



HM TREASURY

Financial Reporting Advisory Board Paper

The Financial Reporting Landscape

Issue:	There have been a number of developments in both the corporate and public sector financial reporting landscapes. These are as a result of the Non-Financial Reporting Regulations, the Parliamentary inquiry into government accounts, the C&AG's reflections on the 2016-17 audit process and the work that government is doing to boost the capability of the Finance Function.
Impact on guidance:	The 2017-18 FReM and PES guidance 2017 were updated to cover key requirements of the Non-Financial Reporting Regulations and the Strategic Report Guidance proposed update.
IAS/IFRS adaptation?	N/A
IPSAS compliant?	N/A
Interpretation for the public sector context?	As above
Alignment with National Accounts	N/A
Impact on budgets/Estimates?	N/A
Recommendation:	The Board is asked to note the developments outlined in the paper and provide any comments that it may have.
Timing:	HM Treasury plan to begin a review of government accounts this summer following production of the 2017-18 departmental ARAs. We will continue to monitor developments and make changes to future versions of the FReM and PES papers as required.

Introduction

1. There have been a number of developments in both the corporate and public sector financial reporting landscapes. Key elements of The Non-Financial Reporting Regulations 2016 and FRC Strategic Report Guidance were reflected in the 2017-18 FReM and the PES paper on ARAs issued in December 2017. The Public Administration and Constitutional Affairs Committee (PACAC) published their report into government accounts last year and HM Treasury is finalising their response. The C&AG's letter to the Permanent Secretary, HM Treasury on the 2016-17 audit process sets out a number of points and there have been several strands of work underway to improve the capability of the Government Finance Function. This paper summarises these developments and sets out the next steps.

Non-Financial Reporting

2. The Non-Financial Reporting Regulations became effective for companies and qualifying partnerships with financial years beginning on or after 1 January 2017. The Regulations implement the EU Directive on Non-Financial Reporting Directive. Key elements have been incorporated into the FReM to enhance the extent of non-financial reporting in the public sector and align with changes in corporate reporting. These include:

3. Within the Performance report:

- The statement of the purpose and activities of the organisation to contain additional narrative including a brief description of the business model and environment, organisational structure, objectives and strategies (Overview section).
- Strengthen sustainability reporting to provide information on environmental matters including the impact of the entity's business on the environment.
- Inclusion of non-financial information in respect of social matters, respect for human rights, anti-corruption and anti-bribery matters.

4. Within the Staff Report:

- Supplement with information pertaining to employee matters such as other diversity issues and equal treatment in employment and occupation not already covered by existing requirements, employment issues, health and safety at work, trade union relationships and human capital management.

5. The Regulations also introduce a requirement for the main trends and factors affecting the future of the entity to be outlined. This goes beyond current FReM requirement to report on purposes and activities of the organisation and how performance is measured and has not been included in the 2017-18 FReM. However, this is partially covered in Single Departmental Plans (SDPs) and PES guidance on the preparation of ARAs applicable for central government departments. There may a need to further strengthen the FReM, SDPs and/or PES guidance in future.

6. In August 2017, the FRC published a consultation with proposals to amend the Strategic Report Guidance. The proposed amendments reflect the legislative changes arising from the UK implementation of the EU Directive on disclosure of non-financial and diversity information, and strengthen the link between the purpose of the strategic report and the director's duty under section 172 of the Companies Act 2006. A number of these amendments have been included in the 2017-18 FReM and PES guidance

to help public sector reporting keep pace with developments in the private sector and promote improved and more balanced reporting:

7. Within the Performance Report:

- Strengthening of the narrative on how entities measure performance to include narrative to explain the link between KPIs, risk and uncertainty.
- Providing a fuller explanation of the relationships and linkages between different pieces of information in the ARAs.

8. The updated Strategic Report Guidance also introduces requirements for entities to consider the principles that reflect the focus on the long-term success of the entity and focus on how value is generated. In addition, Section 172 of the Companies Act requires directors to have regard to the long-term impact of any decisions, the interests of stakeholders and non-financial matters in pursuing their duty to promote the long-term success of the entity. These elements have not been fully reflected in current FReM guidance, and it may be more appropriate to consider them in SDPs which are the basis of the government's planning and performance framework. HM Treasury continue to consider these points and will keep abreast of developments in this area.

PACAC inquiry into government accounts

9. PACAC's report into Government accounts, [Accounting for democracy: making sure Parliament, the people and ministers know how and why public money is spent](#) was published in April 2017 and discussed at the June 2017 FRAB meeting. The report puts forward a large number of recommendations in a wide range of areas including additional reporting requirements. The recommendations in relation to financial reporting focus on the Annual Report element, particularly around making accounts more in tune with the needs of users. In summary:

- Additional reporting of financial and non-financial information by policy area, programme and project, with audited statements.
- Reporting on the unit costs of key services, time series and trend data (for income, assets, liabilities and expenditure, policies and programmes) including future financial projections.
- Tracking expenditure from the Spending Review through to ARAs, as well as ministerial commitments.
- Carrying out research on the users and potential users of ARAs.
- Strengthening the links between outputs and outcomes in the Performance Report, less use of narrative and more use of graphics.
- Annual reports to adhere to the UK Statistics Authority Code of Practice and be audited.

10. There is also a recommendation for the Board which is set out below:

- We recommend that the Treasury make FRAB more representative of the consumers of Accounts and more attuned to users' requirements, by increasing representation on the Board of users or user groups. We further recommend that Treasury and FRAB should consider how, within the framework of recognised accounting standards, Accounts could be made more useful and responsive to the needs of users, providing the sort of information we have proposed within this report.

11. HM Treasury welcomes the report and supports its overriding principles and aims. It has held discussions with the NAO and Parliamentary Scrutiny Unit and is currently finalising its response. In response to the Committee's report and recommendations, the Treasury is keen to undertake a review of departmental ARAs in liaison with the Scrutiny Unit and NAO. It is proposed that the review will build on the Committee's recommendations by evaluating progress since the Simplifying and Streamlining project was implemented and identifying best practice in departmental accounts, as well as exploring the links with developments in corporate non-financial reporting requirements. HM Treasury plan to commence the review in summer 2018 following the publication of the 2017-18 departmental ARAs.

12. Does the Board have any comments on the report's recommendations and the planned review of ARAs?

C&AG letter and Finance Function capability

13. The C&AG wrote to the HM Treasury Permanent Secretary in January 2018 outlining his reflections on the 2016-17 audit of departmental ARAs. He notes the good progress made on issues raised in previous years, particularly in relation to improvements in WGA and the academy sector reporting. However, he also notes the difficulty of the 2016-17 audit cycle and raises concerns over the capability of government finance teams and the impact this has had on the quality and timeliness of ARAs.

14. HM Treasury and the Government Finance Function, led by Mike Driver, have already begun to address this issue and there are a number of ongoing workstreams in this area.

15. The Finance Function Target Operating Model includes the creation of a set of new cross government Finance Centres of Excellence with the aim of improving finance delivery in the future, including more systematic collaboration and sharing of expertise between departments. Two Centres of Excellence are currently operational covering tax and costing. The Technical Accounting Centre of Excellence (TACoE) pilot has made progress and is expected to form a key role in supporting departments and providing high quality advice and understanding of financial reporting across government. It facilitated several workshops throughout January, inviting customers and stakeholders from across government departments to share their thoughts and insights to help develop the proposition. It is expected to go live in July 2018. A Grants Centre of Excellence has also just been launched.

16. The Treasury continues to support colleagues in departments to improve the quality of financial reporting and has issued guidance on the application of the new reporting standards, IFRS 9 and IFRS 15. There has been extensive departmental engagement through technical working groups and professional training and workshops. These include hosting sessions at the Government Finance Conference in January and presenting at the Government Finance Summer Schools in November and December 2017. The Government Finance Academy set up a number of day-long sessions around the UK with a large and wide range of attendees from around government.

Recommendation

17. We ask the Board to note the developments outlined in the paper and provide any comments that it may have.

HM Treasury
15 March 2018