When Sir Andrew Likierman first came across the UK government’s financial accounts in the early 1980s he was baffled by them. The highly complex system dated back to William Gladstone in 1866 and the figures were almost impenetrable. It was hard to tell what was spent and how expenditure was controlled for what was 40% of national income. The few insiders who worked with the figures thought this was the best way of doing things and were cautious about outsiders getting involved.

But Likierman hung in there and learned how the system worked, advising first the Treasury Select Committee then several other Parliamentary Select Committees, and writing reports on improving and simplifying the reporting of government spending. He even wrote a guide called Public Expenditure: Who Really Controls It and How, which was published by Penguin in 1987.

Things weren’t working

By the 1990s a few people in government were becoming increasingly aware of the limitations of long-established financial and accounting processes. The idea came about of moving the whole of the government from planning, reporting and controlling in cash alone to using accrual accounting – the way the rest of the economy operates. This means, for example, spreading the cost of using something that lasts more than a year – a computer, an aircraft-carrier – over its life, not just counting it as a cost in the year it’s bought. So in 1993 Likierman took on the challenge of doing just that when he moved from London Business School to the Treasury to become Head of the Government Accountancy Service, a post created only 12 years before and affectionately known as ‘HOTGAS’.

The UK wasn’t the first government to make this change. Likierman was following in the footsteps of New Zealand, which had changed to accruals after its 1984 financial crisis. But the UK economy is much larger and more complex and the process was to take nine years. The change aroused a lot of interest, and governments around the world came to see how the UK government was going about it. Today many countries follow some accrual accounting principles, although only a handful have gone as far as the UK.

The challenge

For such a big task, Likierman needed and got the backing of the then Chancellor Kenneth Clarke and, when the government changed in mid-project, his successor Gordon Brown. Crucially, he also got the backing of Treasury senior civil servants in charge of public spending, and in particular Andrew Turnbull, now Lord Turnbull, who went on to be Head of the Civil Service.

There was extensive consultation and careful preparation to ensure that established principles could be applied to central government. Certain issues were particularly difficult, for example, whether the rail network was part of the public sector.

There were huge practical problems. Finding out what was government owned was just one of them. The Ministry of Defence asset list turned out to have over two million entries, one of which was Salisbury Plain. Nor was there an established way to value complex assets, such as publicly-owned art.

Just as significant, central government has tens of billions of pounds of working capital in the form of inventory, debtors and creditors, and this is not identified under cash accounting. Likierman gives the example of the Ministry of Defence which often used any spare money left over at the end of the year to buy things “just in case”. So one aircraft had 25 years of spares.

Then there were contingent liabilities. Accrual accounting identifies the potential liabilities the government faces, for example, over clinical negligence claims or to decommission nuclear power stations.

Convincing people

There was also the challenge of training and re-training staff and not just those who were new to financial management. Until the change, the head of finance of a government department was rarely a professional accountant – it wasn’t seen as relevant to the job.

Likierman admits the first years were tough. Few understood why change was necessary or really believed it would happen. It was a fight to convince people even to join the process. Rather than justifying the change, his approach was to ask people to justify the contrary, asking: “Why wouldn’t you want to know what you own, the cost of what you do, have a better way of making decisions, make better use of scarce financial resources and manage finances professionally?”

The end of 1866

The policy recommendations were incorporated in legislation, which Likierman spent a year taking through parliament. He remembers the last stage vividly. “We almost ran out of Parliamentary time but got to the final vote in the House of Lords with a day to spare,” he says. “Then a number of government peers didn’t turn up. If we’d lost that vote, there was a chance the legislation wouldn’t have been reintroduced because a
In the end the government won by just six votes. “It was an emotional moment,” says Likierman. And to his huge relief the Government Resources and Accounts Act became law in 2001, superseding Gladstone’s 1866 legislation.

Positive results
As a result of the changes, government departments today are much more transparent in what they report and have better information for taking decisions. A National Asset Register lists what government owns, including its most costly asset, Trident nuclear submarines. There’s even Whole of Government Accounts, which include a single-page financial statement for the whole of UK government income and expenditure and another one for the balance sheet of what it owns and owes.

So is this just an excuse to employ more accountants? Likierman points out that compared to the savings and the effect of better-informed financial decisions, the cost is minute. And he adds that the savings on the Ministry of Defence’s working capital alone have paid for the whole project many times over.

Likierman left the position as Head of the Government Accountancy Service in 2004 to return to London Business School. And he looks back fondly on an extraordinary project: “It made a real difference and it was a privilege to be part of it.”

Sir Andrew Likierman first joined the School in 1974 and became Dean in 2009. He’s also Professor of Management Practice in Accounting.