HM TREASURY

FRAB 140 (02(1))

April 2020

Financial Reporting Advisory Board Paper

Reviewing the 2019-20 financial reporting requirements in light of Covid-19

Issue:	This paper outlines the challenges from Covid-19 that are emerging, details the steps that HM Treasury have taken since the 19 March meeting, examines the various options for reducing the reporting burden that have been considered and seeks the Board's approval for a preferred way forward .
Impact on guidance:	The proposal is for the 2019-20 FReM to remain unchanged. However, further guidance would set minimum reporting requirements for the performance and accountability reports.
IAS/IFRS adaptation or interpretations?	N/A
Impact on WGA?	Later laying dates for government ARAs are likely to have a knock-on effect to WGA preparation. Any streamlining of financial statements would have a material effect on WGA, though this is not being proposed. Inconsistency in reporting across the public sector will significantly compromise WGA.
IPSAS compliant?	N/A
Impact on budgetary regime?	N/A
Alignment with National Accounts (ESA10)?	N/A
Impact on Estimates?	N/A
Recommendation:	1) approve the setting of minimum reporting requirements in 2019-20, leading to detailed financial statements as per the 2019-20 FReM with streamlined annual performance and accountability reports (Option 4). 2) *[if not agreed prior to the FRAB meeting]* agree that HM Treasury will agree the detailed performance and accountability reporting requirements with Parliamentary Scrutiny Unit, Cabinet Office and NAO as outlined in paragraphs 29 and 30 of this paper, and then look to issue guidance to government entities following ministerial and Parliamentary approval.
Timing:	There is a need for FRAB to act quickly so that we can provide revised reporting guidance for 2019-20 financial year as a matter of urgency.

DETAIL

Background

1. The last meeting of the Board on 19th March took place in quite exceptional circumstances. Tuesday of that week saw the introduction of restrictions in order to try and slow down the spread of Covid-19, and as a result the meeting took place via teleconference. The agenda was amended at short notice and the focus of the discussions in the meeting was on the possible challenges that Covid-19 places on public sector bodies, in both the immediate and medium term, and the knock-on effect on financial reporting. The main challenges identified were around staffing and resource required to prepare the financial statements, and specific financial reporting issues (such as measurement issues and events after the reporting period)

2. As a result of this significant uncertainty, the Board discussed a number of options that could be considered in order to reduce the reporting burden on the public sector. These options have been considered further by HM Treasury and discussed with a wide range of preparers, users and other stakeholders.

3. This paper outlines the challenges from Covid-19 that are emerging, details the steps that HM Treasury have taken since the 19 March meeting, examines the various options for reducing the reporting burden that have been considered and seeks the Board's approval so that HM Treasury can issue guidance as a matter of urgency.

Challenges arising from Covid-19

4. A number of potential challenges to financial reporting were discussed at the Board's last meeting. Views have also been sought from preparers and users, and the main challenges identified are outlined below:

   - The resource available to prepare annual reports and accounts (ARAs) is reduced as staff members fall sick or self-isolate.
   - In some departments finance staff may need to be redeployed to meet other urgent needs, further reducing the available resource.
   - Non-finance staff who are involved in preparing or feeding into the annual report may also be redeployed or less able to prioritise work on ARAs.
   - The abrupt shift to home working may put a strain on equipment and technology, for example if there are not enough laptops to go around or if networks struggle to cope with increased demand.
   - Some government bodies outsource some of their financial reporting to private sector providers which may not be functioning at this time.
   - The restrictions on movement are likely to interrupt key processes, particularly the valuation of physical assets.
   - The work of the auditors may be severely curtailed as they will not be able to carry out fieldwork visits to obtain evidence.

5. The usual expectation is that government bodies will provide a full set of audited ARAs as per the 2019-20 Financial Reporting Manual to similar timescales as previous years i.e. aiming to publish and lay accounts before summer recess in June/July. However, due to the scale of these

unprecedented challenges and the effect it is having on certain departments and government bodies, there is a clear need to review the 2019-20 financial reporting requirements in order to try to ease the burden for preparers, while still maintaining a level of accountability.

Outline of HM Treasury's approach

6. Following the 19th March Board meeting, HM Treasury formed a longlist of potential options for 2019-20 government ARAs based on the various ideas discussed. Due to the amount of uncertainty inherent in the Covid-19 situation, it was sensible to initially explore a full range of possible solutions, including those that were more novel.

7. The longlist of 8 initial options are outlined below:

    1) **"Do Nothing"** - produce 2019-20 ARAs as per the current FReM to normal timescales
    2) **Timing** - Relaxing expectations regarding when 2019-20 ARAs will be laid before Parliament. Full set of ARAs to be produced later in the year before the statutory deadline.
    3) **Staggering** the production of ARAs – producing financial statements for 2019/20 to similar timescales to now, and the annual report some time later.
    4) **Removing** some reporting requirements altogether for 2019-20, leading to <u>detailed financial statements as per the 2019-20 FReM</u> with streamlined annual performance and accountability reports
    5) **Removing** some reporting requirements altogether for 2019-20, leading to <u>streamlined financial statements</u>, accountability and performance reports
    6) **Extending** the reporting period so that one set of ARAs covers 24 months. The new period would run 2019-21, and a full set of annual report and accounts for that period would be published in 2021. Instead, interim accounts and the SOPS would be published for the 2019-20 financial year.
    7) **Exempting** government bodies from producing ARAs for 2019-20 and requiring that <u>interim accounts be published instead</u>; potentially also producing a form of the Parliamentary accountability disclosures (in particular the Statement of Outturn against Parliamentary Supply (SOPS)). No further financial reporting for 2019-20 would be required via ARAs.
    8) **Exempting** government bodies from producing ARAs for 2019-20 without requiring any alternative.

8. HM Treasury explored the options further, setting out and discussing the possible pros and cons of each. It was acknowledged from the outset that there were likely to be issues in any approach taken, but that the exceptional nature of the situation meant that action was clearly needed.

9. These potential options were shared with a wide range of preparers and users. These included the User and Preparer Advisory Group, the Parliamentary Scrutiny Unit, the NAO, Relevant Authorities and government departments. Stakeholders were kept informed throughout the process as certain options were discounted and a preferred way forward emerged. Opinions were also sought from international financial reporting colleagues, though their thinking was not as advanced as the UK's, partly due to having later financial year-ends.

10. Early feedback from some preparers suggested that they were unlikely to be able to produce 2019-20 ARAs as per the current FReM to normal timescales (**Option 1**) and that attempting to do so would place an unreasonable burden on those that prepare ARAs. In some cases, finance

staff and those who produce the annual report had already been redeployed to roles related to the Covid-19 response. It also became clear that the situation was likely to become worse before it got better, and that the impact of Covid-19 was unlikely to be limited to 2019-20 reporting but was also likely to affect the 2020-21 reporting year. Therefore, it became obvious fairly quickly that it would not be possible to produce 2019-20 ARAs as per the current FReM to normal timescales and **Option 1 was therefore discounted.**

The need for flexibility and certainty

11. Another early theme emerging from the feedback was that the Covid-19 crisis was going to affect different entities in different ways. While there would be significant disruption to some organisations, for others the disruption was minimal and they believed that they would be able to produce complete ARAs to similar timescales to previous years.

12. It was therefore important that any guidance issued included a degree of flexibility so that organisations were not discouraged from reporting where they were able to. HM Treasury therefore decided that the easiest way to allow for this flexibility was to provide minimum reporting requirements. This decision was communicated to preparers.

13. There was also a realisation that the Covid-19 situation was changing very quickly, and therefore the preferred option would need to reflect that. Entities were clear that any guidance for 2019-20 should be final and HM Treasury were keen to give certainty and only issue one set of guidance, and to do so as quickly as possible.

Timing

14. It also became immediately clear that entities would appreciate any 'quick wins' in order to help relieve some of the immediate pressure. Each year HM Treasury sets an administrative deadline to lay accounts in Parliament of 30 June, though in reality most entities aim to lay before summer recess. However, the legislative deadline for 2019-20 accounts to be laid in Parliament is 31 January 2021.

15. Therefore, after discussions with both the NAO and the Parliamentary Scrutiny Unit, HM Treasury took the decision to extend the administrative deadline by 3 months to 30 September 2020, while also reminding entities of the later legislative deadline and encouraging entities to continue to lay their ARAs as soon as they can. This approach was supported by the Government Finance Leadership Group who called for HM Treasury to act and were kept informed as thinking developed. The potential disadvantages of this approach were considered and evaluated, including the impact on the 2020-21 reporting year due to later reporting in 2019-20 and risk that ARAs would be potentially less relevant. There would also be knock-on effects to preparing the Whole of Government Accounts and the risk of setting a precedent. However, WGA can only be effective if underlying data is complete, accurate and robust. Therefore, sacrificing timeliness of WGA returns to support departments in preparing robust and accurate accounts is deemed an acceptable short-term compromise. It was vitally important to give some immediate relief and certainty to preparers, given the unprecedented nature of the current situation.

16. This decision has already been communicated to government entities and wider stakeholders and has been well received. In terms of the options outlined in Paragraph 8, the decision on timing would hold regardless of which option on the content of accounts was taken forward, **which therefore removes Option 2 as an option in its own right.**

17. This decision also removed the need for **Option 3** - staggering the production of ARAs by producing financial statements for 2019/20 to similar timescales to now, and the annual report some time later. In any case this idea had received no support from stakeholders as it goes against the notion of a single, coherent document. Publishing the performance report, accountability report and financial statements separately could actually create more work for auditors and preparers and there was no recent precedent for this. **Option 3 was therefore discounted.**

18. Another factor that needed to be considered was that ARAs cannot currently be laid in Parliament without the House of Commons sitting, and they can only be published at the same time that they are laid. The House rose on 25 March and while it is due to return on 21 April, this may not be possible and there is uncertainty around when the House may be sitting over the summer.

The legal framework for government ARAs

19. In order to asses which options for reducing the reporting burden could be taken forward, it was important to assess what is possible within the existing legal framework (Government Resources and Accounts Act (GRAA) 2000) in relation to the content of government ARAs and what period of time they cover. It was also important to assess which options for 2019-20 reporting would require making changes to legislation. Given that Parliament is not currently sitting and there is a need to decide on reporting requirements as quickly as possible, it would not be viable to take forward any option that requires primary legislation unless there is overwhelming evidence that this is the correct thing to do.

20. The GRAA s5(1) specifies that resource accounts are needed for every department that prepares an Estimate. Therefore, it is not possible to exempt bodies from producing ARAs without making changes to legislation, which relates to **Options 7 and 8**. As HM Treasury considered these options it became apparent that while they significantly eased the immediate reporting burden, there were many substantial shortcomings. Not producing ARAs, even with interim accounts and/or SOPS, was almost certainly unlikely to be acceptable to Parliament and likely to lead to strong wider criticism due to the lack of transparency and accountability. It was also felt that these options could send out the wrong message and that at a time of national crisis there was an even greater need for accountability and control, and that failure to produce accounts could set a dangerous precedent.

21. These views were also raised in feedback from preparers, the relevant authorities and users. The issues of the knock-on effect for 2020-21 comparatives and the fact that many bodies have have already done a lot of work that would be now wasted were also raised. **Therefore Options 7 and 8 were discounted**.

22. **Option 6** suggests extending the reporting period so that one set of ARAs covers 24 months. S28 of the GRAA specifies that a financial year is the 12 months ending with 31 March, and therefore extending the reporting period to 24 months would require a change to current legislation. Another major problem with this option was that it moves the reporting burden from now to a year's time and we don't know when or if business as usual will resume. Reporting will also be very out of date by the time it is published and may not be appropriate, and there is no precedent for such a long period of account. These points were also raised by preparers, the relevant authorities and users. **Therefore Option 6 was discounted.**

The remaining options and preferred way forward

23. This leaves 2 options remaining from the longlist set out in paragraph 8:
    4) **Removing** some reporting requirements altogether for 2019-20, leading to detailed financial statements as per the 2019-20 FReM with streamlined annual performance and accountability reports
    5) **Removing** some reporting requirements altogether for 2019-20, leading to streamlined financial statements, accountability and performance reports.

24. Feedback from preparers has been consistent in preferring to compile full financial statements with a streamlined annual report. In general, finance staff are geared up to do this and in general they are not affected directly by Covid-19, with those who prepare the annual report more likely to be diverted to Covid-19 related work. Much relevant work has been already carried out and many of the processes at year-end are automated. It was generally felt that there were few, if any, disclosures in the financial statements where their removal would relieve a significant burden for all government entities.

25. This view is also shared by users. Feedback highlighted how it was important for the ARAs to follow an established framework – any proposal to change the reporting requirements in relation to the financial statements would require a new framework to be developed which was not practicable in the time available and may not be possible within current legislation. This would also make WGA functionally impossible and would have a significant impact on 2020-21 opening balances. This approach would also maintain a high degree of transparency and accountability at an exceptional time when public finances were likely to be under significant scrutiny. In addition, it gives certainty to preparers and means that they don't need to quickly adhere to a new financial reporting framework and ensures that opening balance figures are available for the 2020-21 accounts.

26. It is recognised that the current situation with Covid-19 will have a significant impact on many aspects of financial reporting, including on valuations, data availability and pension liabilities. Events after reporting period were also likely to be significant and there would be audit challenges, such as not being able to visit clients, with a significant number of non-standard audit reports likely. However, it is felt that it is important to produce a credible set of financial statements as per a recognised framework, and it is expected that entities and auditors will set higher materiality levels for 2019/20.

27. It was therefore generally acknowledged that it would be simpler to reduce requirements in the 'front half' of ARAs – the performance and accountability reports – and that doing so would help ease the burden for preparers. While performance reporting is important and some level of performance reporting would need to be retained, it was felt that this is the area of the ARAs that could be reduced significantly, which would save considerable time for preparers. The FLG also supported this approach.

28. HM Treasury's initial proposal is to remove the need for a performance analysis section and produce only a performance overview which concentrates on the most significant matters, such as Covid-19 responses and Brexit. Departments would also be encouraged to seek feedback from their Select Committees on content. Initial high-level discussions with Cabinet Office (who own the policy on performance reporting), NAO and Parliamentary Scrutiny Unit have taken

place and there is broad agreement on the way forward, though the precise detail is yet to be confirmed at the time of writing. It is hoped that the revised performance reporting requirements in 2019-20 will be finalised, agreed and presented to the FRAB meeting alongside this paper.

29. The accountability report may be harder to significantly streamline given the importance of the disclosures to Parliament. At the time of writing, HM Treasury are currently undergoing a detailed exercise to look at each of the accountability disclosures required in the 2019-20 FReM in detail and establish whether they should be retained or can be temporarily removed for one year only. Once this work has been completed, proposals to streamline the accountability report will be put forward to Cabinet Office (who own some of the policy on the staffing and remuneration reports), the NAO and most importantly the Parliamentary Scrutiny Unit. It is hoped that the revised performance reporting requirements in 2019-20 will be finalised, agreed and presented to the FRAB meeting alongside this paper.

30. As stated previously, any guidance would set out the minimum requirements for government bodies so that, if possible, entities would produce performance and accountability reports as per the current 2019-20 FReM. There would be no need for the 2019-20 FReM to be reissued. It would be made clear that this change would relate to 2019-20 only.

31. A summary of all the various options and the reasons why they were taken forward or discounted is provided in Appendix 1.

32. **In summary, HM Treasury have determined that the preferred way forward is Option 4 - removing some reporting requirements altogether for 2019-20, leading to detailed financial statements as per the 2019-20 FReM with streamlined annual performance and accountability reports.**

Next Steps

33. Assuming the proposal is approved by the Board, HM Treasury will look to quickly seek approval from HM Treasury ministers and then from Parliament through writing to the Chairs of the Liaison Committee, Treasury Committee, PACAC and PAC as advised by the Parliamentary Scrutiny Unit. Guidance will be published on gov.uk as soon as possible and communicated widely and extensively to all relevant stakeholders.

34. HM Treasury have been keeping in regular contact with relevant authorities, and DHSC are thinking along similar lines in terms of the requirements for the health sector, though wish to act ahead of the HM Treasury timelines. This is outlined in a separate paper to this meeting. We are also aware that CIPFA/LASAAC have announced more radical proposals. HM Treasury are confident that the approach outlined in this paper strikes the right balance between reducing the reporting burden and maintaining a reasonable level of accountability. We recognise the importance of consistency in reporting across the public sector, and without this WGA will be significantly compromised.

35. It is clear that the Covid-19 situation will have a significant impact on 2020-21 reporting and that changes may need to be made to the 2020-21 FReM, as discussed at the last Board meeting. However, it is currently unknown what the extent of that impact is, and there is an urgent need to provide a solution for 2019-20. Therefore the 2020-21 reporting requirements will be

considered further by HM Treasury and a paper will be brought to the Board at a later point in time.

Conclusion

36. It is an unprecedented time for the world in general. This paper sets out the steps that HM Treasury has taken since the Board meeting of 19 March in trying to find an effective solution for government financial reporting in 2019-20 that balances easing the burden for preparers with providing an appropriate level of accountability. HM Treasury is very conscious that the situation in relation to Covid-19 is ever-changing, and that it is impossible to judge what the situation will be at any point in the future. Given this, it is felt that the solution proposed is the best way forward at this current time and is also the consensus reached by nearly all stakeholders consulted. However, should the situation dramatically change, there may be a need to revise this position in future.

Recommendations

FRAB members are asked to urgently:

1) **approve the setting of minimum reporting requirements in 2019-20, leading to detailed financial statements as per the 2019-20 FReM with streamlined annual performance and accountability reports (Option 4)**
2) **[*if not agreed prior to the FRAB meeting*] agree that HM Treasury will agree the detailed performance and accountability reporting requirements with Parliamentary Scrutiny Unit, Cabinet Office and NAO as outlined in paragraphs 29 and 30 of this paper, and then look to issue guidance to government entities following ministerial and Parliamentary approval.**

HM Treasury
8th April

Annex 1

Summary evaluation of options for 2019-20 financial reporting

Option	Action
Option 1 - "Do Nothing" - produce 2019-20 ARAs as per the current FReM to normal timescales	**Discounted** – the scale of the challenge means that this won't be possible for a lot of entities
Option 2 – Timing – Relaxing expectations regarding when 2019-20 ARAs will be laid before Parliament. Full set of ARAs to be produced later in the year before the statutory deadline	**Partly taken forward -** administrative deadline extended by 3 months to 30 September.
Option 3 - Staggering the production of ARAs – producing financial statements for 2019/20 to similar timescales to now, and the annual report some time later	**Discounted** - no support from stakeholders, goes against the notion of a single, coherent document and could actually create more work for auditors and preparers, and there was no recent precedent
Option 4 - Removing some reporting requirements altogether for 2019-20, leading to detailed financial statements as per the 2019-20 FReM with streamlined annual performance and accountability reports	**Taken forward –** largescale support from stakeholders, maintains credibility, report to existing framework, streamlining the annual report significantly eases the reporting burden
Option 5 - Removing some reporting requirements altogether for 2019-20, leading to streamlined financial statements, accountability and performance reports	**Discounted** – little support from stakeholders, does not significantly ease the burden for preparers, may not be possible within current legislation
Option 6 - Extending the reporting period so that one set of ARAs covers 24 months. The new period would run 2019-21, and a full set of annual report and accounts for that period would be published in 2021. Instead, interim accounts and the SOPS would be published for the 2019-20 financial year	**Discounted** – shifts reporting burden from now to a year's time, no support from stakeholders, no not possible within current legislation, no precedent
Option 7 - Exempting government bodies from producing ARAs for 2019-20 and requiring that interim accounts be published instead; potentially also producing a form of the Parliamentary accountability disclosures (in particular the Statement of Outturn against Parliamentary Supply (SOPS)). No further financial reporting for 2019-20 would be required via ARAs	**Discounted** – little support from stakeholders, not possible within current legislation
Option 8 - Exempting government bodies from producing ARAs for 2019-20 without requiring any alternative	**Discounted** – little support from stakeholders, not possible within current legislation, precedent