Resource Accounting and Budgeting in Government
This report has been prepared under Section 6 of the National Audit Act, 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

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The Comptroller and Auditor General is the head of the National Audit Office employing some 800 staff. He, and the NAO, are totally independent of Government. He certifies the accounts of all Government departments and a wide range of other public sector bodies; and he has statutory authority to report to Parliament on the economy, efficiency and effectiveness with which departments and other bodies have used their resources.
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Introduction

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1 In July 1994 the Treasury published a Green Paper "Better Accounting for the Taxpayer's Money: Resource Accounting and Budgeting in Government" which announced proposals for:

- resource accounting, whereby from 1999-2000 central government departments produce and publish accruals-based "resource accounts" to supplement their current cash-based accounts; and

- resource budgeting, under which the public expenditure planning process, and the Supply process through which Parliament grants legal authority for much of government spending, might both be changed to an accruals basis sometime early in the next century.

2 The Green Paper sought views on resource accounting proposals and indicated that the Treasury would consult Parliament and others on how resource budgeting might be implemented. The consultation period will last until 31 January 1995 and the Government will publish its detailed proposals for resource budgeting as soon as possible thereafter.

3 The Government's proposals represent the most important reform of central government accounting and budgeting arrangements since Gladstone's reforms of the mid-19th century. They mark a significant change in the way departments account and manage and should be seen alongside the Government's plans, in the July 1994 White Paper "The Civil Service: Continuity and Change", to achieve greater efficiency by delegating powers to departments and giving central departments a more strategic role. The proposals may also bring radical changes in the format of Estimates and Appropriation Accounts, with far-reaching consequences for the form of Parliamentary authority over departmental expenditure.

4 The Green Paper was issued shortly after Parliament had considered separate Treasury proposals to revise the format of the Estimates, and therefore the Appropriation Accounts. Both the Committee of Public Accounts and the Treasury and Civil Service Committee expressed reservations about these proposals, and wanted to see them in the context of the imminent Green Paper. In response, the Treasury deferred their changes for one year, and have since been encouraging departments to discuss the format of the Estimates with their relevant departmental select committees. The Treasury returned to Parliament in early 1995 with further proposals, in the light of those discussions and their further work on resource accounting and budgeting, with the aim of revising the Estimates from 1996-97.

Background
Purpose of this report

5 The Comptroller and Auditor General has, in recent years, reported several times on government’s financial reporting to Parliament. The Committee of Public Accounts, and the Treasury and Civil Service Committee, also have a long-standing interest in the nature, form and content of government financial reporting. In recent years, the two Committees have reported on these matters on several occasions (see Appendix A). This report puts the Government’s proposed changes within the context of the Committees’ earlier interest and comments on the Government’s proposals, especially in those areas where the Green Paper asks for views.

6 In their 18th report of 1988-89, the Committee of Public Accounts laid out what they considered should be the main objectives of government financial reporting:

- providing Parliament, and departmental Select Committees in particular, with information which is reliable and sufficient as the basis for examination of departments’ performance in carrying out policies, functions, programmes and projects;

- providing Parliament with information which is reliable and sufficient as the basis for its consideration and approval of the levels of finance voted to services in the Appropriation Act (and the balance of allocation between services);

- ensuring department’s accountability by demonstrating their stewardship of the money voted by Parliament; and

- providing Parliament systematically with information on performance which is reliable as an assurance of the economy, efficiency and effectiveness with which departments are operating services and as the basis for selective enquiries.

7 This report focuses on whether the Green Paper proposals further these objectives. It also touches briefly on the extent to which resource accounts should help improve departments’ and Treasury’s financial management.

8 Debate over the form and content of public sector financial reporting is not confined to the United Kingdom. In drawing up the report note has been taken of international developments in this area. In particular the experience of countries that have already reformed their reporting and budgeting arrangements along similar lines (most notably New Zealand) has been examined, and also the recommendations of international bodies on standards for government financial reporting.

9 This report examines the Government’s plans for resource accounting (paragraphs 10-44), and reviews the possible implications of resource budgeting (paragraphs 45-66).
10 The Green Paper uses the term "resource accounting" to cover:

- a set of accruals-based techniques for accounting and reporting on the expenditure of UK central government; and

- a framework for analysing expenditure by departmental objectives, related to outputs wherever possible.

**Accruals accounting**

11 At present, government departments account on a cash basis, and moneys are brought to account at the time they are paid or received. This accounting convention is consistent with the arrangements whereby Parliament votes government departments' supply of funds in cash and with the Government's cash basis for planning. It is not necessarily the most informative way of presenting financial information however. With cash accounting, there is no requirement to match expenditure with revenues for the period to which they relate, and capital spending is brought to account wholly in the year in which the capital purchase or disposal is made. Cash-based accounts also lack any framework for accounting for assets and liabilities: once an asset is acquired, it effectively disappears from the accounts.

12 Accruals accounting, on the other hand, is a method of accounting which records expenditure and income in the accounting period to which they relate, including spreading the cost of capital items across their useful lives. It also introduces the concept of the Balance Sheet, which provides a snapshot of the assets, liabilities and net worth of an organisation at a given point in time.

13 Accruals accounting has already been adopted in most other parts of the public sector including the National Health Service, nationalised industries and local authorities. Within central government itself, departmental executive agencies and most executive non-departmental public bodies also account on an accruals basis. The Green Paper now proposes to apply accruals accounting to central government departments for the first time.

14 The introduction of accruals-based accounting should bring benefits for departmental management and, most likely, better accountability to Parliament. Whilst departments will have to incur additional costs to develop and implement new accounting systems, accruals accounting would:

- provide a better picture of the true cost of departments' activities, by taking into account all relevant costs including the use of assets, the costs of capital and non-cash costs, and relating these more directly to any revenues generated by those activities.

For many years, departments have produced unaudited and informal "memorandum trading accounts" to show the true cost of many activities where this was needed (for example, to demonstrate that fees recovered the full cost of providing a service). They do so by taking cash figures and
supplementing them by various adjustments and estimates. Under resource accounting, such information should be more readily available, and derive directly from the department's accounting systems.

The difference between cash and true cost will be most marked for activities where there are large asset holdings, acquisitions or disposals; or where there are significant disruptions to the pattern of income and expenditure such that one of them falls into a different accounting period.

- **improve stewardship and accounting for assets and liabilities**, by virtue of departments having to draw up a balance sheet for the first time. Government departments have always been required to maintain inventories of assets, although these were not valued. And since 1993, the Treasury have encouraged departments to publish information on the value and make-up of their asset holdings, although few have done so. At present, departmental Appropriation Accounts provide no details of asset use or holding.

Resource accounting will require that departmental assets are valued, recorded, charged for and reported. This discipline should promote and facilitate good stewardship on behalf of departments, both to justify their use of assets and their retention. Similar arguments apply to liabilities.

In addition, the Committee of Public Accounts have called for improved information on departments' holdings, deployment, stewardship and control of assets, for example in their 8th report of 1986-87. The proposed reforms should go a long way to provide the improved information the Committee sought.

15 In the first instance, most of these benefits will accrue to departments themselves and to the Treasury in their role as the financial managers of government. Improved information on costs and assets will encourage better stewardship and better decision-making. However, this improved information should also facilitate better financial reporting to Parliament, if this information is made available to them in a suitable form.

### Matching resources to objectives and outputs

16 A second feature of resource accounting is the attempt to match resources used to departmental objectives, relating them to outputs wherever possible. The Treasury currently propose that departments will be required to produce and publish as part of their accounts:

- a schedule showing the cost of resources consumed, by main objectives; and

- a schedule analysing output and performance against each main objective.
These proposals mark a continuation of a trend which has been evident over many years:

- since 1982, and the Financial Management Initiative, departments have been encouraged to produce better information on the objectives, outputs, and performance of their activities and functions - to help them manage their resources better and to improve reporting on their performance;

- The Committee of Public Accounts has consistently sought improved information for Parliament on departments' aims and objectives and links with actual performance and outturn. An increasing volume of such information has been introduced into departmental annual reports, although it is not yet comprehensive and is of variable quality;

- departmental executive agencies are required to publish in their annual report information on their financial performance, efficiency and effectiveness, and to measure their performance against the targets set by that parent department; and

- Parliament has also expressed a preference to see Estimates, and therefore Appropriation Accounts, in a form whereby expenditure is shown against the objectives or objects of expenditure (for example, fisheries protection, or the roads programme) rather than the subjects of expenditure (for example, pay or computers or stationery). In many current Estimates and Accounts, expenditure is already brigaded in this way, although by structuring the Estimate around the major programmes of expenditure rather than by direct reference to the objectives of expenditure.

The accounting statements suggested by Treasury would for the first time provide a systematic and consistent presentation of the objectives of departmental expenditure and of departments' achievements against those objectives. No doubt, some departments will be more successful than others at providing such information. And some departments will have greater difficulty in developing meaningful measures of output and achievement. Nonetheless, the integration of performance information with financial statements would help standardise their presentation, provide a stronger incentive to come up with measures, strengthen the linkages between cost and performance information, and help Parliament focus on cost and achievement.

Setting accounting policies and standards

To meet the objectives in paragraph 6, financial statements need to be produced within a set of principles and rules which ensure that information is presented in a consistent manner which is understandable and meets the needs of the users of the statements. For example, in the private sector, companies are required to prepare accounts in accordance with accounting standards which aim to ensure that the accounts provide a true and fair view of their financial performance and standing. Without such a framework, financial statements are open to manipulation and can mislead rather than inform their users. Such a framework is more important for accruals accounts, which require the preparer
to make more judgements and estimates than is the case for cash accounts. Standards are necessary to govern these judgements and to provide an agreed benchmark against which the auditor can examine them; and so that the reader of the accounts can know the basis on which they have been prepared.

20 The Green Paper proposes that the resource accounts should follow UK Generally Accepted Accounting Practice, which the Treasury define as the accounting and disclosure requirements of the Companies Act 1985 and accounting standards (issued or adopted by the Accounting Standards Board) supplemented by accumulated professional judgement. This body of practice and standards is aimed primarily at the private sector. Government policy is to require the accruals accounts of public sector bodies to comply with these requirements, except where in the particular circumstances of the public sector bodies concerned the Government considers them to be inappropriate or others to be more appropriate.

21 The Green Paper recognises that this body of practice may need to be supplemented to develop a framework particularly suited to the requirements of central government. This mirrors the position in other parts of the public and not-for-profit sector, where Generally Accepted Accounting Practice is supplemented by specific requirements for that sector. The Treasury plan to produce a resource accounting reference manual, for use by all departments. So that this manual meets the needs of the preparers and auditors of financial statements, the Treasury intend that it will point out departures from Generally Accepted Accounting Practice and spell out the underlying principles and purposes of government financial reporting.

22 Where there are departures from or additions to Generally Accepted Accounting Practice, there is the question of how any accounting requirements peculiar to central government should be determined. It would be inappropriate for those responsible for preparing financial statements to have the sole responsibility for deciding on the standards such statements should follow.

23 Clearly the Treasury should have a major role in the development of accounting requirements specific to central government. However, Parliament and other users of the accounts, auditors and professional bodies should also play a part in the setting of these requirements. And, since such accounts may become the means of demonstrating that departments have complied with the Appropriation Act, it is particularly important that Parliament should have a say. In Canada, the United States and Australia, the arrangements provide for an independent body to oversee and approve central government accounting standards.

24 In addition, the Treasury should continue to seek Parliament's agreement to accounting standards and practices for central government, which by tradition they have done by consulting the Committee of Public Accounts and the Treasury and Civil Service Committee.
25 The Green Paper sought views on some specific and technical accounting issues, such as capital charging, accounting for government’s long term liabilities such as pensions, and the valuation of military, heritage and infrastructure assets. The National Audit Office are discussing these issues, and other more detailed accounting matters, with the Treasury.

Boundaries of resource accounts

26 The Treasury propose that the reporting entity (that is, the accounting boundary) for resource accounts will be broadly defined as the department and the responsibilities of the Principal Accounting Officer. Each departmental resource account will therefore encompass the core department, together with the associated Next Steps Agencies and Trading Funds. However, it will exclude other organisations with close financial and operational links to the department, in particular non-departmental public bodies. The coverage of resource accounts will not extend to central accounts such as the Consolidated Fund and the National Loans Fund.

27 The Treasury propose to exclude non-departmental public bodies from resource accounts because they are constitutionally independent from their sponsoring department. There would also be practical difficulties in consolidating accounting information from the large number and range of bodies involved, some of which will not have the requisite accounting systems to provide accruals-based data.

28 However, non-departmental public bodies are an important part of central government, and handle a considerable proportion of the moneys voted by Parliament to departments. They in turn may pass on this funding to other bodies. For example, of the £13 billion voted to the Department for Education, about £7 billion is actually spent by non-departmental public bodies.

29 The activities of non-departmental public bodies are clearly linked to departmental aims, much of their income comes from their sponsoring department, they may hold substantial assets purchased from government funds, and the sponsoring department often exercises a significant influence over their activities and management. They may incur liabilities which the taxpayer may have to meet eventually, even where the body has limited liability.

30 Thus, if the assets, liabilities and operations of non-departmental bodies are excluded from departmental resource accounts, the accounts will need to identify clearly the bodies sponsored by the department and include relevant information about them. The notes to the accounts should disclose, as a minimum, the extent to which those bodies relied upon income from the department - both in absolute terms and as a proportion of their total income - and what has been achieved with such expenditure. In this way, the departmental resource account will provide, for Parliament and others, a more complete picture of departments’ expenditures and activities and a clearer link through to the accounts of these sponsored bodies.
Whole government accounts

31 The Government does not favour producing a single account which consolidates or aggregates individual departmental resource accounts. A simple consolidation along these lines may be of little value, given that these individual accounts are narrowly drawn. Furthermore it is not clear that such a consolidation would result in a meaningful accounting entity, since it would not equate to or represent any of the usual bases for describing government activity, that is central government, general government, or the wider public sector.

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32 However, there is public and Parliamentary interest in “whole government accounts” bringing together the income and expenditure, and assets and liabilities of central government. This might be done by building on the information currently contained in the National Loans Fund Accounts, the Consolidated Fund Account and supporting statements. Although there would be no particular benefits for departments themselves, an audited consolidated account on an accruals basis would allow the public and Parliament to see clearly how taxes have been spent, and the assets and the liabilities held on their behalf by central government. Some countries, for example New Zealand and Canada, already produce such accounts and others, for example the United States and Australia, are considering the potential benefits.

33 There may be practical difficulties in producing such an account at this stage. Departments and Treasury will be fully occupied for the next few years with implementing resource accounts. Nevertheless, whole government accounts should be considered once resource accounting has been implemented.

Format of accounts

34 For resource accounts to be of benefit to Parliament, it will be essential that they provide the information Parliament needs in a format which is clear and logical. However, resource accounts cannot be expected to provide all the information Parliament needs: much of the supporting detail, especially detailed data and commentary on objectives and performance, will be found in the departmental annual report. Nonetheless, resource accounts should provide a financial overview, key information, and pointers to the relevant sections of the annual report.

35 The Green Paper proposes that departmental resource accounts should comprise five statements and supporting notes:

- three standard financial statements, referred to as schedules A-C, which follow closely the presentation prescribed for companies - an operating cost statement, balance sheet and cash flow statement; and

- two supplementary statements - a main objectives analysis (schedule D) which will be compulsory, and an output and performance analysis (schedule E) which departments will be strongly encouraged but not required to produce.
Taken together these five statements go a long way towards meeting the needs of Parliament:

- schedules A and D together provide information on how money is spent and the purposes for which it was spent;

- schedule B shows departmental asset holdings, and Parliament's accumulated investment in departments;

- schedule C shows how activity has been financed, and in particular will provide the basis for reconciliation to the amount drawn from Voted sums; and

- schedule E shows departments' performance against objectives.

To make the statements understandable the examples given in the Green Paper are in a highly summarised form. The Treasury recognise that supporting detail will need to be included in the notes to the accounts. Some further detail will be required on the face of the statements. In particular:

- the statements should distinguish between the activities of the core department and its agencies, particularly as the resource account will most likely be the only account for the core department;

- agencies and trading funds should continue to provide separate annual reports and accounts, since it would be difficult to convey sufficient information about each agency, many of which will be major undertakings in their own right, within the confines of a departmental resource account; and

- although the eventual relationship between resource accounts and Appropriation Accounts has not been made clear, it would be sensible to begin from the premiss that resource accounts should distinguish clearly those figures which were voted by Parliament.

Whilst the specimen schedules in the Green Paper give a broad indication of what resource accounts will show, it would nonetheless be helpful to Parliament and to others if the Treasury were to produce a full set of resource accounts for a single department, if necessary using fictitious data, as soon as possible. This would help assure Parliament that the accounts will convey all the information they wish to see, in a format they can understand.

Scope of the audit

The Green Paper proposes that resource accounts should be audited, and that the Comptroller and Auditor General should carry out this audit on behalf of Parliament. This reflects the importance of resource accounts to public and Parliamentary accountability, and the constitutional role of the Comptroller and Auditor General as Parliament's auditor.
39 The Operating Cost Statement, Cash Flow and Balance Sheet are standard financial statements akin to those used in the private sector and for many public bodies which follow commercial accounting standards. It should be possible to give resource accounts a normal "true and fair" opinion, once appropriate requirements for government accounting have been developed. As is currently the case with Appropriation Accounts, this opinion would need to be supplemented by an explicit statement on the regularity of transactions, confirming that they are in compliance with legislation, Parliamentary, Treasury and other relevant authorities.

40 Schedule D provides a breakdown of a department's expenditure against its main objectives, and as such is critical to a full understanding of performance and stewardship. The schedule also provides the most direct link to the purposes of expenditure, the basis on which Parliament votes funds. For Parliament to have independent assurance that departments have used moneys voted to them for the purposes intended, this schedule should be covered by the Comptroller and Auditor General's audit opinion.

41 Schedule E to each resource account will show the department's performance against some key output targets, both financial and non-financial. At present, departments' performance targets and achievement are included in their annual reports but these are not independently validated.

42 The introduction of resource accounts provides the opportunity for Parliament to consider whether they would welcome some external validation of departmental performance data. There are a number of considerations:

- although not all departmental programmes and activities lend themselves to simple quantification of performance, the last 15 years have seen great improvements in public sector performance measurement and the coverage and quality of performance data. And departments should be able to draw on the progress already made, for example by executive agencies and the NHS. Resource accounting should bring further improvements in performance measurement;

- performance data have become increasingly important to Parliament's oversight of departments, and the new Schedule E will be crucial in Parliament in gaining a clear and high level understanding of what has been achieved with departmental resources and voted moneys. As performance data increases in importance and its presentation becomes more systematic - which should be evident by 1999-2000 when resource accounts are published for the first time - the case for validation becomes stronger;

- the National Audit Office already have access to departments' performance data and can review its relevance and accuracy, within the scope of their value for money examinations; and

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- as the Committee of Public Accounts have already recommended, it would be desirable to establish ground rules to govern the admissibility of performance data, for example as to consistency, so that public bodies cannot pick and choose
between performance indicators from one year to another; as to relevance, so that Parliament can quickly see that performance information is central to a body's activities; and as to reliability, so that Parliament can be assured that performance data is materially accurate.

Initially, departments might find it difficult to produce performance data to a standard which could earn a formal audit opinion of the sort which applies to the main financial accounts. Such an opinion should be achievable, however, as the quality of departments' performance information continues to improve.

Dry run accounts and audit

43 The Treasury propose that departments will prepare unpublished accounts in 1998-99, and that these accounts will be audited by the Comptroller and Auditor General. The first set of audited and published accounts would be for the year 1999-2000.

44 Dry run accounts and audit in 1998-99 will be a very sensible step. The National Audit Office's experience of Next Steps agencies has proved that a dry run audit can be of immense assistance to both departments and auditors, to help ensure that accounting systems are capable of producing auditable accounts and that new accounts will not automatically attract an adverse audit opinion. The National Audit Office are already providing advice and assistance to departments, and if individual departments wish to bring forward their dry run, the Office will help them meet a faster timetable.

Resource budgeting

Introduction

45 The Green Paper uses the term "resource budgeting" to cover the extension of resource accounting principles and practices into the processes by which public expenditure is planned and controlled (the Public Expenditure Survey) and by which moneys are voted by and accounted to Parliament (the Supply procedures). If carried forward, resource budgeting may require changes to the legislation relating to Supply procedures and the Estimates and Appropriation Accounts.

46 This report concentrates on the potential implications of resource budgeting on Supply procedures, the prime vehicle for Parliamentary control and accountability, rather than the Public Expenditure Survey, which is an internal mechanism of control within government.

47 The Green Paper provides no details as to how a resource based Supply system might operate. Instead, the Government invites suggestions and the Treasury intend to come forward with further proposals after the consultation period has finished at the end of January 1995. The Comptroller and Auditor General will provide further and more specific comments to Parliament after those detailed proposals are published. It is possible to provide general comments at this stage, however, having regard to the objectives of financial reporting to Parliament described in paragraph 6. These are set out overleaf.
Resource-based Supply

48 It would be possible for departments to adopt resource accounting without changing any Public Expenditure Survey or Supply procedures. The Green Paper recognises too that it would be technically possible to run the Public Expenditure Survey on a resource basis and to maintain the Supply system in cash terms. However, the Government believes that there is a strong argument for Parliamentary systems of voting expenditure to be closely aligned with the government's own systems for planning, controlling and accounting.

49 Running the systems on the same basis, with a resource-based Supply process, could:

- provide a stronger link between the basis of Parliamentary approval and the way departments budget and manage their affairs; and

- avoid the need for departments to run two sets of accounts and two control systems: one for intra-government control and one for Parliament.

However, the full implications of such a change for Parliament will need to be considered after the Treasury produce more detailed proposals.

Existing Supply procedures

50 Parliament will want to consider carefully whether the detailed proposals which the Treasury bring forward preserve Parliamentary control and authority.

The purposes of expenditure

51 It is a feature of Parliamentary authority that Parliament approves expenditure for specific purposes and that a sum appropriated to a specific service cannot be used for another service. Each Estimate presented to Parliament is divided into two parts:

- Part I specifies the services and purposes for which the Estimate is presented (the ambit of the Vote). Part I of the Estimate, which together with the total of Appropriations in Aid in the Part II Summary is reproduced in the Appropriation Act, is of prime importance since it provides the statutory description in that Act of the purpose for which the Supply is granted; and

- Part II shows the subheads under which the Treasury requires the expenditure to be accounted for; and provides formal information on individual services for Parliament's scrutiny. Treasury may exercise their powers of virement as to the allocation of grant between the various subheads of the service in question.

52 Under these arrangements, it is necessary to have a clear description of the services to be covered by an Estimate, in order that there may be no question whether the exercise of virement in any given case is or is not in accordance
with the terms of the Parliamentary grant (as expressed in the Appropriation Act) or with the intentions of Parliament (as deduced from the terms of Part II of the Estimates).

53 This feature can also be seen in respect of new services. Where departments require funds for a new service not covered by the ambit of the Vote, they must present a Supplementary Estimate to seek new Parliamentary authority for this expenditure, even if the new service can be accommodated within existing voted sums. Parliament has previously expressed a wish for services which are large or novel or contentious or which, while small at the outset, involve heavy liabilities in future years, to be brought to their attention in this way.

54 It will be essential that under any new arrangements Parliament votes moneys for purposes which are evident on the face of the Estimates and accounts, and that Treasury exercise discretion to vire between services so long as they are consistent with those purposes. Under the Treasury’s current proposals for simplified Estimates, their powers of virement would be exercised at a higher level than at present: departments would only need to obtain Treasury approval to vire provision between Estimates lines (broadly equivalent to Sections in the current Estimates) or into running costs, rather than between Subheads as they do at present.

55 However, at present many departments have more than one Vote. The number of Votes is expected to fall in 1995-96, from 163 to around 130, when departments will be permitted to mix cash-limited and non cash-limited expenditure on a single Vote. In addition, the advent of one resource account per department could be accompanied by one Vote per department, reducing the number of Votes to around 60.

56 Depending upon the detailed arrangements, Parliamentary authority could be exercised at a higher level than at present, in 60 large blocks of votable expenditure, compared with the current 165. This will give departments greater freedom to manage within their voted totals. And new arrangements on virement (see paragraph 54) will mean that departments will have fewer occasions on which they must return to the Treasury for virement approval.

57 This would represent a radical shift in the level of Parliamentary and Treasury authority and in the degree of delegation to departments. Parliament will wish to consider whether they would be content to exercise their authority at Vote level, particularly if there is a move to one Vote per department, or would prefer to control major components of departmental plans - for example, by voting the main programme totals currently shown at “Section” level within each Vote in the current Estimates, or Estimate lines in the new format now proposed by Treasury.
Voted sums must not be exceeded

58 Departments cannot exceed the sums authorised in the Appropriation Act without seeking Parliamentary authority in one of two ways:

- if known in advance, departments are required to present a Revised or Supplementary Estimate for the additional provision; or

- otherwise, departments must present an Excess Vote to Parliament which is authorised in a subsequent Appropriation Act. In this case, the departmental Appropriation Account includes a report by the Comptroller and Auditor General on the reasons for the excess.

59 There is considerable room for discussion and debate about whether Parliamentary authority should focus on voting resources or cash under a resource budgeting system. But whichever is adopted, the new arrangements should preserve the principle that there should be a limit to the resources or cash authorised by Parliament, and that departments must return to Parliament for further authority, wherever possible in advance. And they should recognise the greater incidence of judgements and approximations in resource budgets and accounts when compared with cash, and ensure that it is possible to match what Parliament has voted with what departments have accounted for.

60 At present, one feature of Parliament's placing of limits on expenditure is that it not only authorises the net amount of expenditure on a Vote but also the amount of receipts it can raise to off-set against costs, thereby controlling gross expenditure. These offsetting receipts are known as "appropriations-in-aid". Income raised in excess of the amounts authorised has to be surrendered to the Consolidated Fund. This is an important control, since it ensures that departments may not raise and dispose of large sums of money without the authority of Parliament. Parliament will wish to see that this principle is carried forward into the new arrangements.

Annuality

61 Under current Supply rules, the sums authorised by Parliament are only available in the financial year for which they are appropriated. The Estimates show only the cash sums expected to come in course of payment during the year to which they relate, and moneys remaining unused by departments at the end of the year have to be surrendered to the Consolidated fund.

62 Annual appropriation ensures that departmental expenditure is subject to regular Parliamentary review and authorisation. The strict application of annuity to Supply has been criticised as the cause of inefficient planning, particularly of long-term projects and end-year spending sprees to use up unspent funds. Since 1983 Treasury have operated a number of schemes to allow departments to carry forward underspends to subsequent years, to provide departments with flexibility, but only in strictly defined circumstances. The Treasury now operate 100 per cent end year flexibility in respect of running
costs. However, full annual Parliamentary authority has been maintained by the requirement for departments to include in the subsequent year's Estimate any money carried forward in this way.

63 Parliament will wish to consider whether the Treasury's proposals for resource budgeting will entail further adjustments in the application of annuality in order to secure improved arrangements. Any changes must of course be consistent with Parliament's overall authority.

The way forward

64 Existing procedures were designed or evolved for a cash-based system of Supply. A well-designed resource or accruals-based system of Supply could in principle provide equivalent, or possibly, higher levels of Parliamentary oversight. The Green Paper makes clear that the Treasury have no intention of losing sight of cash, and that they will exercise a cash management function, albeit at a higher level than at present. If the Treasury can develop a workable system of cash and resource control for their own and departments' use, it should be possible to use this as the basis for an effective system of Parliamentary Supply.

65 The Green Paper does not provide sufficient detail to judge whether this will be the case. The Paper puts forward the possibility that Estimates under a resource-based system might be based on the resource accounting formats outlined in the Paper. However, it is not clear which parts of these formats would constitute information for Parliament and which parts the House would be asked formally to vote on and appear in the Appropriation Act. The Treasury's more detailed proposals will need to make this clear.

66 One of the difficulties for Parliament has been to track expenditure from one document to another, particularly between the Estimates and departmental annual reports, although there have been significant improvements in articulating the linkages between them, and one aim of the current proposals for Estimates reform is to simplify these linkages. There are basic difficulties in current model, however, in that each departmental annual report in February is both prospective (to justify the Estimate) and retrospective (to reflect on past performance), and it is separate from both the Estimates and the Appropriation Accounts to which it relates. The introduction of resource budgeting would provide an opportunity to reappraise the options for financial reporting by departments. One option would be to move to:

- a departmental plan in February containing a resource budget including the Estimates; and

- an annual departmental report in October containing the resource account and Appropriation Account.

This would allow the plan to focus on what is truly new, and on the justification for expenditure, and the annual report to be associated directly with the department's latest accounts and performance data.
The main conclusions of this report are:

- From Parliament's point of view, the Green Paper proposals should be judged by the extent to which they provide Parliament with improved information for its consideration and approval of the sums it votes to services and its examination of departments' performance in operating those services (paragraphs 5-7);

On resource accounting

- Accruals accounting should bring benefits for departmental management, by providing a better picture of the true costs of their activities and by improving the accounting and stewardship of assets and liabilities (paragraph 14);

- This improved information should also facilitate better financial reporting to Parliament, if it is made available to them in a suitable form (paragraph 15);

- The accounting statements proposed by Treasury should provide a systematic and consistent presentation of the objectives of departmental expenditure and of achievements against those objectives, as sought by previous Committees (paragraphs 17-18);

- The proposed resource accounting manual for departments will include or point out departures from Generally Accepted Accounting Practice and spell out the underlying principles and purposes of government financial reporting. It would be inappropriate for those responsible for preparing financial statements to have the sole responsibility for deciding on the standards such statements should follow (paragraphs 19-22);

- Parliament and other users of the accounts, auditors and professional bodies should also play a part in setting these accounting requirements, and the Treasury should continue to seek Parliamentary agreement to changes in accounting standards and practices (paragraphs 23-24);

- If non-departmental public bodies are excluded from departmental resource accounts, the notes to accounts should identify the bodies supported by the department and the extent to which those bodies depend on departmental funding, and what has been achieved with such expenditure (paragraphs 26-30);

- A simple consolidation of departmental resource accounts may be of little value. But there is Parliamentary and public interest in a whole government account which brings together the income and expenditure, and the assets and liabilities, of central government. Some countries already produce such accounts and others are considering the potential benefits (paragraphs 31-33);
the accounting statements proposed by Treasury go a long way to meeting the needs of Parliament, but they need to distinguish the activities of the core department and its agencies; and distinguish clearly those figures voted by Parliament (paragraphs 34-37);

the Green Paper proposes that resource accounts should be audited by the Comptroller and Auditor General. Extending this audit to the statement of expenditure against main objectives would demonstrate that funds had been spent in line with Parliament's intentions (paragraphs 38-40);

information on performance targets and achievements have become increasingly important to Parliament's consideration of Departmental performance. As the Committee of Public Accounts have recommended, it will be important to establish ground rules to govern the admissibility of performance data; and the Comptroller and Auditor General could assist in delivering this objective (paragraphs 41-42);

the Treasury's intention that there will be a dry run account and audit before the first year of published accounts is welcome. The National Audit Office are already providing advice and assistance to departments, and if individual departments wish to bring forward their dry run, the Office will help them meet a faster timetable (paragraphs 43-44);

On resource budgeting

there would be potential advantage in aligning Parliament's procedures for voting and scrutinising expenditure with the government's own systems for planning, controlling and accounting for their expenditure. However, Parliamentary consideration will need to await Treasury's more detailed proposals (paragraphs 48-49);

any new system of Supply should preserve the fundamental principles of the existing system - that Parliament votes money for purposes which are evident on the face of the Estimates and accounts; that Parliament places limits on sums that can be spent, both gross and net; and that there should be controls over unused funds or resources at the end of each year (paragraphs 50-63);

the Green Paper makes clear that the Treasury will control both cash and resources used by departments, although cash control will be at a higher level than hitherto. It must therefore be possible to devise similar Parliamentary controls over cash and resources, at the same or a higher level than exercised by Treasury (paragraph 64);

the reforms offer the opportunity to rationalise financial reporting to Parliament. One option would be to move to two key documents - a departmental plan containing a resource budget including the Estimates, and an annual departmental report containing the resource account and Appropriation Account (paragraph 66).
Appendix A

Financial reporting to Parliament: Conclusions and recommendations from previous Committees of Public Accounts and Treasury and Civil Service Committees

<table>
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<th>Committees of Public Accounts</th>
<th>Main conclusions and recommendations</th>
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<td>Report</td>
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<td>Financial Reporting to Parliament (6th Report of 1986-87, HC 98)</td>
<td>The Committee took evidence on the Comptroller and Auditor General's report &quot;Financial Reporting to Parliament&quot; (HC576 of 1985-86). The Committee called for improved information on the aims and objectives of departmental expenditure, and for this information being adequately linked with out-turn information. It also called for improved information on the deployment, stewardship and control of departmental assets. They also suggested that Appropriation Accounts should be included within Departmental Annual Reports.</td>
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<td>Central Funds and Accountability and the Exchange Equalisation Account (8th Report of 1989-90, HC 267)</td>
<td>The Committee noted that it would be willing to accept less detail if information of greater value was included. It called for Parliamentary approval of Supply to be based more directly on more informative Estimates published earlier, or in some other document tailored more specifically to Parliament's needs.</td>
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<td>Financial Reporting to Parliament (18th Report of 1988-89, HC 354)</td>
<td>The Committee considered two memoranda from the Comptroller and Auditor General. On &quot;Whole Government Accounts&quot;, the Committee called for a clearer and more informative presentation of the relationships between the Central Funds and the Central Government Borrowing Requirement. Following a memorandum from the Comptroller and Auditor General, the Committee noted that Parliamentary scrutiny of government spending plans could be impaired if alignment of information in Estimates and Departmental Annual Reports was unclear, or if important detail was lost from the Estimates or if the current level of detail provided by Vote subheads was lost.</td>
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Treasury and Civil Service Committees

Report

The Form of the Estimates (6th Report of 1980-81, HC 325)

Efficiency and Effectiveness in the Civil Service
(3rd Report of 1981-82, HC 236)

The Structure and Form of Financial Documents presented to
Parliament (2nd, 7th & 10th Reports of 1984-85, HC 110, 322 & 544)


The Form of the Estimates; The Government's Response to the
3rd Special Report of 1993-94, HC 441)

Main conclusions and recommendations

The Committee noted that any reform of Parliamentary procedures with
the object of exercising a more satisfactory control of Supply would
require Estimates to be presented in a form that Parliament wants.

On financial reporting, the Committee called for departments to account
for the resources used and results achieved in relation to objectives and
targets. On the Estimates, the Committee called for more detailed
information on targets and outputs.

On the Estimates, the Committee called for a redesign of the documents
to enable their information content to be clearly distinguished from their
role as instruments for operating Parliamentary Supply procedures.

On the Estimates, the Committee called for clear alignment with the
Departmental Annual Reports and for the latter to contain a summary of
the relevant Estimates.

The Committee noted the principle that it is a duty of Government to
ensure that Parliament is provided with data so that it can properly
exercise its oversight and control functions even though this may
involve Government in compiling and providing data which is not
strictly required for the Government's own purposes. On the Estimates,
the Committee was unwilling to authorise further diminution in the
amount of information contained in the Estimates unless there was
certainty that alternative arrangements for the presentation of this
information were satisfactory.