

15 August 2011

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

(11)04

EXPOSURE DRAFT OF PROPOSED
AMENDMENTS TO THE FReM

Governance Statement

Comments to be received by 10 October 2011



HM TREASURY

**FINANCIAL REPORTING & AUDIT POLICY 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 10 October 2011. Respondents are asked to send their comments electronically to FReM.consultation@hmtreasury.gsi.gov.uk.

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



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Proposed amendments to the FReM

Introduction

Financial Reporting & Audit Policy 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.

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 10 October 2011. 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.

Amend the FReM to reflect adoption of Governance Statement	
Why the amendment is proposed	HM Treasury is consulting on changes to the FReM so that a Governance Statement can be introduced to incorporate and replace the current Statement on Internal Control (SIC). This will pull together, into one place, what is required for the existing SIC and draw in wider governance reporting, much of which is already required on a comply or explain basis as part of governance reporting and under the Companies Act in the Management Commentary.
Paragraph(s) affected by the amendment	5.1.1.c 5.3.2 5.3.3 5.3.4 5.3.5 12.3.6 14.3 14.3.4 14.3.5 Annex 2
Proposed date	2011/12

Background

1. Currently control and governance are reported separately within the resource accounts. The governance elements are mainly required to meet obligations set out in the Corporate Governance in Central Government Departments: Code of Good Practice (CG Code) and the Audit Committee Handbook. Within the private sector, local government and in internal auditing standards, governance, risk management and control are reported together. By drawing these elements together into a Governance Statement it will ensure that these aspects are more consistently and coherently reported.

2. The proposal to remove from the FReM the template currently at Annex 2 is seen as an opportunity to address an often voiced criticism that the Financial Reporting Council refer to as ‘the fungus of “boiler-plate”’. In accordance, for 2009/10 and for 2010/11 the Treasury issued FD letters (MSFD(10)03 and MSFD(11)12) advising against unnecessary duplication of template disclosures. The proposal is to remove standard wording, and to strengthen supporting guidance in Managing Public Money (draft issued under cover of DAO 01/11). This encourages organisations to set this in the context of their own specific governance and risk arrangements whilst setting out the key elements that need to be reported on.

3. The revised CG Code has now been published. This has a ‘comply or explain’ basis, with an aim of strengthening governance and accountability. This is seen as a good opportunity to position the Statement on Internal Control more firmly into the governance context of which it is clearly a part. The NAO has also identified a number of ways that the process could be strengthened and the guidance in Managing Public Money is addressing these points. This will help to ensure that Governance Statements incorporate appropriate disclosures and support better evidenced assurance reporting.

Summary of proposal

4. HM Treasury is consulting on its proposals to replace the Statement on Internal Control with a Governance Statement. For the FReM this will mean changing all of the ‘Statement on Internal Control’ references to ‘Governance Statement’ to ensure that it continues to be mandated within the accounts. We also propose removing Annex 2 to strengthen governance reporting, moving away from a template approach, with supporting guidance in Managing Public Money that addresses some of the recent findings from the NAO.

General questions (applicable to all proposed amendments)

Question 1

Do you agree with HM Treasury’s proposal to amend the FReM 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, and any proposed transition provisions, for the issue as described in the exposure draft? If not, why not, and what alternative do you propose?

FReM chapters addressed

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

FReM Chapter	Subject of amendment
Chapter 5 - Form and content of the annual report and accounts	Replace references to ‘Statement on Internal Control’ with ‘Governance Statement’. At 5.3.3 <ul style="list-style-type: none">• redraft the body text to replace references to ‘Statement on Internal Control’ with ‘Governance Statement’;• retain the distinct reference to the Scottish Public Finance Manual; and,• remove references to Annex 2, replacing with a reference to Managing Public Money.
Chapter 12 - Pensions Accounting	Replace references to ‘Statement on Internal Control’ with ‘Governance Statement’.
Chapter 14 - Whole of Government Accounts	Replace references to ‘Statement on Internal Control’ with ‘Governance Statement’.
Annex 2 – Statement on Internal Control	Delete annex.

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

Introduction

An amendment to Chapter 5 is proposed to reflect the move from a ‘Statement on Internal Control’ to a ‘Governance Statement’.

Why the amendment is proposed

The amendments outlined in this exposure draft seek to amend the FReM to pull together governance, risk and control disclosures into one place.

Proposed amendment

Content

Replace ‘5.3 Statement on Internal Control’ with ‘5.3 Governance Statement’.

Paragraph 5.1.1 c)

Replace ‘Statement on Internal Control’ with ‘Governance Statement’.

Paragraph 5.3.2 Statement of Accounting Officer’s Responsibilities

Replace ‘Statement on Internal Control’ with ‘Governance Statement’.

Paragraph 5.3.3 Statement on Internal Control

Replace title ‘Statement on Internal Control’ with ‘Governance Statement’. Redraft body text as follows:

All reporting entities covered by the requirements of this Manual shall prepare a ~~statement on internal control~~ **governance statement**. ~~A proforma is provided in Annex 2~~ **Guidance on content is provided in Managing Public Money**. ~~although it~~ **This** does not apply to Scottish **and Northern Irish** entities which should refer to the Scottish Public Finance Manual **and Managing Public Money Northern Ireland respectively**. ~~In preparing the statement, the Accounting Officer should reflect the particular circumstances in which the reporting entity operates, and adapt the proforma accordingly to ensure that the statement covers all the entity’s activities. Where a reporting entity includes in its published annual report and accounts financial statements relating to reportable activities, the reporting entity need include only a single statement on internal control~~ **governance statement**.

Paragraph 5.3.4 and 5.3.5

The effective date for the proposed amendment is for the year ended 31 March 2012.

Proposed amendment to Government Financial Reporting Manual Chapter 12 [Pensions Accounting]

Introduction

An amendment to Chapter 12 is proposed to reflect the move from a 'Statement on Internal Control' to a 'Governance Statement'.

Why the amendment is proposed

The amendments outlined in this exposure draft seek to amend the FReM to pull together governance, risk and control disclosures into one place.

Proposed amendment

Paragraph 12.3.6

Replace 'Statement on Internal Control' with 'Governance Statement'.

Effective date of amendment

The effective date for the proposed amendment is for the year ended 31 March 2012.

Proposed amendment to Government Financial Reporting Manual Chapter 14 [Whole of Government Accounts]

Introduction

An amendment to Chapter 14 is proposed to reflect the move from a 'Statement on Internal Control' to a 'Governance Statement'.

Why the amendment is proposed

The amendments outlined in this exposure draft seek to amend the FReM to pull together governance, risk and control disclosures into one place.

Proposed amendment

Paragraph 14.3

Replace 'Statement on Internal Control' with 'Governance Statement'.

Paragraph 14.3.4 and 14.3.5

Replace 'Statement on Internal Control' with 'Governance Statement'.

The effective date for the proposed amendment is for the year ended 31 March 2012.

Proposed amendment to Government Financial Reporting Annex 2 [Statement on Internal Control]

Introduction

The deletion of Annex 2 is proposed as part of the move from a 'Statement on Internal Control' to a 'Governance Statement'.

Why the amendment is proposed

The amendment seeks to discourage the use of templates, with the statement drafted in the context of the organisation's own specific governance and risks. The key elements that need to be reported will be set out in supporting guidance in Managing Public Money Annex 3.1.

Proposed amendment

Annex 2

Delete annex.

Effective date of amendment

The effective date for the proposed amendment is for the year ended 31 March 2012.