create consistent approaches across the government sector. Such a standard CoA was now being introduced. This was generally not an issue for the participating countries, as they largely determined all the accounting practices centrally, including a uniform CoA. A further important development in public sector accounting has been the creation of the **Financial Reporting Advisory Board** which is independent of government and assures consistency in accounting practice and that departure from IFRS can be supported with a sound justification.

Phil Trotter was also the first presenter on day three shifting from detailing how the UK government implemented accrual to the recent and future developments in accounting. He highlighted three recent reforms:

- The so-called “Clear Line of sight” initiative – ensuring a transparent linkage between the budget, supply estimates and the annual accounts;
- Whole of government accounts – now all ALBs are consolidated first into a departmental reporting entity – thus each department is responsible for preparing their consolidated financial



statements prior to consolidating of the entire government sector.

- OSCAR - which is a central reporting IT system designed to capture, record and consolidate financial information ex-post from departments.

In terms of future developments Phil identified a further four areas:

- Streamlining and simplifying accounts - “following the pound” is an initiative which seeks to go beyond financial reporting to show the results achieved and the costs involved;
- Mid-year reporting - to report more than once a year and eventually throughout the year;
- European Public Sector Accounting Standards (EPSAS) – a future harmonisation initiative by the EC; and
- “Cutting the clutter” – all reporting entities are producing accounts but in many cases these are only examined by auditors. The Treasury ran a consultation process regarding stakeholder reporting requirements and in the future they will produce shorter more useful documents, focussed on the major material items.

After lunch CIPFA delivered three presentations. **Ian Caruthers** introduced CIPFA's PFM development work including introducing attendees to some of the publications and tools developed by CIPFA:

1. Whole systems approach to reform – public financial reform in itself is not enough -it needs to focus on all areas of governance to ensure proper traction.
2. Transition from cash to accrual CIPFA's stepping stones guide;
3. Role of the Chief Finance Officer; and
4. The CIPFA financial management model.



Giles Orr followed this by describing the CIPFA Education and Training Program including the four steps to a full professional qualification: Certificate; Diploma; Advance Diploma and the final Professional Qualification. This was further expanded on and described by **Peter Boulding**, including the CIPFA sustainability model for working with countries.



Mr. Giles Orr



Mr. Peter Boulding

The final formal presentation of the workshop was by **John Stanford**, IPSAB. John provided the attendees with the background to and conceptual framework for IPSAS. He also focussed on the differences between the public and private sector in terms of accounting and gave some very useful examples of possible approaches to government accounting, including the most challenging area for the public sector, non-financial/fixed assets.



The successful three day event was formally closed by **Angela Voronin** and **Karen Sanderson**.

In summary, the attendee's now have a better understanding of the way the UK PFM system operates including:

- The very high level of decentralization to Departments (Ministries), with each Department accountable to Parliament;
- The use of accrual for budget and budget execution across the whole of government;
- The fact that the UK Treasury (which acts as a Ministry of Finance) formulates budgets at highly aggregated levels and also has oversight responsibility for Departmental expenditure;



- That there is no programme classification as understood by TCoP member countries;
- No unified CoA exists but despite this HM Treasury manages to produce a consolidated financial statement for over 3000 reporting entities;
- The use of IFRS rather than IPSAS as the basis for financial reporting;
- The existence of an independent Office of Budget Responsibility with a very long term fiscal focus (up to 60 years for some purposes); and
- The focus on advanced training through the Finance Professional Transformation programme.

The TCOP intend to invite HM Treasury to future TCOP events for an update on reform, and also to exchange ideas – TCOP believes that some of the members’ recent experiences with reforms could also be useful to the UK.

