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Abstract:

The government sector in Australia has seen the introduction of accrual accounting principles in recent years. However, this process has been complicated by the presence of two alternative financial reporting frameworks in the form of a) the *Government Finance Statistics* (GFS) uniform framework and b) the accrual accounting rules specified in Australian professional accounting standards, principally AAS 31. While a variety of cash and accrual based measurements are available pursuant to these frameworks, there has been no prescription of the manner in which the alternative measures should be presented. This paper presents the findings from a case study of the 2005-06 annual budgets prepared by the Australian Commonwealth government and the governments of the six Australian States and the two Australian Territories. The study examined the headlined financial outcome (general government sector budget surplus or deficit) announced in the budget papers of the nine governments. Findings indicate the adoption of varying measurement bases and a consequent lack of inter-government comparability. A number of variations to the measurements prescribed in the accounting frameworks were also observed. The paper analyses these government budget surplus and deficit numbers in the context of fiscal responsibility, the Commonwealth government's *Charter of Budget Honesty* and the AASB's current *GAAP/GFS Convergence* project.

Introduction

Annual government budgets are a major aspect of government accountability in Australia and represent the foundation for planning and controlling government financial operations. They are regarded by many as the most important statement by a government each year, while at the same time being subject to considerable "mystique" (Higgins and Borthwick, 1990). However, despite the importance of government budgets, there has been a lack of empirical research examining and comparing the bases for the calculation and presentation of budget numbers by Australian Commonwealth, State and Territory governments. Little attention has been paid to the comparability of headline budget surplus or deficit numbers from an accounting perspective. The adoption in recent years of accrual accounting principles in the Australian general government sector makes an examination of budget surplus/deficit numbers timely, particularly as this development "has been complicated by the simultaneous use by governments of two significantly different accrual accounting frameworks" (Robinson, 2001b, p. 50). These two major alternative frameworks are the *Government Finance Statistics* (GFS) uniform framework and the accrual accounting rules specified in Australian professional accounting standards, principally AAS 31 *Financial Reporting by Governments* (Public Sector Accounting Standards Board, 1998).

Various writers have recognised the problems arising from the presence of the two alternative accounting and budgeting systems (see, for example, Robinson, 2001b; Barton, 2003, 2005; Challen and Jeffery, 2003). In examining this problem, most Australian writers have concentrated on the Commonwealth budget figures (see, for example, Barton, 2003, 2005; Sheehan, 2004, 2005). However, the issue also needs "urgent attention at the State level, where budgets are difficult to interpret (and) fiscal parameters and measures remain unclear" (Sheehan, 2005, p. 63). This study seeks to address the gap in the empirical literature by examining Commonwealth, State and Territory government budgets for the 2005-06 financial year. This will allow further insight into the observation by Robinson (2001a, p. 57) that:

> *... insofar as the move to accrual accounting was "sold" on the basis of improved fiscal transparency, it has failed. Ministers, parliamentarians and other users would appear to be very much confused by the new accrual-based Budget Papers. So even are many trained economists.*

Fiscal responsibility is a general concept that relates to issues such as sound economic management, prudent management of financial risks, promotion of national savings, stable taxation and spending policies, and intergenerational equity. Evaluation of a government's fiscal responsibility requires, inter alia, fiscal *reporting* responsibility comprising clear transparency and accountability with respect to that government's budget figures. It is this aspect of fiscal responsibility that is addressed in the present paper.

The remainder of this paper is structured as follows. The budget surplus/deficit announcements of the nine Australian governments for the 2005-06 financial years are firstly summarised, followed by a discussion of the alternative bases available for the calculation of an individual government's surplus or deficit. Findings from an examination of the annual budget surplus or deficit numbers announced in Australian government budgets for the 2005-06 financial years are then presented, particularly from an inter-governmental comparability perspective. This is followed by a discussion of the findings in the context of fiscal responsibility, the Commonwealth government's *Charter of Budget Honesty Act* (Parliament of Australia, 1998) and the

AASB's *GAAP/GFS Convergence* project (Financial Reporting Council, 2004, p. 1). A summary and conclusions section completes the paper.

Headline budget surplus/deficit numbers

A commonality of all government budgets is that they tend to focus on a single budget surplus or deficit number that is *headlined* in the relevant treasurer's budget speech and in the budget papers. The headline budget surplus or deficit is the number announced by the government as its overall performance outcome.[1] The following headline budget surplus/deficit figures were announced in the annual budget statements for the 2005-06 financial year of the Australian Commonwealth government and the governments of the six Australian States and the two Australian Territories:

> *The 2005-06 general government sector deficit is $91.5m.* (Australian Capital Territory Department of Treasury, 2005a, p. 1).
>
> *…an underlying cash surplus of 8.9 billion is expected in 2005-06…* (Commonwealth Treasury, 2005, p. 1-1)
>
> *This budget will deliver a net operating surplus of $51 million in 2006-06….* (Government of South Australia, 2005a, p. 2)
>
> *…we are forecasting a general government operating surplus of $521 million in 2005-06…* (Government of Western Australia, 2005a, p. 2)
>
> *The Budget result for 2005-06 will be an operating surplus of $303 million.* (New South Wales Treasury, 2005a, p. 21)
>
> *Our fiscal strategy targets were re-set in 2004 and included deficits from 2005-06. With the budget returning to balance in 2008-09…* (Northern Territory Treasury, 2005a, p. 5)
>
> *…on an adjusted basis there is an Underlying Fiscal Surplus of $44.5 million.* (Parliament of Tasmania, 2005, p. 8)
>
> *The Budgeted operating surplus for 2005-06 is $934 million*. (Queensland Government, 2005a, p. 12)
>
> *…the government will meet its commitment to deliver a surplus in excess of $100 million – with an operating surplus of $365 million in 2005-06...* (Victorian Department of Treasury and Finance, 2005a, p. 3)

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[1] This paper uses the term *headline* outcome in a general sense as indicating the budget deficit or surplus number that is given prominence in the budget papers as the overall budgeted outcome. It is also referred to as the "bottom-line" figure (Jensen and Wanna, 2003, p. 264).

How comparable are the above headline budget numbers? It can be seen from the various quotes that there is some variation in terminology used, with governments headlining surpluses such as “operating surplus”, “net operating surplus”, “underlying fiscal surplus”, “underlying cash surplus” or, simply, “surplus”. Any meaningful understanding of, and comparisons between, the above budget announcements obviously requires a knowledge of the specific bases used to derive the surplus/deficit numbers. In particular, meaningful comparisons of the headline budget figures are not possible if they have not been prepared on a common basis.

Alternative bases for the preparation of government budgets

Throughout the past two decades, Federal and State governments of varying political persuasions have pursued and implemented significant agendas of reform within the public sector (Carnegie and West, 2003; Guthrie, 1998). These reforms, referred to generally under the term “new public management” (Hood, 1991) have emerged as a response to a philosophical drive for more “efficient”, “effective” and “accountable” public services (Guthrie, Parker and English, 2003). Not unexpectedly, these reforms have impacted on public sector financial reporting.

Historically, governments in Australia adopted a cash basis of budgeting and accounting. However, when the effects of the various reforms started to impact on budget departments in the early 1990s, a demand arose for performance to be reported in terms of accrual financial information (Guthrie, 1998, p. 7).[2] Ramifications were felt in the budgeting arena as accrual accounting began to impact on government financial reporting, and a number of alternative cash and accrual frameworks have subsequently been developed for government budgeting purposes. The major alternative frameworks are the *Government Finance Statistics* (GFS) uniform framework and the accrual accounting rules specified in Australian professional accounting standards, principally AAS 31 *Financial Reporting by Governments*.

Government Finance Statistics (GFS) framework

The uniform *Government Finance Statistics* (GFS) reporting framework, the latest version of which was published in October 2003, is “a specialised financial reporting

[2] For a discussion of cash versus accrual accounting and accrual accounting developments in the public sector, see, for example, Australian Society of Certified Practising Accountants (1993), Carpenter (1990), Funnell and Cooper (1998), Guthrie (1998), Ryan (1998, 1999) and Walker (1990).

system designed to support economic analysis of the public sector" (Commonwealth Treasury, 2004, p. 8-2). Developed by the Australian Bureau of Statistics, the framework is based on the international equivalent developed by the International Monetary Fund (IMF)[3] and on the United Nations *System of National Accounts* (United Nations, 1993). The aim of the GFS framework is to "meet the community's demand for standardised and detailed financial information about the activities of all Australian governments" (Australian Bureau of Statistics, 2003, para. 1.3). The GFS framework provides for the recording of data on an accruals basis, but with supplementary data recorded on a cash basis (Australian Bureau of Statistics, 2003, para. 2.2).[4]

A number of separate financial statements are produced pursuant to the GFS conceptual framework, these being an operating statement, a cash flow statement, a balance sheet and a statement of other economic flows. Alternative budget surplus or deficit numbers can be drawn from the budgeted operating and cash flow statements, as explained below.

The operating statement presents details of revenue and expense transactions and the net acquisition of non-financial assets for an accounting period. The format of the operating statement results in two measures that can be considered as alternative budget surplus/deficit outcomes. The first section of the operating statement comprises GFS revenues less GFS expenses arising from transactions, this resulting in the *GFS net operating balance*. The revenues and expenses are calculated on an accruals basis, with depreciation included as an expense. The GFS net operating balance represents the "change in net worth due to transactions" (Australian Bureau of Statistics, 2003, para. 2.111). This net operating balance (surplus or deficit) is conceptually the most similar GFS budget outcome measure to conventional net income (profit or loss) calculated pursuant to Australian accounting standards and generally accepted accounting principles. However there are some notable differences that will be mentioned later.

The second section of the GFS operating statement deducts the net acquisition of non-financial assets from the net operating balance, resulting in the *GFS net*

3 The latest version of the IMF's GFS framework was issued in 2001 (International Monetary Fund, 2001).

4 When originally introduced, the GFS adopted an economic cash-based approach rather than an accounting accruals-based approach (Allan, 1993, p. 79).

lending/borrowing balance. The net acquisition of non-financial assets, also referred to as net capital investment, measures the change in the government's stock of non-financial assets due to transactions. Hence, in general terms, the net lending/borrowing balance comprises the net operating balance less net acquisitions of non-financial assets, with depreciation expense added back to avoid double counting.[5]

To illustrate these calculations, Table 1 presents a summary of the 2005-06 operating statements for the Australian Commonwealth and New South Wales governments. The table indicates GFS net operating balances (surpluses) amounting to $8,990m for the Commonwealth government and $303m for the New South Wales government. Deducting total net acquisitions of non-financial assets from the GFS net operating balance results in a net lending balance (surplus) of $7,970 in the Commonwealth budget and a net borrowing balance (deficit) of $979m for New South Wales.

[Insert Table 1 about here]

Also prepared pursuant to the GFS framework is a cash flow statement, indicating the budgeted net increase or decrease in cash held (Australian Bureau of Statistics, 2003, para. 2.119). The GFS cash flow statement is similar in concept to the parallel private sector cash flow statement prescribed by AASB 107 *Cash Flow Statements* (Australian Accounting Standards Board, 2004). Like AASB 107, the GFS cash flow statement prescribes that cash flows be dissected between operating, investment and financing activities. A difference under the GFS framework is that cash flows from investment activities are further dissected according to whether they are investments in a) non-financial assets, b) financial assets for policy purposes, or c) financial assets for liquidity management purposes.[6]

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5 A positive (surplus) net lending/borrowing balance indicates that the government is budgeting, on a net basis, to 'purchase financial assets and/or repay liabilities in order to defray surplus funds' (Australian Bureau of Statistics, 2003, para. 2.112). A negative (deficit) net lending/borrowing balance indicates that the government is budgeting to 'liquidate financial assets, incur liabilities and/or increase equity in order to finance current operations and capital acquisition' (Australian Bureau of Statistics, 2003, para. 2.112).

6 The distinction between investments in financial assets for policy and liquidity management purposes is based on the government's motivation for acquiring the assets. The acquisition of a financial asset is treated as being for policy purposes when the acquisition is for the purpose of implementing or promoting government policy. When a financial asset is acquired for the purpose of managing a government's cash reserves, the acquisition is treated as being for liquidity management purposes (Australian Bureau of Statistics, 2003, para. 2.119).

In summary, the GFS framework specifies three measures that can be considered as budget outcome measures, these being a) the net operating balance (GFS operating statement), b) the net lending/borrowing balance (GFS operating statement) and c) the cash deficit or surplus (cash flow statement).

Australian accounting standards

In parallel with the Australian Bureau of Statistics GFS framework, the Australian accounting profession has developed a number of public sector accounting standards. AAS 31 *Financial Reporting by Governments* (Public Sector Accounting Standards Board, 1998) is the public sector standard that is applicable to Australian Commonwealth, State and Territory governments. As AAS 31 considers these governments to be reporting entities, they are required to prepare general purpose financial reports "because there are users who depend on the financial information contained in them for making and evaluating decisions about the allocation of resources" (Public Sector Accounting Standards Board, 1998, para. 3.2). Financial report users are specified to include "parliamentarians, the public, providers of finance, the media and other analysts" (Public Sector Accounting Standards Board, 1998, para. 3.2).[7]

Accounting standard AAS 31 requires the adoption of the full accrual basis of accounting. While the standard applies for financial reporting purposes, the same basis of accounting can be used for preparing budgeted financial information, and several governments have provided such information in their budget papers.

As noted earlier, the GFS net operating balance is conceptually the most similar GFS budget outcome to conventional net income calculated pursuant to Australian accounting standards, principally AAS 31 for governments. Both measures are derived by deducting expenses from revenues, but there are some notable differences between the two frameworks in the manner in which items are recognised. In particular, the major difference stems from the fact that the GFS framework only recognises revenues and expenses that are transactions-based. Major specific differences relate to accounting for asset writedowns (treated as operating expenses pursuant to AAS 31 but as negative equity revaluations pursuant to the GFS

[7] For a discussion of the manner in which general purpose financial reporting became a significant issue for governments in Australia, see Ryan (1998).

framework), other gains and losses on assets (not included as revenues/expenses under GFS), bad and doubtful debts expense (not recognised under the GFS framework), swap interest revenue and expense (not recognised under GFS), and the acquisition of defence weapons platforms (capitalised and depreciated under AAS 31 but treated as an expense at the time of acquisition under GFS rules).[8]

A major observation at this point is that a structure exists for various budget statements to be prepared under alternative frameworks. However, there is no prescription of the priority to be given in an individual government's budget papers to the alternative statements or to the order in which they are to be presented. Further, there is no prescription of which framework (or frameworks) should be used as the basis for the government's headlined budget surplus or deficit number. This is particularly a problem where the alternative frameworks provide materially different budget outcome numbers. Taking the New South Wales government budget for the 2005-06 financial year as an example, alternative budget surplus/deficit outcomes under the various frameworks are: a) GFS net operating balance *surplus* of $303m, b) GFS net lending/borrowing *deficit* of $979m, c) GFS cash flow statement cash *surplus* of $415m, and d) AAS 31 budget *surplus* of $471m.

Given the different measures available under the alternative frameworks, Challen and Jefferey (2003, p. 50) argue that the "current dual reporting regime causes considerable confusion for financial report users and may encourage governments to indulge in presentation shopping." From a fiscal responsibility perspective, the selection of alternative measures by different governments in announcing their budget expectations can result in reduced accountability and transparency.

Case study of Australian Commonwealth, State and Territory Government budgets

Budget headline surplus/deficit measurement methods: Inter-governmental comparability

The aim in this section is to examine the bases for the headline financial result (general government sector surplus or deficit) presented in the 2005-06 budgets of the Australian Commonwealth government, the six Australian States and the two

[8] See Australian Bureau of Statistics (2003, chapter 7) for a detailed discussion of the accounting policy differences between the GFS framework and AAS 31.

Australian Territories. Such an examination will shed light on the comparability of the headline measurement bases across the nine government budget settings. A listing of the measurement bases adopted for the headline surplus or deficit in the nine government budgets for the 2005-06 year is presented in Table 2.

[Insert Table 2 about here]

The GFS net operating balance was the basis for the headlined surplus/deficit figures in the 2005-06 budgets of New South Wales, Queensland, South Australia, Victoria and Western Australia. The Commonwealth budget utilised an "adjusted" cash basis and Tasmania an "adjusted" GFS net lending/borrowing balance. Of the Territories, the Australian Capital Territory headlined a professional accounting standards (AAS 31) based deficit while the Northern Territory headlined a cash based deficit.

A summary of the alternative bases adopted by the nine governments is provided in Table 3. A majority of the governments (five of the nine) adopted the GFS net operating balance basis for their 2005-06 headlined budget outcome. Moreover, these were all States, meaning that five of the six States adopted a comparable basis, with only Tasmania headlining a number calculated on an alternative basis. However, while five of the States presented headline deficit/surplus numbers calculated on a common basis, there was no commonality among the four remaining governments.

[Insert Table 3 about here]

Further, of the five alternatives adopted, two governments (the Australian Commonwealth and Tasmania) moved to measures representing adjustments to, and therefore departures from, the bases prescribed in the relevant accounting frameworks. The Commonwealth government's budget headlined an "underlying" (adjusted) cash surplus of $8,921m. This compares to the "cash" surplus disclosed in the GFS cash flow statement of $9,383m.[9] The difference is represented by the deduction of $462m of "Future Fund earnings" from the cash surplus figure.[10] These Future Fund earnings are projected to increase to $943m for 2006-07, $997m for 2007-08, and $1,054m for 2008-09 (Commonwealth Treasury, 2005, p. 13-4).

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[9] This cash surplus was represented by net cash flows from operating activities and investments in non-financial assets.

[10] For the 2005-06 year, these Future Fund earnings were represented by Telstra dividends.

The government justifies this accounting treatment on the basis that the Future Fund earnings “will be reinvested to meet future superannuation payments and are therefore not available for current spending” (Commonwealth Treasury, 2005, p. 2-9). However, in representing a case of a government adopting a measurement base for its headlined surplus that is not in conformity with one of the bases prescribed in the alternative reporting frameworks, the Commonwealth’s accounting treatment raises the following significant accountability and transparency issues:

- Is it appropriate to adopt accounting policies in the current budget that anticipate the establishment of the Future Fund prior to the structure of that fund being determined and established by legislation?
- The GFS cash flow statement aims to summarise all cash flows for the general government (budget) sector. However, will the Future Fund, when established, not be part of the general government sector? Given that the revenues and expenses flowing through the fund would otherwise have been reported in the general government sector cash budget figures, it would seem difficult to sustain this argument.
- The explanation in the budget papers suggests that future superannuation payments to be paid from the Future Fund will not be reported in the cash budget figures. Is it appropriate to exclude such significant payments from the budget, and will the government be able to make other outlays from the Future Fund that will similarly be excluded? This is particularly an issue when it is the “underlying” cash surplus that the government headlines in its budget speech and budget papers.
- What reporting requirements will the Future Fund be required to comply with, and in what form will the Future Fund accounts be made available to all stakeholders, including taxpayers and the general public? Will there be the same transparency as there is for the figures presented in the primary budget papers?
- If a public company attempted to set up a similar structure whereby certain assets, liabilities, revenues and expenses were not included in its accounts, wouldn’t that be seen to represent a case of “creative accounting” and “off-balance sheet financing”?

The other government to headline a budget figure not in accordance with any of the prescribed frameworks was Tasmania. The budget speech and budget papers headlined an “underlying fiscal surplus” of 44.5m, this being achieved by adding back $50m of “Special Capital Investment Funds Expenditure” to the GFS net lending/borrowing balance deficit of $5.5m. This adjustment had not been made in Tasmania’s prior year budget, and the government, by making this adjustment, was able to headline a surplus rather than a deficit. It is also pertinent to note that Tasmania’s GFS net operating balance surplus amounted to $28.7m. Hence, Tasmania’s headlined “underlying fiscal” surplus of $44.5m was still 55.1 percent higher than on the basis adopted by the other States in their 2005-06 budgets.

Comparison of financial reporting effects of headline and GFS measurement methods

Despite the above observations, the lack of a common basis for measurement of the headlined surplus or deficit by the nine governments may not be a significant problem if the effects of the different bases did not have material financial reporting effects. Obviously, determination of whether the effects of the adoption of different measurement bases have been material requires comparison with some common measurement base. Fortunately, and as explained earlier, the nine governments present budget figures in accordance with the uniform GFS framework. However, it is important to emphasise that, in all cases, such figures are only observable by a careful examination of the detail within the budget papers. In most cases, the figures calculated on a GFS basis are only disclosed in later chapters or in appendices within the various government budget papers.

Table 4 presents a comparison of the headlined surplus or deficit figures for the four governments not headlining the GFS net operating balance with the figure had the GFS net operating balance method been adopted. The net operating balance basis is selected as the most appropriate for comparison purposes as it is the GFS measure that is most consistent with the accrual basis of accounting and is the method that has the highest frequency of adoption for the headline outcome across the nine governments.

[Insert Table 4 about here]

The headline surplus for the Australian Commonwealth is only 0.8% lower than under the GFS net operating balance method. The Northern Territory, however, has headlined a $68m cash-based deficit when it could have reported a $34m surplus if it had adopted a GFS net operating balance basis. Exhibiting opposite directional effects, the Australian Capital Territory and Tasmania adopted methods that enabled them to headline materially better surplus/deficit numbers. The Australian Capital Territory's $91.5m headlined deficit would have been a $356m deficit had the GFS net operating balance been headlined. Likewise, Tasmania's $44.5m surplus would have amounted to only $28.7m had the GFS net operating balance been headlined. As an overall conclusion, the differences caused by the adoption of differing measurement bases by three of the nine governments (the Australian Capital Territory, the Northern Territory and Tasmania) had material financial reporting effects with respect to their headlined budget announcements.

Inter-temporal comparability issues

A further relevant issue can be raised here regarding inter-temporal comparability. Wines and Scarborough (2004) document the budget headline measurement bases adopted by the nine governments for the 2004-05 financial year. Comparison with the headline bases for the 2005-06 year presented in Table 2 of the present paper indicates that only four of the nine governments (the Australian Capital Territory, the Northern Territory, Queensland and Western Australia) were consistent in the measurement basis for their headlined budget outcome figures across the 2004-05 and 2005-06 years.

Of the five governments changing the measurement base for their headlined outcome in the 2005-06 year, three (New South Wales, South Australia and Victoria) moved to the GFS net operating balance method.[11] The other two governments changing their headline measurement basis, the Commonwealth and Tasmania, both moved in their 2005-06 budgets to "adjust" the GFS basis they had used in the prior year. Hence, it is appropriate to highlight at this point the lack of inter-period comparability in the headlined outcome numbers in a majority (five of the nine) of the government budgets.

[11] New South Wales and South Australia changed from the GFS net lending/borrowing balance basis, while Victoria changed from the AAS 31 basis.

Discussion of fiscal responsibility issues

Accountable budgetary processes are a key mechanism of stable, democratic societies (Wanna, Kelly and Forster, 2000), with fiscal responsibility dependent on clear accountability, transparency, and on limited scope for uncertainty and confusion in government budget reporting. However, it was claimed over a decade ago that budgetary, accounting and financial reporting formats and standards varied between Australian governments and that a lack of consistency in approach was a serious problem (Allan, 1993, p. 77). Since that time, substantial developments have occurred with moves to accrual-based systems and more standardised rules in the form of the GFS framework and professional accounting standards, such as AAS 31.

These accounting reforms have resulted in a proliferation of information in Australian Commonwealth, State and Territory government budgets, with budget surplus/deficit information for the general government sector being provided on various cash and accrual bases. However, there has been no detailed prescription of the manner in which these alternative measures should be presented in government budget papers. This has allowed different governments to give prominence to alternative budget outcomes and to be selective in the headline budget surplus/deficit outcomes they announce. It has also allowed governments in some cases to present budgeted outcomes calculated on bases that represent a departure from the prescribed frameworks, hence resulting in even greater variability. The significant accountability and transparency issues raised by the accounting treatment for the Commonwealth's "Future Fund", as discussed in an earlier section, are particularly illustrative of fiscal responsibility concerns caused by a lack of detailed prescription in the frameworks.

Guthrie (1998, p. 14) alluded to the political impacts and ramifications of government budget statements with the following statement:

> *Terms such as 'budget surplus' or 'budget deficit' are potent political symbols. Politicians claim success if they have 'reigned in' a deficit or 'returned' a surplus, or 'balanced' a budget… The calculation of deficit or surplus may be affected by the way that the government earmarks expenditure as 'capital' or 'recurrent' and also the type of accounting system they report with.*

Robinson (1996b) referred to the propensity of politicians to exploit weaknesses in public sector accounting to misrepresent the state of public finances, and observed that the main target of misrepresentation was the budget bottom line (deficit or surplus) number. Despite efforts to implement more uniform government accounting principles since the time of the above observations, the findings of the present study of the 2005-06 budgets of the nine Australian governments suggest the potential for confusion due to the adoption of varying measurement bases for the announcement of budget outcomes. The adoption of these varying measurement bases hampers both inter-governmental and inter-period comparability. Given this background, the study's findings are discussed in the following two subsections in the context of fiscal responsibility legislation/guidelines and the FRC's GAAP/GFS Convergence project.

Fiscal responsibility legislation and guidelines

Budgets are evaluated according to whether they are fiscally (economically) responsible. Higgins and Borthwick (1990, p. 46) point out that if a budget is perceived to fail this "often ill-defined" economic responsibility test, "the government of the day is bound to come under increasing pressure which, if not rectified, will be reflected in the ballot box." Wanna *et al.* (2000, p. 4) also stress that "budgets have the potential to do governments enormous electoral harm." Hence, there is considerable interaction between budgets as both economic and political documents.

Fiscal responsibility involves, for example, "ensuring that fiscal decisions are not dominated by present considerations at the expense of future ones" (Robinson, 1996a, p. 419). It represents a "commitment on the part of government to reducing heavy debt burdens on future generations" (Albon, 1995, p. 17). An example of legislation seeking to assist in ensuring fiscal responsibility is the Commonwealth government's *Charter of Budget Honesty Act 1998* (Parliament of Australia, 1998). The stated purpose of the Charter is to improve fiscal policy outcomes by requiring fiscal strategy to be based on principles of sound fiscal management and by facilitating public scrutiny of fiscal policy and performance (sch. 1, cl. 1). The principles of sound fiscal management, specified in Part 3 of the Charter, require the Commonwealth government to:

- manage financial risks prudently, including by maintaining general government debt at prudent levels;
- ensure fiscal policy contributes to achieve adequate national savings and to moderate cyclical fluctuations in economic activity;
- pursue spending and taxing policies that are consistent with a reasonable degree of stability and predictability in the level of the tax burden;

- maintain the integrity of the tax system; and
- ensure that policy decisions have regard to their effects on future generations.

Robinson (1996a) argues that, while legislation cannot *compel* fiscal responsibility, it can play an important role in *encouraging* fiscal responsibility. From this viewpoint, he argues that the Charter of Budget Honesty is best viewed as fiscal *reporting* rather than fiscal *responsibility* legislation, "notwithstanding the superficial impression created by the principles of sound financial management which it articulates" (Robinson, 1996a, p. 421).[12]

Nevertheless, whether the Charter is viewed from a fiscal responsibility or fiscal reporting perspective, this study highlights the incomplete nature of the legislation in several respects. The Charter endorses an accrual accounting framework,[13] and the government specifically states that accrual accounting is at the heart of its budgeting and reporting framework (Department of Finance and Administration, 2003). However, while various accruals-based figures are presented in the budget papers, the Commonwealth government has chosen to headline an adjusted cash-based surplus that represents a departure from the reporting rules. A second government, Tasmania, also headlined a surplus figure not in accordance with the prescribed frameworks. These departures do not appear consistent with the full transparency that fiscal responsibility requires, yet they are explicitly allowed. The Charter states that the budget report is to be prepared in accordance with external reporting standards but that disclosure is required of "any ways in which the report departs from those standards" (sch. 1, cl. 3(b)). This can be contrasted with the situation of companies reporting pursuant to the Australian *Corporations Act 2001*, where serious consequences arise from failure to comply with applicable accounting standards.

In the Australian context, taxpayers and the general community will have more complete insights into the fiscal responsibility of the Commonwealth, the States and the Territories if these governments present their budget figures, and particularly their headline surplus or deficit numbers, on a common basis and in an unambiguous manner. Transparency in this respect requires all these governments to have common

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[12] The status of the legislation in terms of legal enforceability is also contestable, given that "nothing in the Charter of Budget Honesty creates rights or duties that are enforceable in judicial or other proceedings" (Parliament of Australia, 1998, s. 3).

[13] An accrual accounting framework is endorsed as the "external reporting standards" on which the Charter is based is defined to mean the GFS framework and the accounting profession's public sector accounting standards (Parliament of Australia, 1998, sch 1, cl. 3).

charters specifying common budget reporting rules. Robinson (1996a, p. 423) correctly states that "it would be a serious mistake to assume that there is, or could ever be, a set of accounting measures capable of giving precise, unambiguous and readily verifiable expression to given fiscal responsibility principles", and that "there is no unique set of accounting measures that is both free of conceptual ambiguities and generally acknowledged to be superior to all others." However, the presence of alternative measures under the different reporting frameworks only serves to exacerbate accountability problems, and particularly given that governments can depart from the prescribed rules without any consequences. The inter-governmental and inter-period comparability problems highlighted in the present study make it difficult to evaluate and compare the fiscal responsibility of the different governments in Australia. Such evaluations and comparisons are currently only possible by delving into the depths of the budget papers. The specification of more consistent budget reporting guidelines applying equally to the Australian Commonwealth, State and Territory governments in *Charter* type legislation or pronouncements would allow for more transparent insights into the fiscal responsibility of Australian governments.

No single calculation, or set of calculations, of a government's surplus or deficit can provide a complete picture. Nevertheless, the rules specified in agreed frameworks, such as in the GFS framework, do provide a standardised basis enabling economic and financial information to be provided that meets specified relevance, reliability and comparability qualities. The alternative figures under the framework provide different information. For example, the net operating balance shows an accrual-based measurement of revenues less expenses, inclusive of depreciation. The net lending/borrowing balance takes into account the net acquisition of non-financial assets in the surplus/deficit measure. The cash flow statement provides cash-based information with respect to operating, investing and financing activities.

The major problem identified by this study is that governments are able to be selective in the choice of the aggregate or aggregates to be emphasised in their budget, and they can depart from the prescribed rules if they wish. Accordingly, from accountability, transparency and fiscal responsibility perspectives, an obvious recommendation is to require governments to clearly present the alternative major aggregates, prepared in accordance with the prescribed framework rules, in the opening sections of their budgets. Governments could still be free to provide whatever additional information they wished to present, but the standardised information would be clearly shown "up-front" to allow improved inter-governmental and inter-period comparability. It would also assist in emphasising that a government surplus or deficit number is not a single, definitive measure that can provide a complete summary of budgeted performance.

GAAP/GFS Convergence

The findings from this study also have implications for Australia's current developments in implementing international accounting standards. In addition to Australia's adoption of international financial reporting standards from 1 January 2005 for companies reporting pursuant to the *Corporations Act 2001*, the Australian Financial Reporting Council (FRC) also has a similar strategic direction for public sector financial reporting. This strategy aims for the AASB to "pursue as an urgent priority the harmonisation of Government Finance Statistics (GFS) and Generally Accepted Accounting Principles (GAAP) reporting" (Financial Reporting Council, 2004, p. 1).[14] The first phase of the strategy will focus on whole-of-government financial reporting by Commonwealth, State and Territory governments, commencing with full year reporting periods ending on 30 June 2006 (Financial Reporting Council, 2004). The first exposure draft issued as part of this strategy, *ED 142 Financial Reporting of General Government Sectors by Governments*, was released in July 2005 (AASB, 2005).[15]

The FRC's strategy, though, "does not direct the AASB to develop standards for budgetary reporting" (Financial Reporting Council, 2004, p. 1). Given the findings from the present study, this could be problematic. This study has highlighted that the GFS rules currently represent the only common reference point for comparing the budget numbers of the various governments.[16] If the revised reporting rules developed pursuant to the FRC's convergence strategy are not also implemented for budgetary purposes, the problems that presently exist in attempting between-government and inter-period comparisons of budget outcomes will continue.

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[14] GAAP reporting includes the rules prescribed in Australian professional accounting standards, including AAS 31.

[15] It should be highlighted that, while the original intention was for the first phase of the convergence project to focus on *whole-of-government* reporting, the AASB's exposure draft has been limited to the *general government sector* (that is, the budget sector, excluding public non-financial corporations and public financial corporations).

[16] Although, to emphasise a point noted previously, only detailed, careful and lengthy examination of the budget papers by an individual possessing specialist accounting knowledge in this area enables such comparisons to be made.

The new exposure draft, *ED 142*, requires the general government sector (GGS) financial report at the end of the financial period to disclose, for comparison purposes with the final financial report figures, the original budget (AASB, 2005, para. 57). However, the original budget is to be presented in the financial report "on a basis that is consistent with the basis prescribed for the GGS financial report" (AASB, 2005, para. 57(a)). In this respect, the exposure draft states that "to the extent the ex ante original GGS budget is not consistent with the information in the financial statements, the ex ante budget basis is restated for ex post budget purposes to align with the accounting basis" (AASB 2005, para. 61).

Accordingly, and this is extremely significant in the context of the findings of the present study, the proposals will implicitly allow governments to present *ex ante* budgets on bases, and incorporating accounting assumptions, that depart from the accounting standard with which the final *ex post* annual financial reports must comply.

Consider this in the context of a government that presents its 2006-07 budget in May 2006. The full year financial report for the 2006-07 year for this government will not be publicly released until some 16 months later, around September 2007.[17] It is only at this point that the government will be compelled to adjust its original budget to the basis on which the final financial outcome report has been prepared (that is, in accordance with applicable financial reporting standards). It is also only then that the extent to which the government, some 16 months earlier, departed from the rules prescribed in applicable accounting standards will be observable. By that stage, the budget for the ensuing 2007-08 year will already have been released and the focus will inevitably have moved away from the earlier year's budget.

Summary and Conclusions

Accountable budgetary processes are a key mechanism of stable, democratic societies (Wanna *et al*., 2000). However, government budgets are not merely financial but are also about political power. As budgets are influenced by the wider power structures in society, they are "of vital interest to all members of society affected by them" (Wanna *et al*., 2000, p. 2). When it comes to budget reporting, a seemingly straightforward

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[17] Under the Charter of Budget Honesty, for example, the final budget outcome report for the Commonwealth government is to be released, with some exceptions, not later than three months after the end of the financial year (Parliament of Australia, 1998, cl. 18(1)).

concept such as the overall government deficit or surplus "hides a minefield of ambiguities, questions of usage, and conflicting definitional issues" (Blejer and Cheasty, 1991, p. 1675).

This study examined the headlined general government sector budget surplus or deficit announced in the 2005-06 budget papers of the Australian Commonwealth government and the governments of the six Australian States and the two Australian Territories. Findings indicate the adoption of varying measurement bases and a consequent lack of inter-government comparability in the headlined budget outcome numbers. A number of variations to the measurements prescribed in the accounting frameworks were also observed, and limitations in inter-period comparability were also identified.

The lack of comparability and potential for confusion indicated by this study's findings has been caused by accounting reforms that have specified a variety of cash and accrual based measurements. As there has been no prescription of the manner in which these alternative measures are to be presented, it is not surprising that different governments have chosen to headline different outcome numbers in their budget announcements and budget papers. This diversity of practice has not been limited by fiscal responsibility legislation, such as the Commonwealth government's *Charter of Budget Honesty Act*, which specifically allows departures from the prescribed reporting rules. The findings were also analysed from the perspective of the new reporting rules proposed in the first AASB *GAAP/GFS Convergence* project exposure draft, *ED 142 Financial Reporting of General Government Sectors by Governments*. The analysis concluded that the proposed accounting standard will not prevent the scope for the inter-governmental and inter-temporal comparability limitations identified in this paper. Further, the adoption in government budgets of measurement bases and accounting assumptions departing from the stipulated external reporting rules will not be proscribed by the rules proposed in *ED 142*.

The ability to evaluate a government's fiscal responsibility requires, inter alia, clear transparency and accountability with respect to the budget figures presented by that government. This paper, though, has raised a number of significant fiscal reporting concerns that impinge on the ability to undertake such an evaluation.

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Table 1
Summary of Australian Commonwealth and New South Wales Government 2005-06 GFS Operating Statements

	C/W $m	NSW $m
GFS revenue	252 511	43 186
GFS expenses (including depreciation)	243 521	42 883
Net operating balance [surplus]	**8 990**	**303**
Less net acquisition of non-financial assets:		
Purchase of non-financial assets	2 920	3 730
less sales of non-financial assets	(285)	(547)
less depreciation	(2 140)	(2 087)
plus change in inventories	340	(2)
plus other movements in non-financial assets	185	188
Total net acquisition of non-financial assets	**1 020**	**1 282**
Net lending/borrowing balance [surplus/(deficit)]	**7 970**	**(979)**

(GFS = Government Finance Statistics)

Table 2
Bases for Headline 2005-06 Budget Surplus/Deficit Measurements

Government	Budget Bases
Commonwealth:	
C/W of Australia	'Underlying' (adjusted) Cash
States:	
New South Wales	GFS Net Operating Balance
Queensland	GFS Net Operating Balance
South Australia	GFS Net Operating Balance
Tasmania	'Underlying' (adjusted) GFS Net Lending/Borrowing
Victoria	GFS Net Operating Balance
Western Australia	GFS Net Operating Balance
Territories:	
Australian Capital Territory	Austn. professional accounting standards (inc. AAS 31)
Northern Territory	GFS Cash

Table 3
Bases for Headline 2005-06 Budget Surplus/Deficit Measurements

Basis for Calculation of *Headline* Outcome	Frequency
GFS Cash	1
'Underlying' Cash	1
Austn. professional accounting standards (inc. AAS 31)	1
GFS Net Operating Balance	5
'Underlying' GFS Net Lending/Borrowing	1
Total number of government budgets:	9

Table 4
Comparison of Headline and GFS Net Operating Balance Budget Outcomes

Government	Budget *Headline* Reported (1)	GFS NOB Outcome (2)	Difference (1) – (2)	Difference as % of GFS NOB Outcome
Commonwealth of Australia	\$ 8 921m surplus	\$8 990m surplus	–\$69m	–0.8%
Australian Capital Territory	\$91.5m deficit	\$356m deficit	+\$264.5m	+74.3%
Northern Territory	\$68m deficit	\$34m surplus	–\$102m	–300.0%
Tasmania	\$44.5m surplus	\$28.7m surplus	+\$15.8m	+55.1%