

19 August 2014

**GOVERNMENT FINANCIAL REPORTING
MANUAL (FReM) EXPOSURE DRAFT No:**

(14)02

**EXPOSURE DRAFT OF PROPOSED
AMENDMENTS TO THE FReM**

**Implementation of the Simplifying and
Streamlining Accounts project**

Comments to be received by 13 October 2014



HM TREASURY

GOVERNMENT FINANCIAL REPORTING TEAM HM TREASURY

This exposure draft of proposed amendments to the Government Financial Reporting Manual (FReM) is published by HM Treasury for comment only. The proposals may be modified in the light of comments received in this consultation process before being presented to the Financial Reporting Advisory Board for its approval. Final proposals approved by the Financial Reporting Advisory Board will be published as amendments to the FReM from the proposed effective date.

Comments on this exposure draft should be submitted in writing so as to be received by 13 October 2014. Respondents are asked to send their comments electronically to FReM.consultation@hm-treasury.gov.uk.

All responses may be published on the FReM website unless the respondent requests confidentiality.



HM TREASURY

PROPOSED AMENDMENTS TO THE GOVERNMENT FINANCIAL REPORTING MANUAL (FReM)

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Proposed amendments to the FReM

Introduction

The Government Financial Reporting team, HM Treasury, has published this exposure draft of proposed amendments to the Government Financial Reporting Manual (FReM) as part of its ongoing work in ensuring that the Manual reflects the latest developments in government financial reporting.

HM Treasury launched the Simplifying and Streamlining Accounts project (the Project) in April 2013 with the aim of simplifying and streamlining the presentation of the statutory annual reports and accounts produced by central government entities so as to better meet the needs of users. This exposure draft details the proposed changes to the 2015-16 FReM as a result of the project.

Structure of exposure draft

The exposure draft includes a section for each FReM chapter for which an amendment is proposed. Each section includes:

- (a) An explanation of why the amendment is proposed.
- (b) When necessary, any specific additional question unique to that proposed amendment;
- (c) The paragraphs of the FReM chapter that are affected by the proposed amendment;
- (d) The proposed effective date of each proposed amendment.

Invitation to comment

HM Treasury invites comments on the proposed amendments. It would particularly welcome answers to the questions set out below. Comments are most helpful if they:

- (a) Answer the question as stated;
- (b) Indicate the specific paragraph or paragraphs to which they relate;
- (c) Contain a clear rationale; and
- (d) Describe any alternative HM Treasury should consider.

HM Treasury will consider all comments received in writing by 13 October 2014. In considering the comments, HM Treasury will base its conclusions on the merits of the arguments for and against each alternative, not on the number of responses supporting each alternative.

Executive Summary

1. This exposure draft seeks views on the proposed amendments to the FReM arising from the Simplifying and Streamlining Accounts project (the Project).

2. Since the introduction of resource accounting and budgeting, HM Treasury has attempted to meet the needs of users of central government annual reports and accounts by applying private sector reporting requirements to entities - with some adaptations made for the public sector context in which they operate. Over a number of years additional requirements have also been included at the request of Parliament and other central government departments in an ad-hoc manner. This has led to an annual report and accounts that is effectively:

- (i) A front-half annual report based on private sector Companies Act requirements with a large number of additional mandatory disclosures; and
- (ii) A back half containing a set of financial statements based on International Financial Reporting Standards (IFRS) as adapted for the public sector context plus the addition of the Statement of Parliamentary Supply.

3. The key findings from the Project have highlighted that user needs are not being met by the current reporting arrangements, in particular that it is hard to link the performance narrative to the figures in the accounts. As such the high level recommendations developed in late 2013 proposed a restructuring of the traditional ‘front-half’ annual report and ‘back-half’ financial statements into three more integrated reporting requirements based on:

- (i) **Performance** – The purpose of the performance section is to “tell the story” of the reporting entity. 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 annual report accounts is integrated to provide a cohesive document.
- (ii) **Accountability** – The purpose of this section is to meet key accountability requirements to Parliament stemming from the fact that it is the primary user of the annual report and accounts. It is also the section that departments will use to demonstrate compliance with norms and specific codes of good corporate governance.
- (iii) **Financial statements** – The evidence gathered during Project has highlighted that that a set of financial statements audited by the NAO remains important to users, and that users want to see better integration between the financial information presented and wider entity performance. The Project also provided a significant amount of evidence, however, that that the concept of materiality is poorly understood and inconsistently applied and that the usefulness of financial statements could be improved through more robust application of materiality.

4. This exposure draft seeks your views on the conclusions reached, and on the proposed amendments to the FReM arising from these conclusions.

Questions

Question 1

Do you agree with HM Treasury's proposal to amend the FReM to implement recommendations from the Simplifying and Streamlining Accounts project as described in the exposure draft? If not, why not, and what alternative do you propose?

Question 2

Do you agree with the proposed effective date for the proposed amendments? If not, why not, and what alternative do you propose?

Background to the Simplifying and Streamlining Accounts Project

1. HM Treasury launched the Project in April 2013 with the aim of simplifying and streamlining the presentation of the statutory annual reports and accounts produced by central government entities so as to better meet the needs of users.
2. Between April 2013 and October 2013, HM Treasury conducted a review of the current annual report and accounts requirements and documents that are produced under existing guidance, undertook a significant amount of outreach work with users, potential users, and preparers of the annual report and accounts, and reviewed private and public sector best practice worldwide. A public consultation was also launched to engage with as wide a range of users and potential users as possible.
3. The key findings from this review and outreach work were:
 - Accountability remains the primary objective of financial reporting in central government, with users interested in how much was spent against budgets and Estimates and how entities are accountable to Parliament.
 - Users place a strong emphasis on the inclusion of audited financial information but increasingly they are also interested in longer-term trends of expenditure and wider performance against objectives.
 - Current reporting is viewed as difficult to navigate and a coherent narrative message is often lacking. This is exacerbated by an overly cautious approach to applying materiality to limit disclosures and a perceived inconsistency between the various different central guidance documents produced for preparers.
 - These issues are not limited to the public sector. A healthy “cutting clutter” debate is taking place in the private sector following a recognition that mandatory requirements for a mass of detail is obscuring the ‘big picture’ and limiting the usefulness of ARA.
4. In addition to the core accountability function that financial reporting fulfils, the Project also highlighted that the development of the Whole of Government Accounts (WGA) and Clear Line of Sight reforms have had a significant positive impact on the usefulness of financial reporting for decision-making purposes. The further integration of performance and financial information is essential to improvements in wider financial management, as recognised in the recent Review of Financial Management in Government¹. Increasing the usefulness of the annual report and accounts for decision-making has also, therefore, been a central aim of the project.

¹https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/209220/strengthening_financial_management_capability_in_government.pdf

Recommendations of the Project²

5. The high level recommendations from the project proposed a restructuring of the traditional ‘front-half’ annual report and ‘back-half’ financial statements into three more integrated reporting requirements based on:

- Performance – “telling the story”
- Accountability; and
- Financial statements

Performance – “telling the story”

6. The performance “telling the story” reporting requirement was proposed in order to meet user criticisms that annual reports and accounts lack an overall narrative and are difficult to understand. HM Treasury’s recommendation to address this problem is to introduce a number of high-level structural elements which aim to improve comparability across departments while providing flexibility for entities to tell their own story about their key activities and outcomes during the financial year. These elements are:

- Clear statement of the purpose and activities of the organisation;
- High level financial information with cross references to the audited accounts;
- Trend information based upon segmental/management information data;
- Commentary against trends and performance against policy; and
- Expected future policy changes

Accountability

7. The “accountability” reporting requirement was proposed because the primary user of the annual report and accounts is Parliament, and there are a number of key accountability requirements resulting from this that must be met and be seen to be met. HM Treasury’s proposal is for a distinct accountability section to be included in the annual report and accounts containing core corporate information including:

- The Governance Statement and information on strategic risks to the entity;
- The remuneration report; and
- Information on Parliamentary accountability – including the Statement of Parliamentary Supply.

Financial statements

² Full recommendations can be found at <https://www.gov.uk/government/consultations/central-government-annual-reports-and-accounts-consultation-on-simplifying-and-streamlining-the-presentation-of-annual-reports-and-accounts>

8. Finally, evidence gathered during the project affirmed that users greatly valued receiving a set of financial statements and disclosure notes that the National Audit Office has audited to international standards of audit. The Project also highlighted, however, significant evidence that the concept of materiality was poorly understood and inconsistently applied, with a checklist approach being taken for the inclusion of information rather than a proper consideration of user needs. While materiality in the public sector is a broad concept encompassing the nature and context of items and economic events as well as monetary value, this checklist approach has meant that information is often included in the annual report and accounts that has little or no value. HM Treasury therefore proposes a final requirement for the annual report and accounts to include:

- Audited financial statements; and
- Disclosure notes for material balances only.

9. As with the other reporting requirements noted, HM Treasury's view was that financial information should be better integrated with other reporting throughout the ARA, rather than being seen as a distinct standalone reporting element.

FReM chapters addressed

The following table shows the topics addressed by these proposed amendments.

FReM Chapter	Subject of amendment
Chapter 3, <i>Parliamentary accountability</i>	Notes to the Statement of Parliamentary Supply
Chapter 5, <i>Form and content of the annual report and accounts</i>	Substantial amendments throughout the chapter to reflect changes to the annual report and accounts as a result of the Project

Proposed amendment to Government Financial Reporting Manual Chapter 3, *Parliamentary accountability*

Introduction

An amendment to Chapter 3, *Parliamentary accountability*, is proposed.

Why the amendment is proposed

The amendment is proposed to reduce the number of mandatory notes to the Statement of Parliamentary Supply and to group together other disclosures from elsewhere in the FReM which relate to Parliamentary accountability.

Proposed amendment

The requirement to produce Note 1, Statement of accounting policies, will be removed. However, differences between accounts and budgets will still have to be explained if they impact the reconciliation of resource outturn to net operating cost.

The requirement to produce Note 2, Analysis of net outturn by section, will be retained. Entities will need to provide an explanation of the reasons for variances.

The requirements of Note 3, Reconciliation of resource outturn to net operating cost against Administration Budget and Administration net operating costs, will be reduced such that the reconciliation is only needed for the resource outturn.

Note 4, Reconciliation of net resources to net cash requirement, and Note 5, Analysis of income payable to the Consolidated Fund, will be retained but may be published in an annex.

Other notes related to Parliamentary accountability will be maintained with the following amendments:

- The reporting requirements for remote contingent liabilities will be reduced to align with the reporting requirements for contingent liabilities elsewhere in the annual report and accounts
- Public Sector Information Holders will only need to report by exception if they have not complied with cost allocation and charging requirements
- Details of loans made will only need to be disclosed within the accounts and not with the other disclosures on Parliamentary accountability.

The changes to chapter 3 are shown in track-changes overleaf.

Note 1: Statement of Accounting Policies

~~3.2.7 This note sets out the Statement of Parliamentary Supply accounting policies followed in compiling the Statement of Parliamentary Supply and the associated notes. It sets out the version of ESA that has been used and explains any interpretations of the system that have been applied to the accounts.~~

Notes 1 and 2: Analysis of net outturn by section

3.2.7 These notes follow the format of Part II of the Estimate. The first part of the note analyses net resource outturn by section and between administration costs, programme costs and income, comparing the net total outturn for each section within each budgetary control limit with the Estimate. The second part of the note analyses net capital outturn by section and between gross expenditure and income, comparing the net total outturn for each section within each budgetary control limit with the Estimate. The notes should give an brief explanation of the reasons for variances between the Estimate and outturn, with more detail being given in the Management Commentary.

Note 3: Reconciliation of resource outturn to net operating cost and against Administration Budget and Administration net operating costs

~~3.2.8 This note is in two parts:~~

~~3.2.9 Note 3.1 reconciles the net resource outturn (from Note 21) to the net operating cost shown in the Statement of Comprehensive Net Expenditure. All reconciling items must be briefly explained. Reconciling items, other than capital grants to external bodies (treated as resource expenditure in the Statement of Comprehensive Net Expenditure but as capital in budgets) and differences related to differing treatments of PFI will be rare, but might include prior period adjustments relating to errors or accounting policy changes at the instigation of the department itself, and occasional non-budget income or expenditure.~~

~~3.2.10 Note 3.2 shows outturn against the Administration Budget and a reconciliation to Administration income and expenditure included in the Statement of Comprehensive Net Expenditure.~~

Note 4: Reconciliation of Net Resources to Net Cash Requirement

~~3.2.11 3.2.8 This note reconciles the net resource outturn to the net cash requirement. It should briefly state the reasons for any variances between the Estimate and outturn, with the detailed reasons being explained in the Management Commentary. This note may be published as a note to the Statement of Parliamentary Supply or within an annex.~~

Note 5: Analysis of income payable to the Consolidated Fund

~~3.2.12 3.2.9 This note analyses income payable to the Consolidated Fund and will only be required if non-budget income has arisen during the year. Amounts collected by the department as agent of the Consolidated Fund should not be included, but should be accounted for in a separate Trust Statement if material (see Chapter 8). This note may be published as a note to the Statement of Parliamentary Supply or within an annex.~~

Other notes relating to Parliamentary accountability

3.2.13 In addition to the requirements for notes supporting the *Statement of Parliamentary Supply*, entities covered by Managing Public Money or Managing Public Money Northern Ireland should include the following disclosures, where the amounts are over the limit prescribed in *Managing Public Money or Managing Public Money Northern Ireland*:

- a) (departments only) the names of any public sector bodies outside the boundary for which the department had lead policy responsibility in the year, together with a description of their status (for example, trading fund or public corporation);
- a)b) a brief description of the nature of each of the entity's material remote contingent liabilities (that is, those that are disclosed under Parliamentary reporting requirements and not under IAS 37) and, where practical, an estimate of its financial effect; information about contingent liabilities not required to be disclosed under IAS 37 Provisions, Contingent Liabilities and Contingent Assets because the likelihood of a transfer of economic benefits is considered too remote, but included for parliamentary reporting and accountability purposes. For quantifiable remote contingent liabilities, the note should disclose the opening balance, any increase in the year, any amounts that crystallised in the year (that is, the liabilities have become reportable under IAS 37), any obligations that have expired during the year and the closing balance. The note should also state the amount that has been reported to Parliament by departmental Minute and provide a reconciliation between that and the disclosed amount where different. Reporting entities should list unquantifiable remote contingent liabilities, explaining why they are unquantifiable;
- c) (Public Sector Information Holders only) a statement is required if the entity has not complied with the cost allocation and charging requirements set out in HM Treasury guidance;
- b)d) a statement of losses; and special and other payments where the total amounts incurred are over the limits proscribed in Managing Public Money or Managing Public Money Northern Ireland. In the case of reporting on special payments which are severance payments, the detail to be disclosed should include the number of special severance payments made, the total amount paid out, and the maximum (highest), minimum (lowest) and median values of payments made. Where an entity's reporting of special severance payments does not include some or all of these details in circumstances in which doing so would conflict with a legal obligation arising as a result of the Data Protection Act 1998, or otherwise, this fact should also be disclosed; and
- e)e) notation of gifts made over the limits proscribed in Managing Public Money or Managing Public Money Northern Ireland; and
- d) details of loans made.

Effective date of amendment

The effective date for the proposed amendment is 1 April 2015

Proposed amendment to Government Financial Reporting Manual **Chapter 5, *Form and content of the annual report and accounts***

Introduction

An amendment to Chapter 5, *Form and content of the annual report and accounts*, is proposed.

Why the amendment is proposed

The amendment is proposed to restructure the annual report into a performance report and an accountability report and to make changes to the presentation of the financial statements.

Proposed amendment

Due to the extensive nature of the changes to the chapter, it is reproduced in full overleaf without track-changes.

Effective date of amendment

The effective date for the proposed amendment is 1 April 2015

5.1 Introduction

- 5.1.1 This chapter sets out the requirements for the format and content of the annual reports and accounts of the reporting entities covered by the requirements of this Manual, with the exception of pension schemes (see chapter 9).
- 5.1.2 Reporting entities are reminded that materiality is an overriding principle of reporting. Unless explicitly required by this Manual or other applicable guidance produced by the Relevant Authority then information should only be provided in the Annual Report and Accounts if it is material, recognising that a disclosure can be material by nature and/or context and not just value.
- 5.1.3 The annual report and accounts comprises:
- a) the performance report (section 5.2);
 - b) the accountability report (section 5.3); and
 - c) the IFRS financial statements (section 5.4).
- Reporting entities must prepare and publish an annual report and accounts as a single document unless the relevant authorities have specifically agreed otherwise. Illustrative financial statements are provided on the gov.uk website³.
- 5.1.4 This chapter does not set out the requirements for the format and content of the annual reports and accounts of reportable activities, which are set out in the relevant accounts directions.
- 5.1.5 Departments financed through the Westminster or the Northern Ireland Assembly Estimates process should refer to chapter 3 for guidance on the Statement of Parliamentary Supply. These departments should also refer to the illustrative Department Yellow.
- 5.1.6 The accounts to be published by spending bodies accountable to the Scottish Parliament will follow the format agreed between Scottish Ministers and the Public Audit Committee of the Scottish Parliament. The format of those accounts will be based on the principles, but not the detail, set out in this chapter.
- 5.1.6 In the case of **executive agencies** and **trading funds**, the preparation of an annual report as described above will satisfy the requirement for the preparation of a Foreword and a report as required by Cm 914 The Financing and Accountability of Next Steps Agencies (agencies), section 4(6A)(b) of the Government Trading Funds Act 1973 (trading funds) and article 8(7)(b) of the Financial Provisions (Northern Ireland) Order 1993. There is thus no need to produce a separate report in addition to the annual report described above. The document presented to Parliament should be described as “Annual Report and Accounts”.
- 5.1.7 In the case of other **ALBs** that are not incorporated as companies but do already have a statutory obligation to prepare a separate report, the preparation of an annual report described herein will satisfy the requirement for the production of this separate report. This annual report will be presented to Parliament with the accounts as a combined document described as the “Annual Report and Accounts”. Where there is currently no statutory requirement for the preparation of a separate report, ALBs will prepare an annual report as described herein for inclusion in the accounts which will be described as the “Annual Report and Accounts” and presented to Parliament.
- 5.1.8 ALBs that are incorporated as companies should comply with the requirements of the Companies Act 2006 in full and are not required to comply with the requirements of this chapter.
- 5.1.9 ALBs which are charities are not required to comply with the requirements of this chapter. They should follow the requirements of the Charities’ SORP and regulations made under Charities legislation.

³ Illustrative pro-forma financial statements are provided for Department Yellow, Agency Pink, NDPB Green, Trust Statement Purple and Pension Scheme Magenta.

- 5.1.10 A reporting entity that wishes to publish a document additional to its annual report and accounts that contains summary financial information should comply with the requirements of section 426 of the Companies Act 2006. The summary data must not be published in advance of the full annual report and accounts being laid before Parliament⁴ as to do so would be a breach of Parliamentary privilege.

5.2 The performance report

Scope of the performance report

- 5.2.1 The purpose of the performance section of the annual report is to provide information on the entity and wider group where relevant, its main objectives and strategies and the principal risks that it faces. The requirements of the performance report are based on the matters required to be dealt with in a Strategic Report as set out in Chapter 4A of Part 15 of the Companies Act 2006 and in a Directors' Report as set out in Chapter 5 of Part 15 of the Companies Act 2006 and Schedule 7 of SI 2008 No 410. The requirements of the Companies Act 2006 have been adapted for the public sector context and only need to be followed by entities which are not companies to the extent that they are incorporated into this Manual.⁵
- 5.2.2 Westminster departments are also required to follow annual guidance on reporting requirements promulgated by HM Treasury through PES papers.
- 5.2.3 The performance report must provide a fair, balanced and understandable analysis of the entity's performance, in line with the overarching requirement for the annual report and accounts as a whole to be fair, balanced and understandable (paragraph 5.3.12 of this manual).
- 5.2.4 Auditors will review the performance report for consistency with other information in the financial statements.
- 5.2.5 The performance report shall be signed and dated by the Accounting Officer or Chief Executive.
- 5.2.6 The performance report is required to have two sections: an 'Overview' and a 'Performance analysis'.

Overview

- 5.2.7 The purpose of the "Overview" is to give the user a short (no more than 10 to 15 pages) summary that provides them with sufficient information to understand the organisation, its purpose, the key risks to the achievement of its objectives and how it has performed during the year.
- 5.2.8 As a minimum, the Overview must include:
- A statement from the entity's lead Minister or Chief Executive providing their perspective on the performance of the organisation over the period;
 - A statement of the purpose and activities of the organisation;
 - The key issues and risks that could affect the entity in delivering its objectives; and
 - A performance summary.

Performance analysis

- 5.2.9 The purpose of the "Performance analysis" is for entities to report on their most important performance measures.

⁴ Parliament is used in this context to mean the Westminster Parliament, the Scottish Parliament, the National Assembly for Wales and the Northern Ireland Assembly.

⁵ The FRC has produced guidance on the Strategic Report which can be found at <https://frc.org.uk/Our-Work/Publications/Accounting-and-Reporting-Policy/Guidance-on-the-Strategic-Report.pdf>

5.2.10 As a minimum, the performance analysis must include:

- Information on how the entity measures performance i.e. what the entity sees as its key performance measures and how it checks performance against those measures;
- A more detailed analysis and explanation of the development and performance of the entity during the year. This analysis is required to utilise a wide range of data including key financial information from the financial statements section of the accounts; and
- Performance on other matters, including sustainable development, as promulgated by HM Treasury through PES papers.⁶

5.3 The accountability report

Scope of the accountability report

- 5.3.1 The purpose of the accountability section of the annual report is to meet key accountability requirements to Parliament. The requirements of the accountability report are based on the matters required to be dealt with in a Directors' Report, as set out in Chapter 5 of Part 15 of the Companies Act 2006 and Schedule 7 of SI 2008 No 410, and in a Remuneration Report, as set out in Chapter 6 of the Companies Act 2006 and Schedule 8 of SI 2008 No 410.
- 5.3.2 The requirements of the Companies Act 2006 have been adapted for the public sector context and only need to be followed by entities which are not companies to the extent that they are incorporated into this Manual.
- 5.3.3 Westminster departments are also required to follow annual guidance on reporting requirements promulgated by HM Treasury through PES papers.
- 5.3.4 Auditors will review the accountability report for consistency with other information in the financial statements and will provide an opinion on the following disclosures which should clearly be identified as audited within the accountability report:
- Single total figure of remuneration for each minister and director;
 - CETV disclosures for each minister and director;
 - Payments to past directors, if relevant;
 - Payments for loss of office, if relevant; and
 - The Statement of Parliamentary Supply and related notes.
- 5.3.5 The accountability report shall be signed and dated by the Accounting Officer or Chief Executive.
- 5.3.6 The accountability report is required to have three sections: a Corporate Governance Report; a Remuneration and Staff Report, and a Parliamentary Accountability and Audit Report.

Corporate governance report

⁶ Spending bodies accountable to the Northern Ireland Assembly will report on sustainability within the framework established by the Northern Ireland Executive's Programme for Government. Relevant guidance will be issued by the Northern Ireland Executive. Spending bodies accountable to the Scottish Parliament will report on sustainability within the framework established by the Scottish Government and in accordance with guidance issued by the Scottish Government. Spending bodies accountable to the Welsh Assembly Government will prepare a sustainability report within the Management Commentary based upon targets outlined by the Welsh Assembly Government. The Welsh Assembly Government will issue relevant guidance.

5.3.7 The purpose of the corporate governance report is to explain the composition and organisation of the entity's governance structures and how they support the achievement of the entity's objectives.

5.3.8 As a minimum, the corporate governance report must include:

- The directors' report
- The statement of Accounting Officer's responsibilities
- The governance statement

The directors' report

5.3.9 The directors' report must include the following, unless disclosed elsewhere in the annual report and accounts in which a cross-reference may be provided:

- a) (departments) the ministerial titles and names of all ministers who had responsibility for the department during the year;
- b) (departments) the name of the person occupying the position of the permanent head of the department;
- c) (reporting entities other than departments) the names of the chairman and chief executive unless disclosed elsewhere in the annual report;
- d) (all reporting entities) the composition of the management board (including advisory and non-executive members) having authority or responsibility for directing or controlling the major activities of the entity during the year. This means those who influence the decisions of the entity as a whole rather than the decisions of individual directorates or sections with the reporting entity;
- e) (all reporting entities) details of company directorships and other significant interests held by members of the management board which may conflict with their management responsibilities. Where a Register of Interests is available online, a weblink may provided instead of a detailed disclosure in the annual report;
- f) (all reporting entities) information on personal data related incidents where these have been formerly reported to the information commissioner's office; and
- g) (all reporting entities) other disclosures are promulgated by HM Treasury through PES papers.

For the remainder of this manual, individuals described in bullets b) to d) above are referred to as directors.

Statement of Accounting Officer's responsibilities

5.3.10 The Statement of Accounting Officer's responsibilities is required to explain the responsibilities of the Accounting Officer or Chief Executive of each reporting entity and reportable activity covered by the requirements of this Manual for preparing the financial statements. Model examples of Statements of Accounting Officer's responsibilities are provided in Annex 1.

5.3.11 The Accounting Officer is required to confirm that, as far as he or she is aware, there is no relevant audit information of which the entity's auditors are unaware, and the Accounting Officer has taken all the steps that he or she ought to have taken to make himself or herself aware of any relevant audit information and to establish that the entity's auditors are aware of that information.

5.3.12 The Accounting Officer is required to confirm that the annual report and accounts as a whole is fair, balanced and understandable and that he or she takes personal responsibility for the annual report and accounts and the judgments required for determining that it is fair, balanced and understandable.

Governance statement

- 5.3.13 All reporting entities covered by the requirements of this Manual shall prepare a governance statement. Guidance on content is provided for specific sectors and jurisdictions governed by the Relevant Authorities⁷. Where a reporting entity includes in its published annual report and accounts financial statements relating to several reportable activities, the reporting entity need include only a single governance statement.
- 5.3.14 Where the financial statements in respect of a reportable activity are published separately from the accounts of the reporting entity, accounts preparers should prepare a governance statement in respect of the reportable activity.

Remuneration and staff report

- 5.3.15 The remuneration and staff report sets out the entity's remuneration policy for directors, reports on how that policy has been implemented and sets out the amounts awarded to directors and where relevant the link between performance and remuneration.
- 5.3.16 In addition the report provides details on remuneration and staff that Parliament and other users see as key to accountability.
- 5.3.17 There is a presumption that information about named individuals will be given in all circumstances and all disclosures in the remuneration report will be consistent with identifiable information of those individuals in the financial statements. Non-disclosure is acceptable only where publication would:
- be in breach of any confidentiality agreement;
 - prejudice the rights, freedom or legitimate interest of the individual;
 - cause or be likely to cause substantial damage or substantial distress to the individual or another, and that damage or distress would be unwarranted; or
 - affect national security or where an individual may be at risk if his or her name is disclosed.
- 5.3.18 In other cases, it would be for the staff member to make a case for non-disclosure, which should be considered by the employer on a case-by-case basis. Where non-disclosure is agreed, the fact that certain disclosure has been omitted should be disclosed.
- 5.3.19 Westminster departments are also required to follow guidance contained in the annual Employer Pension Notice issued by the Cabinet Office.

Remuneration policy

- 5.3.20 Entities must disclose their policy on the remuneration of ministers and directors for the current and future years. In most cases it will be sufficient to refer to the work and recommendations of the Senior Salaries Review Body.

Single total figure of remuneration for each minister and director

- 5.3.21 Entities must disclose each component and the overall single total remuneration figure for each minister and director in the format proposed by the Cabinet Office and using the methodology defined by the Cabinet Office, in the Employer Pension Notice. The components of the single total remuneration figure are:
- a) Salary and allowances – should be disclosed in bands of £5,000 for officials and actual amounts for ministers. Salary and allowances covers both pensionable and non-pensionable amounts and includes, but may not necessarily be confined to: gross salaries; overtime; reserved rights to London Weighting or London allowances, recruitment and retention allowances; private-office allowances or other allowances to the extent that they are subject to UK taxation and any ex-gratia payments. It does not

⁷ Managing Public Money (including Annex 3.1), Scottish Public Finance Manual, Managing Public Money Northern Ireland, The Annual Governance Statement; Rough Guide for Practitioners (CIPFA Finance Advisory Network), Annual guidance issued by the Department of Health and Monitor.

include amounts which are a reimbursement of expenses directly incurred in the performance of an individual's duties. For ministers, only the salary payable in respect of their role as minister of the department should be shown;

- b) Performance pay or bonuses payable – should be separately reported from salaries, in bands of £5,000.
- c) Non-cash benefits – the estimated value of non-cash benefits (benefits in kind) should be disclosed to the nearest £100;
- d) Accrued pension benefits – The value of pension benefits accrued during the year is calculated as (the real increase in pension multiplied by 20) plus (the real increase in any lump sum) less (the contributions made by the individual). The real increases exclude increases due to inflation or any increase or decreases due to a transfer of pension rights.

Pension entitlements for each minister and director

5.3.22 Entities must disclose the pension entitlements for each minister and director in the format proposed by the Cabinet Office, in the Employer Pension Notice. This must include:

- the real increase during the reporting year in the pension and (if applicable) related lump sum at pension age (ministers age 65) in bands of £2,500;
- the value at the end of the reporting year of the accrued pension and (if applicable) related lump sum at pension age (ministers, age 65) in bands of £5,000;
- the value of the cash equivalent transfer value at the beginning of the reporting year to the nearest £1,000;
- the real increase in the cash equivalent transfer value during the reporting year, to the nearest £1,000;
- the value of the cash equivalent transfer value at the end of the reporting year to the nearest £1,000; and
- in the case of a partnership pension account, the employer's contribution (in these circumstances, the disclosures in the bullets above will not apply).

Compensation on early retirement or for loss of office

5.3.23 If a payment for compensation on early retirement or for loss of office (paid or receivable) has been made under the terms of an approved Compensation Scheme, the fact that such a payment has been made should be disclosed, including a description of the compensation payment and details of the total amounts paid (the cost to be used must include any top-up to compensation provided by the employer to buy out the actuarial reduction on an individual's pension).

Payments to past directors

5.3.24 Entities must provide details of any payments made to any person who was not a director at the time the payment was made, but who had been a director of the entity previously, unless already disclosed within a previous directors' remuneration report, the current year single total remuneration disclosure or within the disclosure of compensation for early retirement or loss of office. Only payments of regular pension benefits which commenced in previous years and payments in respect of employment for the entity other than as a director may be excluded.

Fair pay disclosure

5.3.25 Entities must disclose the following information together with prior year comparatives:

- The median remuneration of the reporting entity's staff. This is based on annualised, full-time equivalent remuneration of all staff (including temporary and agency staff) as at the reporting date;

- The range of staff remuneration;
- The ratio between the median staff remuneration and the mid-point of the banded remuneration of the highest paid director; and
- An explanation for any significant changes in the ratio between the current and prior year.

5.3.26 For departments, the calculation should exclude arm's length bodies within the consolidation boundary. Further guidance is provided on the gov.uk website.

Staff report

5.3.27 The staff report must include the following information for all entities:

- a) Number of senior civil service staff (or equivalent) by band
- b) Staff numbers – Entities should provide an analysis of staff numbers distinguishing between:
 - Staff with a permanent (UK) employment contract with the entity;
 - Other staff engaged on the objectives of the entity (for example, short term contract staff, agency/temporary staff, locally engaged staff overseas and inward secondments where the entity is paying the whole or the majority of their costs). Where the number of staff under any one category of 'other staff' is significant, that category should be separately disclosed;
 - Ministers; and
 - Special advisers.
- c) Staff composition – Entities should provide an analysis of the number of persons of each sex who were directors, senior civil servants (or equivalent) and employees of the company
- d) Sickness absence data
- e) Staff policies applied during the financial year:
 - For giving full and fair consideration to applications for employment by the company made by disabled persons, having regard to their particular aptitudes and abilities
 - For continuing the employment of, and for arranging appropriate training for, employees of the company who have become disabled persons during the period when they were employed by the company
 - Otherwise for the training, career development and promotion of disabled persons employed by the company
- f) Expenditure on consultancy
- g) Off-payroll engagements – summary data on the use of off-payroll arrangements to meet requirements promulgated by HM Treasury in PES guidance.
- h) Exit packages – summary data on the use of exit packages agreed in year in the format proposed by the Cabinet Office.

Parliamentary accountability and audit report

5.3.28 The Parliamentary accountability and audit report brings together the key Parliamentary accountability documents within the annual report and accounts. It comprises:

- a) (departments financed through the Westminster or Northern Ireland Assembly Estimates process) Statement of Parliamentary Supply and supporting notes;
- b) (all entities) regularity of expenditure;

- c) (all entities) fees and charges – the analysis should include the following information for each service (i) the financial objective (ii) full cost (iii) income (iv) surplus or deficit (v) performance against financial objective;
- d) (all entities) remote contingent liabilities;
- e) (all entities) long-term expenditure trends; and
- f) (all entities) the Certificate and Report of the Comptroller and Auditor General to the House of Commons.

5.3.29 The requirements for (a) to (d) are detailed in Chapter 3. The requirements for the disclosure on long-term expenditure trends are detailed in PES papers promulgated by HM Treasury.

The Certificate and Report of the Comptroller and Auditor General to the House of Commons

- 5.3.30 All entities are required to have their financial statements audited by the auditor named in the relevant legislation or other legislation or governing statute. The general presumption is that the auditor will be the Comptroller and Auditor General, the Auditor General for Wales, the Auditor General for Scotland or the Comptroller and Auditor General for Northern Ireland.
- 5.3.31 Entities should refer to the guidance on the handling of public funds and to the individual websites of the audit offices for information about the role of the auditor.
- 5.3.32 The audit opinion will be in the form required by International Standard on Auditing (UK and Ireland) 700 and Practice Note 10 Audit of central government financial statements in the United Kingdom. The precise form of the audit opinion will depend on the results of the audit and is the responsibility of the auditor.
- 5.3.33 Where the relevant legislation requires the auditor to report on the examination of the financial statements, the auditor will provide such a report. The form and content of the report is the responsibility of the auditor. Where the auditor has no substantive comment to make, the report will generally be in the form of a single sentence appended to the audit opinion in the form: 'I have no observations to make on these financial statements'. Where there is a substantive report, it will be referred to in the audit opinion, but will be quite separate from it.
- 5.3.34 The Companies Act 2006 s.479A was amended with effect from 1 October 2012 to include conditions for exemption from audit for subsidiary companies within a group.⁸ Subsidiary companies limited by guarantee would normally be subject to audit by the Comptroller and Auditor General, Auditor General for Wales, the Auditor General for Scotland or the Comptroller and Auditor General for Northern Ireland and therefore not eligible for exemption. If an entity wishes to use the exemption for a subsidiary company limited by shares, this must be approved by the relevant authority (through sponsoring bodies where appropriate) who will assess whether the exemption is appropriate for the particular circumstance.

5.4 The annual accounts

- 5.4.1 This section provides guidance to reporting entities on the format and content of the (Consolidated) Statement of Comprehensive Net Expenditure, the (Consolidated) Statement of Financial Position, the (Consolidated) Statement of Changes in Taxpayers' Equity and the (Consolidated) Statement of Cash Flows, together with the relevant notes. The following paragraphs make it clear how different types of reporting entity should present financial statements. The detailed requirements for the format and content of the financial statements of reportable activities are set out in the accounts directions for those activities. This section sets requirements based on the Companies Act 2006 and details adaptations and interpretations of the

⁸ Statutory instrument 2012/2301 *The Companies and Limited Liability Partnerships (Accounts and Audit Exemptions and Change of Accounting framework) Regulations 2012* available on the legislation.gov.uk website

following accounting standards that provide guidance on the formats of, and disclosures in, financial statements:

IAS 1 *Presentation of Financial Statements*;

IAS 7 *Statement of Cash Flows*;

IAS 10 *Events after the Reporting Period*;

IAS 24 *Related Party Disclosures*; and

IFRS 8 *Operating Segments*.

- 5.4.2 Other accounting standards, which are dealt with in other chapters of this Manual, might include disclosure requirements. Unless indicated otherwise, those disclosure requirements apply in full.
- 5.4.3 All reporting entities shall prepare individual or group accounts as appropriate using IAS 1. Where departments prepare group accounts IAS 1 is interpreted to require that the financial statements provide two columns, one showing the core department plus agencies and the other showing the group.
- 5.4.4 IAS 1 provides guidance on the comparative information to be disclosed in the financial statements. These requirements should be applied in full except that reporting entities should note that a decision on whether to include corresponding amounts in disclosures specific to government departments and agencies (for example, in relation to information on the Statement of Parliamentary Supply) will be taken on a case-by-case basis and will be shown in Department Yellow.

Statement of Comprehensive Net Expenditure

- 5.4.5 IAS 1 requires entities to prepare a Statement of Comprehensive Income. This Manual adapts IAS 1 as set out below.
- 5.4.6 Departments preparing annual accounts and executive agencies preparing financial statements under the Government Resources and Accounts Act 2000 or under the Government Resources and Accounts Act (Northern Ireland) 2001 shall prepare a Statement of Comprehensive Net Expenditure. Row headings should be based on the department's material sources of income and expenditure. Where a department or agency considers that an alternative format is required to improve the understanding of the body's financial performance, they should seek the approval of the relevant authority, with agencies seeking approval through the sponsoring department.
- 5.4.7 In applying IAS 1 where this Manual refers to the Statement of Comprehensive Net Expenditure or Statement of Comprehensive Income, ALBs should interpret this terminology as appropriate for their own circumstances.
- 5.4.8 ALBs which are trading funds should prepare a Statement of Comprehensive Income.
- 5.4.9 ALBs which are companies may make use of the exemption available under section 408 of Chapter 4 of Part 15 of the Companies Act to omit the company's individual profit and loss account and only report the group profit and loss account if the conditions in section 408 are met.

Statement of Financial Position

- 5.4.10 IAS 1 requires entities to prepare a Statement of Financial Position and provides guidance on the minimum presentation required on the face of the statement of financial position.
- 5.4.11 The Statement of Financial Position must be signed by the Accounting Officer or, where relevant, Chief Executive.

Statement of Cash Flows

- 5.4.12 IAS 7 sets out the requirements for the format of the Statement of Cash Flows. Entities financed by Supply issued from the Consolidated Fund should include

amounts drawn down from the Consolidated Fund and paid to the Consolidated Fund on a gross basis in the financing section.

- 5.4.13 In reconciling the operating cost to operating cash flows, entities should exclude movements in debtors and creditors relating to items that do not pass through the Statement of Comprehensive Net Expenditure (balances with the Consolidated Fund; and debtors and creditors linked to loans from the National Loans Fund, capital expenditure, finance leases and PFI contracts);
- 5.4.14 In analysing capital expenditure and financial investment, entities should adjust for debtors and creditors relating to capital expenditure and those relating to loans issued to or repaid by other bodies.
- 5.4.15 In analysing financing, entities should adjust for debtors and creditors relating to the capital expenditure in respect of finance leases and on-balance sheet PFI contracts.

Statement of Changes in Equity

- 5.4.16 IAS 1 requires entities to prepare a Statement of Changes in Equity. IAS 1 is interpreted for the public sector context such that all reporting entities are required to present a Statement of Changes in Taxpayer's Equity following the format in IAS 1. Entities funded from Supply or grant-in-aid will need to adapt the format to disclose transactions with the General Fund.
- 5.4.17 The General Fund represents the total assets less liabilities of a department or agency, to the extent that the total is not represented by other reserves and financing items. Supply financing is credited to the General Fund, as is financing from the National Insurance Fund (relating to benefits expenditure) and from the Contingencies Fund. An amount equal to any expenditure on standing services is credited to the General Fund.
- 5.4.18 Where expenditure is funded directly by the Consolidated Fund, a department should account for the transaction in its Statement of Comprehensive Net Expenditure if it satisfies both of the following criteria:
 - a) the entity has the ability to deploy the economic resources involved; and
 - b) the entity has the ability to benefit (or to suffer) from the deployment of those resources.
- 5.4.19 The financing of public sector entities is ultimately tax-based and an IAS 1-based notion of capital does not apply to many of them. Capital disclosures should be given only with the agreement of the relevant authority (through the parent or sponsoring department where appropriate).

Notes to the accounts

- 5.4.20 **Accounting policies** – The notes to the accounts must include a statement that the accounts have been prepared in accordance with International Financial Reporting Standards as adapted and interpreted by this Manual. Executive agencies that are not whole departments and ALBs must also include a note that the accounts have been prepared under a direction issued by [relevant authority] under [reference to appropriate legislation].
- 5.4.21 **Operating income** - All reporting entities should provide an analysis of operating income, together with commentary where appropriate, that enables users of the financial statements to understand the nature of the entity's operating income.
- 5.4.22 **Other operating costs** – Entities should provide an analysis of operating costs as recorded in the Statement of Comprehensive Net Expenditure in separate notes to the financial statements. This should include staff costs as set out below, service charges under PFI contracts, the individual components of non-cash items, and an analysis of other significant expenditure items.
- 5.4.23 **Staff costs** – Entities should provide an analysis of staff costs distinguishing between:
 - Staff with a permanent (UK) employment contract with the entity;

- Other staff engaged on the objectives of the entity (for example, short term contract staff, agency/temporary staff, locally engaged staff overseas and inward secondments where the entity is paying the whole or the majority of their costs). Where the number of staff under any one category of 'other staff' is significant, that category should be separately disclosed;
 - Ministers; and
 - Special advisers.
- 5.4.24 **Cash and cash equivalents** – Entities shall disclose the opening position, the net change in balances and the closing position separately for cash and cash equivalents. Where applicable, the closing position should be further analysed between balances held with the Government Banking Service (GBS)⁹ and balances held in commercial banks.
- 5.4.25 **Financial instruments** – Only where the entity is exposed to material financial instrument risk should the appropriate IFRS 7 disclosures be made. Material financial risk includes significant credit risk from receivables.
- 5.4.26 **Commitments under PFI contracts** – For 'off-balance sheet' service concessions entities should disclose the total payments to which they are committed distinguishing between those that are due to be made within one year, between one and five years, and later than five years. For 'on-balance sheet' service concession arrangements entities should disclose the total rentals due within one year, between one and five years, and later than five years, less the interest element to give the present value of obligations.
- 5.4.27 **Information about related undertakings** – If not disclosed elsewhere in the annual report and accounts, entities shall disclose the name of each of its subsidiaries, or provide a weblink to where this information is available. If the entity has significant holdings¹⁰ in undertakings other than subsidiary undertakings, then the following must be disclosed:
- The name of the undertaking;
 - If the undertaking is incorporated outside the UK, the country in which it is incorporated, or, if it is unincorporated, the address of its principal place of business;
 - The identify of each class of shares in the undertaking held by the company and the proportion of the nominal value of the shares of that class represented by those shares; and
 - If the entity holds more than 50% of the nominal value of the shares in the undertaking, the aggregate amount of the capital and reserves of the undertaking as at the end of its financial year and its profit or loss for that year, if material.
- 5.4.28 **Third party assets** – These are assets for which an entity acts as custodian or trustee but in which neither the entity nor government more generally has a direct beneficial interest. Third party assets are not public assets, and should not be recorded in the primary financial statements. Material third party assets should be disclosed. Where significant the note should differentiate between:
- a) third party monies and listed securities: the minimum level of numerical disclosure required is a statement of closing balances at financial year-end. For listed securities, this will be the total market value. Optionally, when considered significant by the entity and at its discretion, further disclosures may be made, including gross inflows and outflows in the year and the number and types of securities held;

⁹ Where GBS is using Citi and Royal Bank of Scotland Group to provide the banking services, funds held in these accounts should not be classed as commercial bank balances.

¹⁰ A holding is significant for this purpose if it amounts to 20% or more of the nominal value of any class of shares in the undertaking or the amount of the holding exceeds one-fifth of the amount of the company's assets.

- b) third party physical assets and unlisted securities: disclosure may be by way of narrative note. For physical assets, the note should provide information on the asset categories involved. Such disclosure should be sufficient to give users of the financial statements an understanding of the extent to which third-party physical assets and unlisted securities are held by the entity; and
- c) In the event that third party monies are found to have been in a public bank account at the end of an accounting year, commentary should be included in the note on cash at bank and in hand and in the disclosures above on the amount of third party monies held in the bank account.

5.5 *Presentation to Parliament and publication*

- 5.5.1 HM Treasury will lay before the House of Commons the resource accounts of departments (including agencies that are whole departments) under section 6(4) of the Government Resources and Accounts Act 2000. They will then be published.
- 5.5.2 Agencies that are not whole departments will lay their annual reports and accounts before the House of Commons under section 7(3)(c) of the Government Resources and Accounts Act 2000. They will then be published.
- 5.5.3 The Auditor General for Wales will lay before the National Assembly for Wales the resource accounts of the Welsh Ministers (Welsh Assembly Government) under section 131(6) of the Government of Wales Act 2006. The Auditor General for Wales will lay the resource accounts of Estyn (Her Majesty's Chief Inspector of Schools in Wales) under Schedule 6 section 6(2)(b) of the Government of Wales Act 1998. They will then be published.
- 5.5.4 The Department of Finance and Personnel will lay before the Northern Ireland Assembly the resource accounts of Northern Ireland departments (including agencies which are whole departments) under section 10(4) of the Government Resources and Accounts Act (Northern Ireland) 2001. They will then be published.
- 5.5.5 In the case of Northern Ireland agencies which are not whole departments, the parent department will lay before the Northern Ireland Assembly the annual report and accounts of those agencies under section 11(3)(c) of the Government Resources and Accounts Act (Northern Ireland) 2001. They will then be published.
- 5.5.6 Scottish Ministers will lay before Parliament accounts prepared under the Public Finance and Accountability (Scotland) Act 2000 under section 22(5) of that Act. They will then be published.
- 5.5.7 The procedure for publishing and laying the accounts of ALBs varies according to the provisions of the governing statute. Where the legislation requires the accounts to be laid before Parliament or where accounts are placed in the library of the House of Commons (and perhaps also the House of Lords), the accounts should be published thereafter.
- 5.5.8 The procedure for publishing and laying the accounts of ALBs in Northern Ireland varies according to the provisions of the incorporating statute. If responsibility does not lie with the Comptroller and Auditor General, the ALB is normally required to submit the audited accounts to its sponsor department, who will arrange to lay them before the Northern Ireland Assembly. A copy should be placed in the library of the Northern Ireland Assembly.
- 5.5.9 The Comptroller and Auditor General will lay before Parliament the annual reports and accounts of trading funds under section 4(6)(b) of the Government Trading Funds Act 1973. Trading funds may then publish them.
- 5.5.10 The Comptroller and Auditor General will lay before the Northern Ireland Assembly the annual reports and accounts of trading funds in Northern Ireland under article 8(6)(b) of the Financial Provisions (Northern Ireland) Order 1993. The annual reports and accounts will then be published.