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# **Standing Committee on Government Operations and Estimates**

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**EVIDENCE**

**Tuesday, September 26, 2006**

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**Chair**

**The Honourable Diane Marleau**

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## Standing Committee on Government Operations and Estimates

Tuesday, September 26, 2006

• (1115)

[English]

**The Chair (Hon. Diane Marleau (Sudbury, Lib.)):** I call the meeting to order.

As you will recall, we had made a decision last spring to study the accrual process at the federal level. We had arranged that the Auditor General and officials from Treasury Board would meet with us last week. Unfortunately, we had to cancel; however, they're here today, and I'd like us to get under way as quickly as possible.

I'll turn it over first to the Auditor General, who can introduce the people with her, and then to the people from the Office of the Comptroller General.

Madame.

[Translation]

**Ms. Sheila Fraser (Auditor General of Canada, Office of the Auditor General of Canada):** Thank you, Madam Chair.

I want to begin by thanking you for inviting us to participate in a briefing designed to assist the Committee as it considers an issue raised in our May 2006 *Status Report*. In Chapter 1, "Managing Government: Financial Information", we discussed the need for the government to address the issue of accrual-based budgeting and appropriations at the departmental level.

With me today are Mr. Douglas Timmins, Assistant Auditor General and Mr. Clyde MacLellan, Principal, who are both responsible for that audit.

This Committee's initiative to do an in-depth study of accrual-based budgeting and appropriations is an excellent idea. It follows a series of recommendations by the Public Accounts Committee that the government implement accrual-based budgeting and appropriations. I hope the presentation today will enhance your understanding of the concepts and issues surrounding this matter.

As I said in my opening statement to this committee on June 13, the concepts of accrual accounting, accrual-based budgeting and appropriations, and accrual-based financial information can be difficult for non-accountants to understand.

For that reason, we provided the Committee with a copy of a presentation that my Office and Treasury Board Secretariat had given to parliamentarians when the government issued its first set of full-accrual summary financial statements.

[English]

We have incorporated elements of that presentation into our briefing today. It illustrates accrual accounting concepts, explains the benefits of using this form of financial information, and highlights key points with respect to the matter of accrual-based budgeting and appropriations.

Although the government has implemented accrual elements in its government-wide budgeting activities, I noted in my opening statement of June 13 that departments and agencies are not using accrual financial information effectively. This is because their budgets and appropriations are based largely on the cash method of accounting. Also, in my opinion, the failure to use accrual information was a factor when departments chose the less cost-effective option for office accommodation, as noted in our chapter on the acquisition of leased office space. As you will recall, we discussed that matter with the committee at its June 1 meeting.

While we recognized in our financial information chapter that a department's cash requirements and cashflow management will continue to be important information for Parliament, we concluded that Parliament would be better served if it also received information in the estimates and appropriations based on accrual accounting. Such an approach would make the process more consistent with the one used in the government's financial reporting of results.

The government has been studying this issue since 1998 but hasn't established a clear position on the direction it will take. I believe it is time, after eight years of study, that the government decides. This committee's study and consideration of the issues should reinforce for the government that parliamentarians have an interest in seeing this matter resolved, and that they wish to know how government plans to manage and implement the necessary changes.

Madam Chair, this concludes my opening statement. With your permission, I would now like to ask Doug Timmins to present the overview of accrual-based budgeting and appropriations. As I said earlier, I hope this presentation will enhance members' understanding of the concepts, issues, and possible resolutions with respect to accrual budgeting and appropriations at the departmental level.

After the presentations, we will, of course, welcome any questions the committee members may have.

Thank you.

• (1120)

**The Chair:** Thank you.

Please, Mr. Timmins.

[*Translation*]

**Mr. Douglas Timmins (Assistant Auditor General, Office of the Auditor General of Canada):** Madam Chair, members of the Committee, good morning.

I'm very pleased to have an opportunity to make this presentation in order to help the Committee launch its study of accrual-based budgeting and appropriations.

Because this is a very complex subject, even for accountants, we will review it step by step. First of all, we will briefly explain the concept of accrual accounting; following that we will explain how it applies to budgeting and talk about the issues related to both budgets and appropriations.

Let's review the agenda first. Our presentation will address the following topics: accrual accounting, the basics; accrual budgeting and appropriations; why moving forward with this issue is important; some challenges and concerns; what is happening internationally; what is happening domestically; possible Committee questions for government; and the conclusion.

[*English*]

On page 3 of the presentation, we go through the basics. We thought we would begin with the basic concepts of accrual accounting. I know the objective today is to talk about accrual appropriations and budgets, but I'll just go through the basics of the accrual accounting difference. I'll come back to explain it as we move through the other issues.

Accounting on an accrual basis is recommended by CICA and by international standards. It's generally used in most environments in government these days, or it's certainly moving in that direction.

Accrual accounting recognizes income when earned and expenses when incurred, whereas on the old basis, the cash or the equivalent is received or paid. Accrual accounting does not wait until the cash changes hands to record the transaction. It keeps track of assets and liabilities from the initial recording until they're finally settled, paid, or used in terms of assets. So it's the costs of consuming them over time, particularly in terms of assets.

Turning to page 4, I'll go through a simple example. If an organization purchases and receives supplies for \$1,000 in the month of March, it pays for the supplies only in April. Under the accrual method, the \$1,000 of supplies would be recorded as soon as the expense was incurred, in this case March. Under the cash method, it would be when it was paid, in April.

I'll go through another example that is slightly more complex. The government purchases equipment costing \$100,000 on April 1, 2004. It's expecting to use that equipment for ten years. Under the accrual method, you would record the \$100,000 cost of the asset in

the year ending March 31, 2005. Then you would record amortization of \$10,000 for each year it is used over the ten years.

Under the former method, the entire \$100,000 would have been recorded in the year in which it was purchased, the year of expenditure. There is no recognition of the usage of the asset over time. The accrual method continues to track the outstanding balance of the asset until it's sold or removed from service.

• (1125)

Continuing that example on slide 6, the accounting would look as it is shown here. You have the impact on operations in the first year, 2005. Under the accrual basis it would be \$10,000, and in 2006 it would be \$10,000. That's the amortization that would be reflected in each of those years. Under the former basis, the second line, the impact on operations, you would have the whole \$100,000 being recorded in 2005 and nothing in the future years.

Below that we reflect the impact on the balance sheet. In this case, for the current under the accrual basis you would continue to carry the depreciated value of that asset, so at the end of the first year you would have the \$100,000 less the \$10,000 of amortization, for \$90,000. The second year you would have another \$10,000 of amortization, which would reduce that balance to \$80,000. That would continue through. Under the former method you would have nothing recorded; it would be nil, because the former basis recorded the full purchase of \$100,000 when it was originally done.

I have one more example on slide 7. This one I will come back to and explain later in terms of accrual appropriations and budgeting. In this example, on March 31 the government recognizes that it has an environmental cost for remediation of a toxic site, and it's estimated to cost \$100,000 over the next 10 years, but the work will begin on July 31, 2005, and the cost in that year will be \$10,000.

Under the accrual method the government would record the entire \$100,000 cost on March 31, 2005. It would recognize the full liability at that time. Under the former method only \$10,000 would have been recognized because that's the amount that was paid. The accrual method continues to track this liability until the outstanding balance owing has been fully paid. The initial \$10,000 would be reduced against the \$100,000, similar to the example I explained on capital assets.

Turning to slide 8, we again see the accounting of the effect of this transaction. Under the current accrual basis, \$100,000 would be recorded against operations in 2005. This is the incurring of the liability, because the full obligation is the \$100,000 known at that time. The former basis would show nothing in 2005 and would only recognize the payment of \$10,000 in 2006. The impact on the balance sheet is somewhat similar to the capital asset example. Under the accrual basis we would record \$100,000 the first year, \$90,000 the second year because \$10,000 has been paid or reduced against it. Under the former basis, the balance sheet would reflect nothing because it was on a cash basis and would only record the \$10,000 as paid.

I've now discussed three examples of accrual accounting. The important part of this is the timing of the recognition of the expense that occurs when the event happens, even if the payment is many years apart from that. The difference is most significant or visible when you have long-term liabilities or long-term assets. For anything that tends to be relatively short-term or immediate, there is not much impact. Things like buildings or equipment, pension liabilities, and environmental liabilities are where the big differences occur. Under accrual accounting, the recognized liability and the assets remain on the statements, and they are reduced through usage or payment over time.

- (1130)

Turning to slide 9, I'll explain a few basic advantages that accrual accounting provides. It provides a reflection of the full scope and size of government, so you have all the resources, all the financial and non-financial assets, recognized. The obligations, or all liabilities, are recognized and the costs are reflected. The focus is on the consumption of resources. It links the full cost of running a particular program with the results achieved, and it retains information, particularly on assets, until things are fully used in operations.

Slide 10 continues the explanation of some of the advantages.

*[Translation]*

Accrual accounting allows Parliament and the public to hold government accountable for stewardship of its assets, the full costs of its programs, and its ability to pay down the national debt.

As a result, it better reflects the impacts of all the decisions made by a government, rather than being limited to showing only those decisions made to pay for loans, assets, acquisitions and services.

*[English]*

Fuller information is available to government under this method. There's more focus on assets. There's more attention to managing liabilities and more focus on the full cost of programs and services.

Slide 12 is a snapshot of the different methods we currently have, which ones are using accrual and which ones are using near-cash. You will see later on that a similar summary of this is provided in the Comptroller General's presentation.

What I would point out here is that the federal budget at the government-wide level is on accrual, the summary financial statements are on accrual, and the departmental financial statements

are on accrual. Those departmental financial statements presently are unaudited, but there is a plan to move towards auditing them.

The key that I'm going to be talking about in the rest of the presentation is what is on this slide: the second line under budgeting, departmental budgeting and estimates; and the third line, appropriations. Those are, as you will see in the departmental column, near-cash. We are suggesting that it would be appropriate particularly to move departmental budgeting and estimates to an accrual basis to make them consistent with the reporting that you have at the departmental financial statement level and to be consistent with the federal budget level, which is accrual.

Accrual exists, as I say, but where it is lacking the most is in departments. There certainly has been an increase in the use of accrual. Cabinet submissions are now using accrual, but it's not routine for departmental management to focus accrual information. They continue to be accountable for the budgets and the appropriations, which are on a near-cash basis.

Later on, I'll speak to that a bit more.

Slide 13 deals with, if budgeting and appropriations were accrual, what would be the impact of that.

Well, the budgets, estimates, and appropriations would more closely be related to costs and revenues anticipated, regardless of when items are paid or received; budgeting and forecasting would be based on anticipated economic events, revenues, and costs in the fiscal year, not anticipated receipts or payments; and departmental managers would be more accountable for accrual financial information. This, we think, is important. They need to be thinking about more than just the near-cash information when they're making decisions. To us, this is a key change, which I'll speak to again a little later.

There are certainly some issues that have to be dealt with, the issues related to capital assets and long-term obligations, particularly for appropriations, and I think we'll hear some of that suggested by the Comptroller General when he speaks later.

It is important, in my view, that we think about potentially separating the issues of budgeting and appropriations. Certainly it's easier to move forward on the issue of budgeting. There are some issues perhaps with appropriations that you will pursue as you discuss this further.

I'll go now to slide 14.

•(1135)

[*Translation*]

Some of the advantages of using accrual accounting for budgeting include: more comparable information, better control and monitoring of actual performance; improved transparency of the government's performance; improved accountability at department and agency levels — the use of financial resources on the same basis as the budget; better information for planning; controlling operating and capital spending, and decision-making; and more focus on long-term consequences of current decisions.

[*English*]

There are some challenges and concerns.

Retraining of financial managers is certainly an issue that's been raised. The concept is difficult to understand. I hope we are helping people understand it a bit today.

It's still important for government to manage cash, and yes, we acknowledge that's true. There's the difficulty of managing the large non-cash expenditures or the accrued liabilities that will be paid at some time in the future. There's also a learning curve and a change management issue that I think is a bit connected to the issue of retraining.

We believe that leadership will be critical to making this happen, and managing the long-term non-cash items is certainly a challenge, particularly for appropriations. But as I'll explain in a few minutes, others have found a way to address it and we think Canada can do it as well.

I think it's important to note, and I've said this a couple of times already, that departmental managers need to be more accountable on managing non-financial assets and certain liabilities.

I'm going back to the example that I talked about earlier on the environmental remediation costs. The current method of departmental budgeting and appropriations—and this is important; this is departmental budgeting and appropriations, not the accrual accounting in the financial statements—would recognize in 2006 only the amount that was paid towards the cleanup. Even though the entire \$100,000 cost would be reflected in the government's summary financial statements, at the level of departmental budgeting and in the appropriation, it's not there. The inconsistency of that information is something that we think needs to be addressed.

The current budgeting does not require departmental managers to think about the full cost of the remediation. They only need to think about the short-term costs. The key challenge for us is to see that departmental managers focus on accrual costs, concentrate on the broader perspective of the cost of programs, and leave the conversion of the accrual information back to cash, which is still important to manage, to the financial managers in the organizations.

In my view, it is exactly the reverse of where we are today. Currently, the financial information is done in the financial shop at the end of the year to produce the accrual departmental financial statements and the accrual financial statements of the Government of Canada, but the management in the organization is managing only the cash appropriation.

We're saying that should be changed around. Make the information that is presented in the budgets and the estimates on an accrual basis. Managers will manage that information and then do the reconciliation to the cash number that needs to be appropriated. Let the financial managers, not the operational managers, worry about whether there's sufficient cash. That's a key point in this.

I'll quickly reflect on a couple of further points on what's happening internationally.

Most of the OECD countries have or are moving to accrual accounting. France has decided to move to accrual accounting but to retain cash-based budgeting. Accrual-based budgeting and appropriations are used in Australia, New Zealand, and the United Kingdom. These ones are the leaders and they've been advancing the matter. I know there are some views as to whether they are fully satisfied, but to our knowledge, they are continuing to move in that direction.

It's moving even faster domestically. Most of the provinces and territories have accrual-based government-wide budgets, and many of them have departmental budgets and appropriations that are on an accrual basis. We think the committee may wish to discuss with representatives of some of these provinces how they've addressed the issues and challenges. We can certainly recommend a few that would be ready and willing to discuss their approach with the committee.

•(1140)

Within Canada, our view is that the federal government is clearly behind. We think they should move forward on this issue.

[*Translation*]

Finally, we believe the Committee could play a very significant role by putting a number of questions to the government.

For example, who in government is the champion advancing this issue? Has that person received enough support?

[*English*]

What does the government propose as a strategy for moving toward accrual-based budgeting and appropriations, including addressing the unique issues associated with capital acquisitions and long-term liabilities?

[*Translation*]

Does the government have enough human resources and skills to make such a change? If not, how can it overcome this limitation?

[*English*]

Has government set aside enough funds to undertake a change in the budgeting and appropriation process?

In conclusion, it is our view that the concerns do not need to impede the progress. The committee support, we think, will help persuade the government to move forward in this area.

I thank you for your interest in this subject. *Merci*.

• (1145)

**The Chair:** Thank you.

I'm going to ask whether the committee would like to have one round of questioning before we go on to the members from the Comptroller General's office?

**Mr. Mike Wallace (Burlington, CPC):** I have questions.

**The Chair:** Then why don't we go directly to that? We'll start with Mr. Bains.

**Hon. Navdeep Bains (Mississauga—Brampton South, Lib.):** Thank you very much, Madam Chair. I have a couple of questions.

First of all, thank you very much for the presentation. I have a bit of an accounting background, so it helps remind me of some of the courses I took when I was in university. Wow, it sent shivers down my spine.

**Some hon. members:** Oh, oh!

**Hon. Navdeep Bains:** It's exciting stuff, I tell you. That's why I went into politics, by the way. I got my CMA and I realized accounting wasn't my calling.

I do appreciate the presentation because it does allow us to understand the basics of accrual accounting. Slide 12 here illustrates that it's not simply accrual accounting we're looking at. The current process is more of a hybrid in terms of cash-basis accounting versus accrual.

I ask you, is that disconnect a problem? Is it better to have two cash bases, for example, when we're talking about budgeting versus reporting? When it comes to reporting we have an accrual basis, but when it comes to budgeting we have a cash basis. Can a conflict possibly arise from that? For example, when a decision is made, when you look at it on a cash basis it might make sense, but on an accrual basis it might not make sense. Is that conflict something you see often, or does nothing like that exist?

**Ms. Sheila Fraser:** I think the conflict Mr. Bains has noted is exactly the point we're trying to raise here. On the summary financial statements, or the financials of the whole of government, and for the summary budget, the government moved to an accrual basis, which we believe is a preferable method of accounting and which I think most countries...the OECD countries mentioned are moving there. So the accrual method of accounting is far preferable to cash.

The difficulty is that it hasn't moved down into the departments, so the departments are still basically using cash. It does create problems, and I would go back to the chapter we did on rental properties and buildings within government where the department was not picking the most cost-effective option, which in many cases was to purchase, because the cash was not available in the budget that year. Because they're working on a cash basis, they would then go for these long-term leases. I really think if we moved to an accrual basis, they would only be including in their results, if you will, a portion of the cost, or the life of the building would reflect the total

costs of the building, and I really think the decisions would be different in that case.

**Hon. Navdeep Bains:** This hybrid model that we have, where we have one reporting mechanism and one budgeting way of accounting for it—cash basis versus accrual—does that cause more problems in terms of decision-making? Is it simply better to be either accrual or cash?

**Ms. Sheila Fraser:** We would say that it should be a consistent method of accounting throughout.

**Hon. Navdeep Bains:** The reason I ask is that we've gone to reporting in accrual, but because the decisions are made on a cash basis, I think that might cause more problems. What I'm getting at is that we should have stuck with cash and then made one giant leap toward accrual, as opposed to going step by step. Is that something you agree with or disagree with?

**Ms. Sheila Fraser:** The government made the decision to only go there for reporting a number of years ago. I think at the time they had to be congratulated, because Canada was a world leader in doing that and has certainly had some of the best financial reporting of countries around the world. I think it probably had to go step by step because these are very large changes and do involve a significant change within financial management in government. The difficulty, though, is that many financial managers are saying it's effectively like keeping two sets of books.

**Hon. Navdeep Bains:** Exactly. It's causing more work.

**Ms. Sheila Fraser:** They work on cash all year long, and then there's all this effort at year-end to transform it to accrual. So people are never really using the accrual concepts so they're not managing the liabilities, they're not managing the assets, they're not thinking about those things because it only comes in at year-end.

**Hon. Navdeep Bains:** Correct, and it's not even a value-added because it's basically a bookkeeping exercise to reconcile the difference between the two.

Also, you talked about the transition from cash to accrual and you mentioned possible committee questions for government in terms of the resources that would be entailed in this and the cost. Have you in any shape or form costed out what it might be in terms of taking it from the current cash basis in the departments to accrual?

**Ms. Sheila Fraser:** No, we have not.

**Hon. Navdeep Bains:** Do we have any range or idea of the cost entailed in this?

• (1150)

**Ms. Sheila Fraser:** The Comptroller General might have an indication of that.

**Hon. Navdeep Bains:** Do you have any ballpark figure as to the range of cost entailed in transforming the departments from a cash basis to an accrual one?

**Mr. Charles-Antoine St-Jean (Comptroller General of Canada, Office of the Comptroller General, Treasury Board of Canada Secretariat):** Madam Chair, the very high-level estimate could be in the \$150 million range. There are many assumptions that go into it. It's not a \$5 million or \$10 million exercise, so it's not insignificant. But we're managing a \$200 billion organization, so you have to put things into context.

**Hon. Navdeep Bains:** Aside from the cost of it in terms of the training, the culture, the work culture, how would that factor into the timeline as well? Say for instance the resource was there, the money was there, and the wealth seems to be here as well. All committee members seem to agree that the change needs to take place, or there seems to be consensus at least. What would be the timeline associated with a change like this? What would you give in terms of a timeline to bring about this change, aside from the financial resources, which are the other components of it?

**Mr. Charles-Antoine St-Jean:** We're going to be looking later on to see the study. The study gave us some kind of timeline of five years to do it on a progressive basis. So in five years everybody could be on an accrual basis from both a reporting basis and also an appropriation basis. The question is also cultural change. It's going to take some time to do it, to advocate people, to get people to learn this. When I was talking to my colleagues in New Zealand about when they moved to it, they told me it took them about ten years. But we've obviously done all the reporting ourselves here, so now we just have to do the last leg, which is the budget and the appropriation.

So it's going to take us some time. It's not something you do overnight.

**Hon. Navdeep Bains:** I'm not sure if you'll be able to answer this question. My intentions are completely straightforward here.

You've indicated that certain provinces have gone to accrual accounting, and there's been this discussion with respect to fiscal imbalance in terms of moneys being transferred from provinces to the federal government and back to the provinces. According to your understanding of what they've determined is the fiscal imbalance that exists, do they use accrual-based accounting to determine the number, or a cash basis? Could you answer that question, because this raises a good point when you're talking about reporting. This argument or discussion takes place in the public format, but to the average person, first of all, they don't even understand the accrual basis of accounting.

In terms of this gap that is talked about, how is this gap determined by the federal or provincial government in terms of the discussion? I'm not sure if you can answer it.

**Ms. Sheila Fraser:** I really can't answer it, Mr. Chair. I know that most of the provinces and the territories prepare their financial statements on accrual or some modification of accrual. I'm not sure that those are the numbers, though, that they use in this calculation of fiscal imbalance. I think it's more economic studies, in fact, and various other studies. So I'm not sure this has an influence on that.

**Hon. Navdeep Bains:** It is just a side question, because we were taking about accrual. It just came to my mind.

**The Chair:** Thank you very much.

Before we go to the next speaker, there's an internal study you've been working on for some time. Has that been made public yet?

**Mr. Charles-Antoine St-Jean:** We're going to be referring to this study, which was done by an external consultant, in the presentation.

**The Chair:** Yes, but we haven't seen a copy of that.

**Mr. Charles-Antoine St-Jean:** We'll be referring to it; it's in some of the information from the auditor.

**The Chair:** Madame Thibault.

[*Translation*]

**Ms. Louise Thibault (Rimouski-Neigette—Témiscouata—Les Basques, BQ):** I have no questions. Like this gentleman, I'm having a devil of a time understanding what this is all about. However, that does not mean I won't have some in a few days. Thank you.

[*English*]

**The Chair:** Mr. Nadeau has a question.

[*Translation*]

**Mr. Richard Nadeau (Gatineau, BQ):** I'm trying to assimilate some of this information in order to better understand the documents you've provided us and that I studied carefully. I have a couple of questions.

Let's take the example of the purchase of a building for \$100,000, an amount that is not included in the budget, that does not appear under voted spending, and let's assume that the payments are spread over a ten-year period, on the basis of \$10,000 annually. How exactly could the government purchase the building if it doesn't have the \$100,000? I don't know if you see what I'm driving at here.

**Ms. Sheila Fraser:** Madam Chair, that is one of the challenges as regards parliamentary votes. Parliament must always approve the use of public funds.

One solution might be to have a \$100,000 budget identified as capital, but on the results side, the departmental budget would only show \$10,000 a year. It's important to find combinations that accurately reflect the cash amount, which is still significant. Of course, the cash position has to be monitored, but as regards operations, that must be done on the same basis as the summary financial statements at year-end. So, there could be a combination of the two.

• (1155)

**Mr. Richard Nadeau:** Fine. Thank you.

In the documents, the suggestion is to use accrual accounting. The government has already said that it would implement this within a certain timeframe.

Having said that, if I understood you correctly, a number of countries and provinces are already using this method. Consequently, they must already have answers to the question I've just asked you. I assume it's similar to what you have presented.



My question deals more with the historical aspect of this. You may not be the one to answer it, but it is really a general question.

For how many years has the government been saying it wants to implement accrual accounting?

**Ms. Sheila Fraser:** Accrual accounting has been in place for four years. Indeed, the Public Accounts should be tabled Thursday, and that will mark the fourth year the government is reporting its results on the basis of accrual accounting.

**Mr. Richard Nadeau:** Full accrual accounting? Not using a hybrid system?

**Ms. Sheila Fraser:** No.

**Mr. Richard Nadeau:** They are already doing that.

**Ms. Sheila Fraser:** Yes.

**Mr. Richard Nadeau:** I see. That's good news.

Mr. St-Jean, you said that in some countries — you referred to New Zealand — it took about 10 years to change the culture or, at least, the system.

Is that what we're looking at here in Canada? Are we on the right track?

**Mr. Charles-Antoine St-Jean:** At this stage, since we have already completed that part of the financial reporting that represents 50% of the work, we are already well advanced. Will it take 10 years? No. We are thinking it may be more like five years, but that is what it will take.

**Ms. Sheila Fraser:** I would just like to add that the government has not announced publicly — unless Mr. St-Jean is doing that today — that it intends to move to the next step. The government has always said that the financial statements would be prepared using accrual accounting, but it has never actually made an announcement or a formal commitment along those lines.

That's why we are saying that after so many years of study, a decision is needed.

**Mr. Richard Nadeau:** Fine. Thank you.

Thank you, Madam Chair.

**The Chair:** Thank you.

Mr. Kramp.

[English]

**Mr. Daryl Kramp (Prince Edward—Hastings, CPC):** I have two or three overview points, but first I would like to commend our research department for helping us be prepared for this by spending their summer compiling a tonne of information for us to peruse and supposedly know a little more than we did going in.

It's going to be a challenging process, but I and many committee members believe that we have to get to a point where decisions are made. You have echoed the concern that it's been eight years with still no decision. I really believe we have to get to a point where we have a decision, regardless of what that decision is. There has to be some kind of consistency in operation. So I'm hopeful that the information will come from witnesses like you and others who will be called to at least lead us in a definitive direction. That's just a bit of an overview statement.

I don't know if you're allowed to say, but obviously all of your recommendations have not been accepted by the government. I can recall sitting on the public accounts committee as well, where recommendations were made and the government didn't take them, or it accepted them in part. Have you had any direct communication where reasons were given for rejection, or reasons were given to your departments as to why it would not be preferable to go along this line? Have you even had communication with the different levels of government, the agencies and/or the departments, expressing any reservations about the accrual process?

**Ms. Sheila Fraser:** I would say that the major discussions have been held with the Treasury Board Secretariat and the Comptroller General's office over the years. I don't know that we've ever had any explicit reasons as to why. The difficulty comes back to the fact that there is no decision. Government has consistently said over years that it is a complex question, and we're studying it and looking at it.

We're saying that now the time is to make a decision either to move ahead—and obviously there will be many issues that will have to be addressed, it will take time, and this will not be a simple matter that can be brought in overnight—or we say no, and then there has to be some way within departments that they manage more than cash. I think there has to be a decision.

There has never actually been a rejection of the recommendation. It's more a question of studying it.

• (1200)

**Mr. Daryl Kramp:** Then perhaps I could take that same question and ask Mr. Charles-Antoine St-Jean this. In your mind and in the minds of your predecessors, why have they not gone ahead? Why have they not either adopted or enacted, and what reasons have they given? Are there written responses, or is it just sitting in no man's land and blissfully being ignored?

**Mr. Charles-Antoine St-Jean:** I don't think it has been blissfully ignored. As the Auditor General has said, this is a complex issue. It's been under study for eight years, and so on.

There are different players around the table. If we prepare financial information for a certain purpose on a certain basis, it also must meet the needs of the users. If we go to the estimates on the accrual basis, it also means that Parliament will be focusing its attention on the use of resources and not only the use of cash. So far, to a large extent, the signal has been on the cash, or near-cash, or near-accrual. I do support the view that we are custodians of all the resources of the Government of Canada: cash, liabilities, the long-term and short-term assets—not only cash. It also means that members of Parliament have to focus their attention on the full use of the assets and liabilities of the Government of Canada.

**Mr. Daryl Kramp:** You're saying then that obviously the accounting process is or should be an exact science. However, it has been influenced in either the decision or non-decision by political influence, for various reasons. Are you saying that?

**Mr. Charles-Antoine St-Jean:** No, I'm not saying it has been political influence. It's that when the decision-makers—parliamentarians—look at the estimates, you are looking at them from a cash or near-cash perspective. In the future, if you want to go to resource management, you also have to look at the assets and liabilities, look at the balance sheet.

At the moment, you are looking more at just the statement of operations of the Government of Canada. You don't look at the balance sheet. When you approve the estimates, you don't approve a balance sheet, or you don't ask for a balance sheet or a forecast balance sheet.

**Mr. Daryl Kramp:** Right, so does the implementation of accrual remove some of the discretionary capacity of the departments and/or Parliament?

**Mr. Charles-Antoine St-Jean:** It would give better information to everybody.

**Mr. Daryl Kramp:** Thank you.

**The Chair:** I think Mr. Moloney wanted to add something.

**Mr. David Moloney (Senior Assistant Secretary, Expenditure Management Sector, Treasury Board of Canada Secretariat):** Thank you.

It's the Treasury Board Secretariat, working with the Comptroller General and the Office of the Comptroller General, that prepares the appropriations requests that the President of the Treasury Board tables in the supply bills that you actually vote on in Parliament.

I would like to speak to your question, if I could. There are three quick points I'd like to make in response to a couple of points. I think they're covered in the presentation that the Comptroller General will take us through, but I will just quickly review that.

The commitment in 1998 was that the government would move to accrual for budgeting and reporting. In fact, as the Auditor General stated, those were put in place four years ago—the government's reports and the government's annual budget.

Second, from the point of view of the most financially significant decisions, whether they are in respect of liabilities or assets, those that are large enough to require cabinet approval are in fact taken on an accrual basis. That took place four years ago, when the government switched its overall basis of accrual and reporting. For example, if a decision is made to purchase a building or any other sorts of assets that are large enough to require cabinet decisions, what we bring forward to Parliament in terms of our cash request for appropriations will reflect the one-time need that cabinet approved, but not the ongoing amortization that the accrual accounting would show.

That takes me to the third point. One of the members asked whether these other governments or other provinces in fact have sorted out how to deal with the need for Parliament—as the Comptroller General is saying—to see through to both the cost of delivering services and also the cash implications from year to year, because we cannot in fact leave it to financial managers inside the departments to check on whether there is enough cash.

That of course is important government-wide. Managers are accountable to manage to what you vote for them. But when we look

across provinces and across other national governments, there are a variety of ways that parliaments in fact vote, control, and oversee spending under accrual budgeting and reporting at the departmental level.

If we think about the simple example of the \$100,000 purchase, currently if a manager has \$100,000 cash available in his appropriations, he has authority to spend that money, and we don't see the year-by-year consequences. The example showed that on a 10-year life example, under accrual accounting, it would be appropriate to reflect a cost of \$10,000. Some parliaments vote the \$100,000, as you do, and the \$10,000 is not evident to you. Some parliaments vote the \$10,000 only. Some parliaments vote the \$100,000, and then automatically authorize a multi-year appropriation so that you will charge the \$10,000 year by year.

This has not historically been an approach that the Parliament of Canada and parliamentarians have been comfortable with, to encumber the fiscal framework automatically with the—

• (1205)

**Mr. Daryl Kramp:** Quite honestly, where you're going right now is just like ancient Egyptian hieroglyphics to me. You're losing me totally with your explanation. I understand what we started off with, but understand, you're speaking to laymen. We don't have an accounting designation.

I need something simpler in order to understand where you're going. I want it so simple as to say why it is advantageous to stay with the status quo and why we are not moving to the next process.

**The Chair:** Mr. Kramp, perhaps we'll address that shortly. You are already way over your time.

I'll go to Mrs. Nash, and then I'll ask the Comptroller General to make his presentation so that perhaps he can explain some of these things in a clearer fashion.

Madame Nash.

**Ms. Peggy Nash (Parkdale—High Park, NDP):** Thank you, Madam Chair.

You know what they say about a little bit of information, especially when it comes to accounting information.

First of all, I want to thank you for your presentations. I also appreciated getting the information from the Library of Parliament. It was very helpful for someone like me who does not have an accounting background. We want to keep it simple.

It was helpful for me to understand, from the background notes we got, how accrual accounting could help with respect to real estate purchases and to making better decisions for the long as opposed to the short term. I thought that was helpful; I think I'm getting the examples you've offered here.

One question that comes to mind around liabilities of the government concerns the issue of pensions in the public service. Can you explain to us what the difference would be between how the pension obligations of the federal government for the public service are accounted for today and how they might be accounted for under accrual accounting?

**Ms. Sheila Fraser:** I'll start by saying that the Government of Canada uses accrual accounting for its pension obligations, and for the major pension obligations has done so for the last four years. Whether for the public service, for veterans, and so on, those are all recorded on the books of Canada.

The main difference with cash is that currently under accrual accounting, as public servants work each year, there is a calculation done of the cost related to the pension they will ultimately receive. There is an actuarial evaluation done periodically—I'll try to make it simple—so there is a calculation of the cost. That is done, and that's the amount that's recorded as an expense in the operations.

The amount that's actually paid into a pension fund could be a completely different amount. In many cases, in fact, there is no amount paid into a pension fund, but there is a recording of the amount that will ultimately be payable to the employees. It's actually showing the liability, the amount the government will owe for future pension costs, and that is being recorded year after year, as people work and earn those pension benefits.

• (1210)

**Ms. Peggy Nash:** But that's being done now?

**Ms. Sheila Fraser:** It's being done now.

**Ms. Peggy Nash:** So there would be no change.

**Ms. Sheila Fraser:** There would be no change. It's important to note that at the summary level, as we say on page 12, summary financial statements are on an accrual basis and have been for the last four years. The federal budget as well is on an accrual basis. The issues we're really talking about are at the departmental level. They are essentially working on a cash basis; they are not managing.... For example, they wouldn't have the pension benefits in their day-to-day operations; they'd only be worried about the cash.

Doug, did you want to add some more?

**Mr. Douglas Timmins:** Yes, let me add that the pension liabilities for the future would be recognized in the consolidated financial statements of the Government of Canada, but at the departmental level all they would be budgeting for is the amount of cash that would be paid to meet that obligation in the next year.

**Ms. Sheila Fraser:** The easier one to understand, I think, is the case of environmental liabilities, Doug's example. In the summary financial statements, the government goes through and assesses all of the sites—it has done studies—and says, we think the costs of remediation or whatever will be *x* billions of dollars, and we've recorded that as a liability, an amount that will eventually have to be paid to clean this up.

At the departmental level, all they're concerned with is how much cash they have in the year to clean up a site. This is probably putting it in simplistic terms, but they don't have that number for the overall future liability. They're not managing the future liability; they're managing the cash in their department.

**Ms. Peggy Nash:** I'll ask just one last question on that, so that I understand. If for example the government decided to bring in, we'll say, under an NDP government, a national child care program, and the decision was taken that over a ten-year period this would be the amount of money that would be spent, the accounting of it would not change from the way it is accounted for now, because we're already

doing it on an accrual basis. But for departments, the accounting of spending on a yearly basis would change, and they would have to show more liability up front.

Does that...?

**Ms. Sheila Fraser:** This is going to get complicated. No, this is one of these expenses that, as Doug mentioned, we call current expenses. If there was a commitment for a child care program, the services would be done year after year and the amounts would probably be paid year after year. So the amount of consumption of resources is probably pretty much the same as cash.

It's not the same as if you said.... I'm trying to think of what it could be. The issues come into what we call long-term liability. For example, for people working over many years who have a pension benefit at the end, we say you should recognize their rights to that pension as they're working. So you record a bit of the expense each year.

For environmental sites, we recognize now that there's something that has to be cleaned up. So you say, okay, we have to clean it up. It may take us many years to actually do that. It's related to the event, whereas with providing child care—and most of the government operations, in fact—it is an event that would happen within the year. It wouldn't have longer-term implications.

• (1215)

**Ms. Peggy Nash:** Thank you for clarifying that.

**The Chair:** Thank you.

I think we'll go to Mr. St-Jean now so that we can have the other side of the presentation.

**Mr. Charles-Antoine St-Jean:** It's a very similar side.

**The Chair:** A very similar side, is it?

I often wonder whether we see a little bit of *Yes, Minister* going on here. I'm not sure.

[*Translation*]

**Mr. Charles-Antoine St-Jean:** Thank you, Madam Chair, for giving us this opportunity to present the views of the Comptroller General and the Treasury Board Secretariat regarding the use of accrual accounting within the federal government. We have a brief 18-page presentation.

[*English*]

For Mr. Wallace, the annex is just there if you want to know more about it. The presentation is only on the first 17 or 18 pages.

[*Translation*]

On page 3, under the heading “Background”, as my colleague mentioned, the 1996 budget stated that the federal government intended to move to full accrual accounting for budgeting and accounting purposes.

As pointed out by the Auditor General, since 2002-2003, the government's financial statements, the Public Accounts, and the budget are prepared on the basis of full accrual accounting, with an unqualified auditor's report.

[English]

New Zealand and Australia also have the same kind of statement as we do.

The estimates, appropriations, and most departmental plans and reports remain on a near-cash basis. General international acceptance of benefits or accrual-based financial reporting exists, but no consensus exists on the extent and use of accrual accounting for budgeting appropriations.

When we talk to our colleagues around the world, especially on the budget side, as my colleague has said, very few countries have gone to that extent. Australia, New Zealand, and the U.K. are three; others have chosen not to do so. The U.S., for example, has chosen not to do so, for various reasons.

Next we present a gradation of the different bases of accounting, ranging from cash to near-cash to accrual bases of accounting. I think this was explained by Mr. Timmins with regard to examples of those various bases, so I don't think there is any need to explain it further, perhaps with the exception of the accrual basis.

We talk very often about expenses, but we should also be talking about revenue. The Government of Canada does accounting for non-exchange revenue—income tax, corporate income tax, personal income tax—on an accrual basis. We also do most of our revenue, the non-tax revenue of about \$7 billion, on an accrual basis, but for some of them, for different reasons, we're still doing it on a cash basis. That makes it very complex when we try to reconcile the numbers.

The best example is our friends at the RCMP. At the end of the year, they collect the receivables from all the municipalities around the country. They make sure that each receivable is transferred in cash on March 31. So instead of having a receivable on March 31, they have to have cash....

Sorry?

• (1220)

**Mr. Mike Wallace:** It's paid?

**Mr. Charles-Antoine St-Jean:** It's paid. They have to have cash to recognize the revenue instead of having a receivable. Everybody else recognizes a receivable, but for them, they need to have the cash to recognize it. That makes it a bit more complex to explain to a layman, say, why some are on an accrual basis and some are on a cash basis.

That's one of the difficulties in moving to a consistent basis of accounting.

**Mr. Mike Wallace:** I'll come back to that in my questions.

**Mr. Charles-Antoine St-Jean:** Okay.

On the next page, you can see how the financial function works. There are different cycles in the financial function, ranging from budgeting and planning to financial management to financial reporting.

Budgeting and planning deals with the start of the year. This is where you make your plan. This is where the Minister of Finance prepares the budget. This is where the main estimates are also

prepared. This is also where the RPPs are prepared, the departmental plans.

During the year, financial management deals with the decision-making and the management of resources at that time. It's the management of not only cash but full management resources as well. So you manage your receivable, your liabilities, your fixed assets, your loans—all the non-financial assets, all the financial assets, and so on—and you do this management to save more in terms of internal management purposes.

After you complete the cycle for the year, you have to account for what you have done. This where you report on the financial reporting, and this is where we prepare the public accounts, which will be tabled later this year.

The financial reporting can be done for general purpose financial statements, such as public accounts, but it can also be done for specialized external reporting, as we do for Parliament on certain matters.

**The Chair:** Can you tell us how Revenue Canada reports? There are moneys owing to Revenue Canada, right?

**Mr. Charles-Antoine St-Jean:** Yes.

**The Chair:** I'm sure they report that on an accrual basis; they record the asset as the moneys owing. But when they're budgeting, how does that work? They don't do it on an accrual basis there, do they?

**Mr. Charles-Antoine St-Jean:** The revenue for the Government of Canada is done at the budgetary level. The Minister of Finance will be making his projection in terms of what is the budget and what will be the revenue base for the Government of Canada. That is done on an accrual basis.

**The Chair:** That's done on an accrual basis, but I talk about that because I know that Revenue Canada, on the other hand, when they do their budget...their year-end budget or whatever. All of a sudden, the bureaucrats will get an order that now they can't travel any more because their budget's all gone, or they're being cut by so much. You might as well turn around and say you're not going to collect this much money now, because you've cut the budget of the people who go and collect.

Is there some way of reconciling this so that you can have an actual impact from cutting the budget at Revenue Canada, meaning that you're going to lose this much more money, or...?

**Mr. Charles-Antoine St-Jean:** There are two different streams. On the revenue itself, the Minister of Finance will be making his projection, his budget, in terms of what amount will be raised. What you're talking about is the operating expenses of the department, and that's where the department, then, to manage its affairs, makes sure it has enough resources to make sure it collects the—

**The Chair:** But there is something strange that happens at Revenue Canada oftentimes. I have difficulty understanding how they make those decisions.

Madame Fraser.

**Ms. Sheila Fraser:** We actually just did an audit on the accounts receivable and management at the Canada Revenue Agency. The calculation of the receivables is a very extensive process at the end of the year, which takes several months. So they actually wait until assessments are issued in May, for example, for personal taxes, and then use that and do estimates.

Essentially, throughout the year, they manage the cash collections, and I think one of the points we made in the audit was that management over the receivables—which, if memory serves me correctly, were \$18 billion—needed to be significantly improved. So the focus in management is on cash collections, not on managing \$18 billion of receivables. That, I think, is one of the examples of how accrual and accrual budgetings need to come into the day-to-day operations.

**The Chair:** Anyway, that was just an aside. Continue.

**Mr. Charles-Antoine St-Jean:** Thank you for the precision.

On page 5 we talked about the three cycles, the three main importances of the financial function: budgeting, financial management, and financial reporting.

When we look at page 6, different information is used for different functions for different users. When we're talking about planning and budgeting, planning and budgeting is for before the action takes place and for proposed activities for a future period, expressed in financial terms. It's for internal and external users.

Financial management will include a wide variety of information required, with focus on providing the specific information required for specific situations—for example, decision-making, oversight, and control—and it's primarily for internal users.

Financial reporting is to provide information on the financial results and financial situation of an entity. General purpose financial statements and special purpose financial reporting take place. It's primarily for external users.

What is key here is that we have different information for different users, because they have different needs. External reporting would want to know what you've done globally, but then internal management would want to know what you have done specifically for certain programs or certain activities. It's okay to have different bases of accounting, depending on whether you're internal management or external management.

We've looked at page 7, and as Doug Timmins has made reference to, this is a comparison of how the basis of accounting works either at the aggregate level or at the departmental level. We see here that for some we have accrual, and some others are near-cash. The estimate is near-cash, the RPP is near-cash, capital planning is on an accrual basis, but the departmental level is done in near-cash. So even though a lot of progress has been made over the last eight or nine years since 1996, and since 2003 in particular, and a lot more accrual has been introduced in management, we still have different bases. This is where some confusion happens, when we have different bases of accounting for reporting or management.

Probably one of the most important slides I'd like to focus your attention on, as I mentioned before, is page 8. This is where the needs of Parliament need to be clearly addressed, but also,

Parliament needs to tell us what it wants us to focus on. Do you want us to focus on cash, or do you want us to focus on resources? I would say that resources, which includes cash, would be a good decision. But you need to expand the focus of parliamentarians, not just on cash but also on the appropriation of the full resources.

When you look at the financial systems, at the blue box, this is where you have most of the accrual information. The grey or the green slide is where you have the near-cash or near-accrual kind of data. Because you ask us to report to you on cash or near-cash for the appropriation, we do the accounting for both. We do the accounting for financial reporting, which is in blue, and we also do the accounting for appropriations, which is in green here. There are some differences between those two. So you see that volume I of the public accounts, which will be tabled very soon, is prepared on an accrual basis. Volume II is where we reconcile all the authorities.

• (1225)

[*Translation*]

All the authorizations and appropriations voted by Parliament are presented more on a near-cash basis. That is where we review the differences. That means doing a reconciliation. Last year, in the Public Accounts of the Government of Canada, note 5 or 6 in the financial statements referred to a \$32 or \$33 billion reconciliation between the Public Accounts and appropriations. This is a large amount to reconcile between financial statements prepared on essentially a near-cash basis and some prepared on the basis of accrual accounting. It is an important note to look at, because it indicates that the reconciliation can involve a large amount.

[*English*]

It's a big number between those two bases.

On page 9 is an overview to indicate what the current votes are, the annual cap on near-cash amounts for three types of expenditures. Normally there's the operating vote, the capital vote, and the grants and contributions vote, votes 1, 5 and 10, but it varies from department to department, meaning that you have limited information for financial and expenditure management on efficiency measures, reallocation decisions, departmental stewardship, and dysfunctional decision-making. As the Auditor General said, during the year the department will be managing on a cash basis, and at the end of the year they will have to reconcile every number on an accrual basis—instead of doing it throughout the year, managing this on an accrual basis, as everybody else does.

So the current financial management does allow for management on an aggregate fiscal framework, which is done on an accrual basis, but at the departmental level this is a bit more complex. That's the way Parliament has decided to exercise its control, more on the cash and not on the resources.

• (1230)

**The Chair:** Isn't that an old way of doing it? Because we've done it that way for many years is the only reason we're still doing it that way. Big businesses do it the opposite way. Sure, you have cashflows. You need to know how much cash you need to operate on a day-to-day basis, but you don't do it after the fact, you do it before. Then managers know they need this much cash and that's what you do.

**Mr. Charles-Antoine St-Jean:** Of course, but we also have to be fair. We have talked about New Zealand, Australia, and the U.K. It's not 180 countries around the world that do this. But we're far ahead of many countries. Those countries have shown us the way. Also, many provinces are doing so, so I think we have to change.

**The Chair:** We're going that way. We're going to be pushing you guys into that way.

**Mr. Charles-Antoine St-Jean:** Page 10. I would like to talk briefly about the consultant's study. The consultant study was conducted last year and was tabled with us on March 31. We've been looking at it to make sure we understand it. We have to have further discussion with the consultant but also internally to understand it and see where it leads.

This was a joint study between the Office of the Comptroller General and the expenditure management system group of the Treasury Board Secretariat. It's important that the two elements be joined in this study because this is where the two bases of reporting are placed.

**The Chair:** Does anybody know when or if you're going to make this study public? We're anxious to see what the results of this study are and the details that flow from it.

**Mr. Charles-Antoine St-Jean:** I would like to be able to tell you that today, Madam Chair. I will have to defer to the secretary to confirm that, but I can give you the salient points of the study.

If we look at the study itself, on page 11, we asked the consultants to compare the Canadian situation with a number of countries. We asked them to look at where some of the Westminster countries, Australia, New Zealand, and the U.K., are in that process. We also asked them to look at France and the U.S. and the Netherlands. It was not a random selection, but these countries are known to be the most advanced in terms of financial management and financial reporting.

The U.S. has no plan whatsoever to implement accrual accounting for budgetary appropriation. Reform there is focused on improved performance measurements and reporting, so the largest country in terms of resources has decided not to go that route.

The Netherlands has decided to go to accrual budgeting and reporting at the agency level, but the appropriation remains at the cash and commitment base, so there is a mixed bag with these countries.

Probably the three closest to pure accrual accounting for appropriation would be New Zealand, Australia, and the U.K.

When we look at page 12, the perspective of selected Canadian jurisdictions, the study looked at the experience of the moment in Alberta, B.C., and Ontario in particular, and we also looked at what's

happening in the other provinces—Saskatchewan, Manitoba, and Ontario. There is no doubt the provinces are ahead of the federal government in that field. B.C. and Alberta, in particular, have the strongest approach to accrual-basis appropriation.

When we look at page 13, the conclusions of the study, in terms of potential benefits, improved transparency is one that comes back all the time, from the perspective of having fewer reconciliations. If you manage on a basis and you report on that basis, you don't have to do that reconciliation at the end of the year because you manage it throughout the year on that basis, which improves transparency. Also, financial statements are better understood, because if everybody is working on the same basis, it makes life simpler for everybody to report on one basis and manage on one basis. There is improved accountability, better information with which to hold government to account. It's easier to compare financial results with plans. There is also improved management, better information on cost of programs, because you then have the full cost of programs.

Looking at the investments in capital assets, when you look at the overall scheme of things in the federal government, our expenses are about \$210 billion, we invest about \$4 billion to \$5 billion a year in capital investment, so that gives you better handling of that \$4 billion to \$5 billion.

There are also all the other non-financial assets and liabilities. I'm talking about loans, environmental liabilities, land claims. There is a better understanding of these.

What is important also, as my colleague has said, is the separation of cash management from program management. Cash should be managed as a treasury function. The role of the Department of Finance is to make sure the Government of Canada has the cash. We should not be multiplying that responsibility by 10,000 financial officers—

• (1235)

**The Chair:** But doesn't Treasury Board manage cash now?

**Mr. Charles-Antoine St-Jean:** Because appropriation is on a near-cash basis, they do manage cash, but the question is separating the cash from the operation, talking about that discussion about the fixed assets. You should take the right decision from an asset usage perspective, and then look at the financing. Go and see your treasurer to see how it can be done, either with cash, operating lease, capital lease, whatever. You need to make sure you've made the right decision.

At the end of the day it gives better management over a broader range of assets and liabilities. The biggest benefit of this is that it would reduce the level of confusion for all players when they look at the reporting of appropriation and financial reporting.

A key implementation issue is on page 14. Necessity is one...when you introduce that kind of change, it probably has to also be part of a larger change. We will be doing some cultural change in terms of the way we manage. My colleagues at the expenditure management system have been working hard on the MRRS policy and the program activity architecture.

**The Chair:** What's the MRRS? A lot of people don't understand; they're not used to that language.

**Mr. David Moloney:** It's the management reporting results structure policy.

**The Chair:** We don't always know your acronyms.

**Mr. Charles-Antoine St-Jean:** My apologies; it's a buzzword. I'm sorry—point well taken.

As part of that reporting strategy for Parliament, how do you want to see the activities reported back to you? I think that should be part of the same exercise.

As for the significance of changes, no doubt there will be some technical issues, and there are going to be some policy issues, procedures, and systems. We have a PAYE directive, but PAYE only deals with the end of the year—PAYE means “payable at year-end”. If we're going to manage this on an accrual basis, maybe we'll have, say, payables at the end of the day. We'll make sure we capture all the liability on an ongoing basis, not only once at the end of the year, or at least on a quarterly basis, to make sure you have the information. Legislative changes will be called for, probably in the FAA, to adopt the proper basis of accounting to reflect this.

As for cultural change, I had that discussion. It's a bit like when we adopted metric measure in Canada—we went from fahrenheit to Celsius, or from miles to kilometres. Some of us remember that transition. It took a few years, and still sometimes we lapse back to pounds of meat. So it's going to take some time; it's something our minds will take some time to adapt to.

**The Chair:** Would it be possible for us to just say we'll concentrate on fixed assets, for starters, or...? If you think it's going to be so difficult, push one thing....

**Mr. Charles-Antoine St-Jean:** It's a mindset. We manage resources.

**The Chair:** So it's the mindset that's the problem?

**Mr. Charles-Antoine St-Jean:** It's not a problem. That's the mindset we need to move to management resources, not only cash. So a loans portfolio is as important as a fixed asset. Cultural change is important, but it's not done overnight.

On the estimate of cost, when you talk to the consultant, it's a very high-level estimate. It could be \$150 million. It's going to depend on the system we need, because we still need to track cash. We also need to track the accrual basis and we need to compare the numbers. It's going to take a lot of training and retraining some of our financial officers who have been used to managing cash. It's a new process with new routines that will need to be done. It's going to take some time. So \$150 million is a high-level estimate.

On the timing, if we implement this approach, our recommendation is that we do it at the same time as we do the implementation of the other policies, on the results and structure and also the PAA to make sure we have changes at the same time, so it's comprehensive.

If you look at page 15, it gives you an idea in terms of the complexity and why it's so complex. If you do a little algebra, going back to your  $x$  and  $y$  axes, on the  $y$  axis you have six different approaches; on the  $x$  axis you have five different approaches. It's not something that has only one way. Different countries have used

different approaches. Australia, for example, went to the sixth, full-cost appropriation, and then they retrenched back to something closer to the fourth. They experimented with something that was not right. We have to be careful in picking and choosing to find the winning solution.

If I were making a guess in terms of what would be the sweet spot for the Government of Canada over the long term, I would say probably 5.4 would not be a bad place to land, but it's going to take a bit of time. It would be government-wide, and it would be the accrual appropriation and financial statements. That would be a good place to land.

But you can see we have from one to six. These are different models. I'm sorry, I'd like to make it simpler, but these are the different approaches that are available on the market at the moment. They are available for different countries, different provinces. You can have from government-wide only to government-wide and all departments. I'm sorry, but it's not easy.

Moving to page 16, the notional implementation plan, we asked our consultants if they could give us an idea in terms of how much it would take and what major steps would be involved. They recommended that it would probably take something like 60 months to go to the full solution. There would be intermediate checkpoints to make sure we're on the right track and that parliamentarians feel comfortable with the information being presented. Again, page 15 tells us it is complex, and page 16 tells us it's going to take some time, and a bit of patience will be required from parliamentarians to move along to the solution.

On page 17, the study's conclusion, although the increasing use of accrual accounting is a technical accounting change, it could have a significant impact on people, process, and systems. Therefore, if we're going to go there, how we go there is also very important. It's important that you have the right information throughout the transformation.

We also need to know where you want to go in terms of what information will satisfy you to hold the government to account. I think it's a two-way street. We can give you some information, but we'll also be depending on you to provide us with some guidance in terms of what would be useful to you.

On page 18, the last point, what we will be proposing is a made-in-Canada design framework. We have some specific issues that we deal with in Canada that the provinces don't deal with to the same extent. I'm talking about environmental liability. When I was looking at the public accounts, I saw that we have something like \$5 billion to \$6 billion of environmental liability. Provinces normally do not have large amounts of environmental liability. I think it would be important for Parliament to recognize the liability, but also parliamentarians have to tell us the pace at which they want this liability to be discharged. We have to reconcile those two pieces of information.

● (1240)

I think I will conclude on this note.

● (1245)

**The Chair:** Thank you.

We have time for a few more questions.

I'll go to Mr. Alhabra.

**Mr. Omar Alhabra (Mississauga—Erindale, Lib.):** Thank you, Madam Chair.

Thank you, everybody, for coming here again to help us navigate through what appears to be a very complex situation, although I'm sensing there's a consensus here that the accrual type of accounting is a good thing.

If you're allowing Mr. St-Jean to summarize or reduce the three difficult challenges in moving forward with this, those would be procedural challenges, cash management, and cultural change. Would that be it?

**Mr. Charles-Antoine St-Jean:** To a large extent, that would be it.

**Mr. Omar Alhabra:** Madam Fraser, regarding the private sector—and there are a lot of corporations and organizations that are quite large, some of them representing a few of the larger economies in the world—what type of accounting systems do they use or what type of reporting mechanisms do they use, from your experience?

**Ms. Sheila Fraser:** The private sector uses accrual accounting and has for decades. The difference, of course, with the private sector is that it doesn't have appropriations. So that's a major difference between it and the government and parliamentary sector.

The private sector will have budgets that will be on an accrual basis, but will also have things like cashflow statements, so they will be doing tracking. They will have several different tools available to them, which will give them a full base, so the cashflow, for example, is very important in the private sector.

**Mr. Omar Alhabra:** I was going to argue that they have, rather than appropriation in the same sense as we have it, a form of cashflow management and also appropriation of cash from their treasury or from their lenders.

**Ms. Sheila Fraser:** Absolutely. The treasury function is often one of the most critical functions in any large corporation.

**The Chair:** I think Mr. Moloney wanted to add something.

**Mr. David Moloney:** There is one extra element, a fourth domain, I believe, and that is the domain of Parliament's control. How would Parliament like to see, overlook, and control spending?

If members wouldn't mind, there's a slide on page 44 that I think summarizes the particular example of the chair when she was talking about tangible capital assets. As the member has said, there's a strong consensus that we would get better financial decisions in terms of managing resources if departmental managers were able to take the accrual approach. That will require Parliament to change the nature of its votes.

On slide 44 we are looking at tangible capital assets. There are many other aspects. I'm sorry, I tried before to run quickly through what's on page 44. It is complicated; however, there are at least four models, and in fact there are more that are summarized in later pages.

Today you vote acquisition costs; that's the current model. You could vote only amortization and not vote the capital acquisition. How would you like to see and be aware of the \$100,000 expenditure while you're voting the \$10,000 year by year?

The third there is to set-up, and we refer here loosely to statutory. Another definition could be a multi-year appropriation. So in year one, you would essentially vote as Parliament that the amortizations could be appropriated for the following ten years, essentially without parliamentary review. That would be a significant departure. But you could still vote one time on the acquisition vote.

Or you could do what some jurisdictions do: you could vote both every year. That's what I was referring to doing in the month of June. Certain parliaments have found that rather confusing: we just voted on this; you want \$100,000, and then you want \$10,000? How do we keep track of that? Doing so is not beyond our ability.

We in the secretariat very much welcome your hearings and the fact that you're willing to devote the time, because we're going to have to have your very explicit instructions and acceptance to change the very nature of a lot of these votes, and it will take us some time to do. But that fourth dimension is—

**Mr. Omar Alhabra:** I appreciate that. Thank you, Mr. Moloney.

But if I go through the presentation made by the Comptroller General, the benefits listed are improved transparency, improved accountability, and improved management. So while I understand there will be some challenges and perhaps some changes in the mechanism for voting, the reality is that accrual accounting—and I think there is a consensus here—will improve transparency, accountability, and management.

As I asked the last time we met, isn't there a cost every year-end when we have to reconcile how we manage our cash and then how we report on accrual accounting? That would be eliminated if we adopted accrual accounting.

• (1250)

**Mr. Charles-Antoine St-Jean:** There are not only costs at the end of the year; there are also surprises. That's one aspect. But it's not only at the end of year. Because we have two bases, it makes life complex throughout the year. One always asks what the impact of the year-end balance will be, but it's not only at the end of the year; it's throughout the year.

**Mr. Omar Alhabra:** So it's a huge cost and it brings surprises. Do you agree that those would be somewhat minimized if we adopted accrual accounting in our management?

**Mr. Charles-Antoine St-Jean:** When people have been culturally acclimatized to the new way of doing business...and it's going to take some time. Let's not discount that.

**Mr. Omar Alhabra:** On the surplus that was just announced, is it accrual or cash?

**Ms. Sheila Fraser:** It's accrual.

**Mr. Omar Alhabra:** Thank you.

[Translation]

**The Chair:** Do you have any questions, Ms. Thibault or Mr. Nadeau?

**Mr. Richard Nadeau:** You used the example of the metric system. When we adopted the metric system, the culture of inches and feet still existed. The fact remains that we did move to a different system, although it took a certain amount of time.



On page 7 of the document you prepared for us, I see identical or similar information to what appeared in the previous presentation.

Is it possible that in the near future, in terms of the criteria that appear on the left side of the table, accrual accounting will be used across the board — in other words, at both the aggregate and departmental levels?

**Mr. Charles-Antoine St-Jean:** Yes, eventually.

**Mr. Richard Nadeau:** Is that what we are moving towards?

**Mr. Charles-Antoine St-Jean:** As I mentioned in relation to this table, it shows that there has been significant movement since 1996, notably in 2003 and subsequently. We still have some way to go, but that is the direction we would like to move in — in other words, a single basis of accounting for both levels.

**Mr. Richard Nadeau:** So, a political decision will have to be made in order to complete this process?

**Mr. David Moloney:** Part of the decision is strictly within the purview of Parliament, since the nature of appropriations would be different. Of course, the government has to...

**Mr. Richard Nadeau:** Would it be possible to get something in writing that would assist us in preparing a motion, for example, or having legislation passed by the House of Commons that would say: "With the passage of this legislation, we are moving from the stone age to the age of enlightenment, with the implementation of accrual accounting?" That may be too much of a caricature, but is it possible, since it is used elsewhere?

**Mr. Charles-Antoine St-Jean:** The decision to adopt this method of accounting is a decision to be made by the government. There are advantages and disadvantages. My characterization of our current situation would not be that we're in the stone age — far from it.

**Mr. Richard Nadeau:** That is what is suggested by the Auditor General as the approach to take, but it is not moving forward at the speed of a development that... So, it's a purely political approach.

**Mr. Charles-Antoine St-Jean:** As my colleague already stated, it depends on what Members of Parliament want as a system to hold the government accountable. The first time I appeared before the Public Accounts Committee, I asked the Chair if we could introduce the idea of multi-year votes, which would make things easier for us. The Chair replied that here accounts are managed on a cash basis and that votes are also prepared on a cash basis. So, I'm trying to reconcile the two.

• (1255)

[English]

**Ms. Sheila Fraser:** With all due respect to the representatives from government, I find it a little disingenuous to be blaming parliamentarians for not going ahead with this. The public accounts committee has recommended at least four or five times that government adopt accrual-based budgeting and appropriations. Certainly one parliamentary committee has expressed it.

I find it a bit much to think that parliamentarians are going to sit around and think about how they're going to deal with appropriations for capital assets. Surely it's the responsibility of government to make the decision on whether to go ahead. Yes, involve parliamentarians, show them the options, and get them involved, but it is really up to government to make the decision on whether this is advisable or not.

[Translation]

**The Chair:** Mr. Nadeau, would it be possible for Mr. Wallace to have one minute of speaking time?

[English]

**Mr. Richard Nadeau:** Madam Chair, I have a whole page of questions. Can we invite them back?

**The Chair:** Yes.

**Mr. Richard Nadeau:** Thank you.

Even in the presentation it was shown that there aren't a lot of countries doing it at a national level. Some of them have backed off a bit. We have close to five accountants in front of us saying it's an accounting way—

Ms. Sheila Fraser: Is that good or bad?

Mr. Richard Nadeau: There aren't that many accountants elected, and I don't know why that would be.

I have a lot of questions and I don't think it's appropriate to try to do it—

**The Chair:** We'll have them back again if we can, although not this Thursday because we have to do estimates. We're going to meet with Madam Barrados next Tuesday, but we'll do it on the Thursday after that if we can.

**Mr. Mike Wallace:** I move to adjourn.

**The Chair:** I want to remind you that on Thursday we're going to vote and adopt the main estimates, so there will be no witnesses.

**Mr. Mike Wallace:** Will we get to discuss them?

**The Chair:** Yes, we will.

[Translation]

Would you like to say something?

**Mr. Charles-Antoine St-Jean:** I'm sorry, Madam Chair, but I have to co-chair an international committee meeting next Thursday.

**The Chair:** Well, we'll see what we can do. However, it is important that we continue this discussion.

[English]

We'll see you on Thursday. The meeting is adjourned.





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