

Australian government budget balance numbers The hybrid nature of public sector accrual accounting

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Abstract

Purpose – The purpose of this paper is to analyse the nature and comparability of budget balance (surplus/deficit) numbers headlined by the Australian Commonwealth Government and the governments of the six Australian States and the two Australian Territories. It does this in the context of the transition to Australian accounting standard AASB 1049 Whole of Government and General Government Sector Financial Reporting.

Design/methodology/approach – A case study research method is adopted, based on a content/ documentary analysis of the headline budget balance numbers in the general government sector budget statements of each of the nine governments for the eight financial years from 2004-2005 to 2011-2012.

Findings – Findings indicate some variation in the measurement bases adopted and a number of departures from the measurement bases prescribed in the reporting frameworks, including AASB 1049. Findings also reveal that none of the nine governments have headlined a full accrual based budget balance number since the implementation of AASB 1049 in 2008.

Research limitations/implications – While the study focuses on the Australian general government sector environment, it has significant implications in highlighting the ambiguity in the government budget balance numbers presented and the monitoring and information asymmetry problems that can arise. Research findings have wider relevance internationally in highlighting issues arising with the public sector adoption of accrual accounting.

Practical implications – The paper highlights the manner in which governments have been selective in the manner in which they present important budget aggregates. This has important practical and social implications, as the budget balance number is one of the most important measures used to evaluate a government's fiscal management and responsibility.

Originality/value – The paper represents the first detailed examination of aspects of the effect of the transition to AASB 1049.

Keywords AASB 1049, Budget balance numbers, General government sector, Government budget reporting, Surplus/deficit

Paper type Research paper

1. Introduction

The aim in this paper is to investigate the budget balance (surplus/deficit) numbers headlined by the nine Australian Commonwealth (Federal), State and Territory governments over the eight budget years from 2004-2005 to 2011-2012[1]. The research period spans the introduction of Australian Standard AASB 1049 Whole of Government and General Government Sector Financial Reporting (Australian Accounting Standards Board, 2009b). AASB 1049 was issued with the aim of harmonising the two major alternative frameworks for Australian government reporting; the Government Finance Statistics (GFS) uniform framework and GAAP (generally accepted accounting principles) as specified in Australian

Accounting Standards. Various writers recognised the problems and potential for confusion arising from the presence of the two alternative accounting and budget systems and the possibility for governments to select between, and modify, alternative bottom line numbers [2]. Accordingly, the aim of the present study is to examine the nature and comparability of budget balance numbers emphasised by the relevant governments in their budgets. Given that alternate measures for budget balance numbers are available under relevant standards and frameworks, the study seeks to address the following general research question:

RQ1. To what extent are the budget balance numbers headlined by the nine Australian Governments comparable and calculated in accordance with the relevant rules?

The paper addresses a gap in the literature by providing contemporary empirical evidence on the selection and presentation of budget (accounting) numbers in a public sector setting where an accrual-based accounting system has been implemented. Government budgets and budget transparency can be examined from an agency theory perspective (Hood, 2001; Benito and Bastida, 2009). Voters, taxpayers and the general public (the electorate) can be considered as principals for whom politicians and the government act as agents (Hood, 2001). Within this view, government budgets are central in fulfilling a monitoring function and in reducing information asymmetry between the principals and agents.

It has been recognised that there are gaps in our understanding of the implications of decisions to transform accounting, reporting and financial management processes from cash to an accrual footing (Carlin, 2005). This study addresses one aspect of that gap from an agency theory perspective.

The paper proceeds as follows. A theoretical background to government financial and budget reporting is provided in the following section, followed by a discussion of budget balance numbers and government financial reporting frameworks in Australia. The study's research questions and method are then outlined, followed by a presentation and discussion of research findings. A summary and conclusions section completes the paper.

2. Theoretical background to government financial and budget reporting

Government budgets have, historically, been 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). Government budget papers have been considered to be "the most authoritative, timely, widely distributed and reported statements of each government's financial results and plans" (Allan, 1993, p. 77). As evidenced by the considerable media coverage they generate, this continues to be the case today.

One theoretical approach that can be applied to the issue of budget transparency is that of principal-agent (agency) theory (Hood, 2001; Benito and Bastida, 2009). From an agency theory perspective, the "electorate" (voters, taxpayers and the general public) can be considered as the principals [3], for whom politicians and the government act as agents (Hood, 2001). In modern democracies, the distance between the electorate and the elected agents gives rise to the same kinds of principal-agent problems as are encountered in the private sector (Bergman and Lane, 1990). In fact, it has been argued that principal-agent problems in the public sector may be even more severe than those in the private sector. This is because, given the ambiguities of political life and uncertainty about the state of the

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Wines, Graeme and Scarborough, Helen 2015, Australian government budget balance numbers: the hybrid nature of public sector accrual accounting, *Accounting research journal*, vol. 28, no. 2, pp. 120-142.

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environment, the implicit political contract tends to be underspecified (March and Olsen, 1989; Bergman and Lane, 1990).

One of the major aims of agency theory is to “find the most satisfactory way of negotiating, specifying and monitoring contracts so as to minimise the likelihood of violations resulting from opportunism on the part of the agent” (Boston et al., 1996, p. 30). All contractual arrangements between the state and the governed contain important elements of agency (Ross, 1973, p. 134). While contracts are usually thought of as formal and explicit legally binding ones, they can also be implicit, obligational or relational contracts that are relatively open-ended and incomplete in form (Boston et al., 1996). Boston (1995, p. 11) refers to these contracts as being in the nature of “mutual undertakings”.

Budget reporting combines aspects of both formal and informal contracting with respect to the monitoring of government behaviour. Governments are required to comply with legislation and various general reporting guidelines in preparing budgets. However, the specific accounting requirements may not necessarily be tightly specified and, as will be illustrated in this paper, may allow considerable scope for flexibility and alternative presentations in government budget papers.

The management of many principal-agent relationships is complicated by incomplete information, asymmetrical information and various uncertainties (Boston et al., 1996). A particular difficulty is that information about an agent’s actions is not only imperfect but skewed in favour of the agent, yielding adverse selection and moral hazard problems that must somehow be managed (Moe, 1984). In the budget setting, an individual government has access to information that the electorate, as principal, does not. Given political processes, governments have an incentive to exploit this situation to their advantage, particularly given the difficulty of observing their behaviour. This is particularly the case for government budget surplus/deficit numbers. Terms such as creative accounting, accounting devices, fiscal illusion and fiscal gimmickry have been used when referring to strategies designed to influence reported government budget balance numbers, with these strategies aimed at putting the best possible gloss on the accounts (Easterley, 1999; Koen and van den Noord, 2005; Irwin, 2012). In terms of agency theory, such strategies have monitoring and asymmetrical information implications.

A central tenet of agency theory is that the design of an efficient incentive structure also requires the development of monitoring systems and mechanisms for inducing agents to reveal as much of their privately held information as possible (Moe, 1984). In the context of government accountability, the preparation and publication of clear and understandable budgets is central to this accountability and monitoring function. Higher levels of disclosure and transparency can lessen information asymmetry and the principal-agent problem (Benito and Bastida, 2009). But it must be recognised that budget rules are political rules that are made and enforced by political leaders (Schick, 2003; Benito and Bastida, 2009). Hence, as noted above, the accounting provisions related to the specific calculation of a government’s budget balance number may not be tightly specified and may allow for a considerable degree of latitude. This can affect the monitoring of politicians by the electorate.

3. Budget balance numbers and government financial reporting frameworks in Australia
Governments have implemented significant reforms within the Australian public sector over the past two to three decades (Guthrie, 1998; Carlin and Guthrie, 2003). These reforms, referred to generally under the heading New Public Management or NPM (Hood, 1991), aim

to drive more “efficient”, “effective” and “accountable” public services (Guthrie et al., 2003). The NPM reforms have incorporated accounting and management technologies drawing on private sector performance criteria and practices and market-based activities (Carlin and Guthrie, 2003; Lapsley, 2009; Lapsley et al., 2009; Wanna, 2010a, 2010b). From the early 1990s, a demand arose for performance to be reported in terms of accrual-, rather than cash-based, financial information (Guthrie, 1998). However, the presence of the two alternative GFS and GAAP accounting and budget systems in Australia caused problems and potential for confusion. At the direction of the Australian Financial Reporting Council (FRC, 2002), the Australian Accounting Standards Board (AASB), therefore, sought to harmonise the two frameworks, and accounting standard AASB 1049 (AASB, 2006, 2007, 2009b) was issued to fulfil this aim. These frameworks and developments, and the alternate bases for the calculation of government budget balance numbers, are discussed in the following sub-sections.

3.1 GFS framework

Adopted by the Australian Bureau of Statistics (ABS), the GFS framework is based on the international equivalent developed by the International Monetary Fund (IMF, 2001) and on the United Nations System of National Accounts (United Nations, 1993). The GFS framework provides for the recording of data on an accruals basis, but with supplementary data recorded on a cash basis (ABS, 2003, 2005)[4].

The statistical concepts underlying the GFS framework are designed to enable the preparation of uniform economic statistics for all IMF member countries (ABS, 2005, p. 5). The term “government finance statistics” refers to “statistics that measure the financial activities of government and reflect the impact of those activities on other sectors of the economy” (ABS, 2005, p. 1). While, in developing the GFS framework, the ABS worked closely with the accounting standard setting authorities, it was conceded that “differences between accounting and statistical concepts are inevitable because they serve different purposes” (ABS, 2005, p. 5).

An operating (income) statement prepared in accordance with the GFS framework presents details of revenue and expense transactions and the net acquisition of non-financial assets for an accounting period. Two major alternative budget balance (surplus/deficit) measures can be drawn from the statement. It must be emphasised, though, that the GFS operating statement is based on transactions only (ABS, 2005, para. 2.119). The first section of the operating statement comprises revenues less expenses arising from transactions, this resulting in the net operating balance. The revenues and expenses are calculated on an accruals basis, with depreciation included as an expense (ABS, 2005, para. 2.61). The GFS net operating balance represents the “change in net worth due to transactions” (ABS, 2005, para. 2.113). It is noteworthy that, being a transaction-based measure of performance, the GFS net operating balance does not represent a full accrual accounting measure of net income[5].

The second section of the GFS operating statement deducts the net acquisition of non-financial assets from the net operating balance. Depreciation expense is added back to avoid double counting, with this results in the net lending/borrowing balance. This balance is also referred to as the fiscal balance (Commonwealth Treasury, 2011b, pp. 1-5).

Also prepared pursuant to the GFS framework is a cash flow statement (ABS, 2005, para. 2.122). The GFS cash flow statement presents cash flows dissected between operating, investment and financing activities, with cash flows from investment activities further

dissected according to whether they are investments in non-financial assets, financial assets for policy purposes or financial assets for liquidity management purposes. The cash-based measure of the budget balance is calculated as the net cash flows from operating activities plus net cash flows from the acquisition and disposal of non-financial assets.

3.2 GAAP and Australian Accounting Standards pre-AASB 1049

In parallel with the GFS framework, the Australian accounting profession developed a number of public sector accounting standards. AAS 31 Financial Reporting by Governments, requiring the use of a full accrual basis of accounting, was the standard applicable to Australian government sector reporting (Public Sector Accounting Standards Board, 1998). Reflecting a full accrual accounting basis, the budget balance (operating surplus/ deficit, or operating result) calculated pursuant to AAS 31 exhibited important differences to the GFS transactions-based net operating balance. Major differences related to accounting for asset writedowns (treated as operating expenses under AAS 31 but negative equity revaluations pursuant to the GFS framework), other gains and losses on assets (not included as revenues or expenses under GFS), bad and doubtful debts (not recognised under the GFS framework) and the acquisition of defence weapons platforms (capitalised and depreciated under AAS 31 but expensed at the time of acquisition pursuant to the GFS framework)[6]. Material variation between the budgeted GFS net operating balance and the AAS 31 budget balance resulted from the above accounting policy differences. For example, the Commonwealth Government's 2004-2005 budgeted GFS net operating balance amounted to a surplus of \$1 496 million, while AAS 31 accounting treatments resulted in a budget deficit of \$355 million (Wines and Scarborough, 2006).

3.3 GFS/GAAP convergence and AASB 1049

In addition to Australia's adoption of international financial reporting standards from 1 January 2005 for private sector reporting entities, the Australian Financial Reporting Council (FRC) also adopted a parallel convergence strategy for public sector financial reporting (FRC, 2002). Exposure draft ED 142 Financial Reporting of General Government Sectors by Governments (AASB, 2005) was released in July 2005. This was subsequently issued as accounting standard AASB 1049 in September 2006 to apply to annual reporting periods beginning on or after 1 July 2008 (AASB, 2006). The standard was revised and reissued as AASB 1049 Whole of Government and General Government Sector Financial Reporting in September 2007 (AASB, 2007) and then again in August 2009 (AASB, 2009b). Financial statements prepared in accordance with AASB 1049 continue to present three budget balance numbers that are consistent with the GFS framework:

- (1) the net operating balance (that is, the net result from transactions);
- (2) the net lending/borrowing (fiscal) balance; and
- (3) the cash surplus/deficit[7].

Also calculated pursuant to AASB 1049 is a budget balance number that represents a final accrual accounting surplus/deficit measure that is equivalent to the net profit number produced by private sector entities in accordance with Australian Accounting Standards. This is referred to as the Operating Result. As noted earlier, the difference between the net operating balance and operating result is that the latter includes various non-transaction other economic flows, consistent with full accrual accounting principles. Examples of these other economic flows include impairment losses, fair value adjustments and other asset

writedowns, foreign exchange gains and losses, superannuation fund gains and losses and expenses recognised via accrual provisions.

To illustrate these calculations, Table I presents a summary of the alternative budget balance numbers taken from the 2011-2012 budgeted financial statements of the Australian Commonwealth Government and the Victorian and Queensland State Governments. The table indicates derivation of the following four major alternative budget balance numbers:

- (1) net operating balance (from transactions);
- (2) operating result;
- (3) net lending/borrowing (fiscal) balance; and
- (4) cash surplus/deficit.

As shown in Panel B of Table I, there is considerable variation in the four budget balance measures for each government.

Table 1. Summary of 2011-2012 general government sector budget balance numbers for the Australian Commonwealth, Victoria and Queensland.

	C/W \$ million	VIC \$ million	QLD \$ million
<i>Panel A: calculation of alternate budget balance numbers</i>			
<i>Accrual measures of surplus/deficit</i>			
Revenue	3,49,961	47,439	43,007
Less expenses (including depreciation)	(3,65,817)	(47,299)	(47,065)
Net operating balance (from transactions)	(15,857)	140	(4,058)
Other economic flows included in operating result	(1,667)	(76)	(97)
Operating result*	(17,524)	64	(4,155)
Net operating balance (as above)	(15,857)	140	(4,058)
<i>Less net acquisition of non-financial assets</i>			
Purchase of non-financial assets	10,561	4,119	7,180
less sales of non-financial assets	(1,361)	(302)	(226)
less depreciation	(5,636)	(2,345)	(2,872)
plus change in inventories	578	(13)	39
plus other movements in non-financial assets	263	1,250	213
Total net acquisition of non-financial assets	(4,405)	(2,709)	(4,334)
Net lending/borrowing (fiscal) balance	20,262	(2,569)	(8,392)
<i>Cash measure of surplus/deficit</i>			
Cash receipts from operating activities	3,41,029	47,522	45,668
Cash payments for operating activities	(3,51,474)	(45,040)	(46,629)
Net cash flows from operating activities	(10,445)	2,482	(961)
Cash flows from investments in non-financial assets	(9,242)	3,816	(6,954)
Cash surplus/(deficit)	(19,687)	(1,334)	(7,915)
<i>Panel B: summary of budget balance numbers</i>			
Net operating balance (from transactions)	(15,857)	140	(4,058)
Operating result*	(17,524)	64	(4,155)
Net lending/borrowing (fiscal) balance	(20,262)	(2,569)	(8,392)
Cash surplus/(deficit)	(19,687)	(1,334)	(7,915)
Note: *Operating result = full accrual-based surplus/deficit based on Australian Accounting Standards			

Examples of headline budget balance announcements in annual budgets for the 2011-2012 year of the nine Australian Governments are as follows:

- (1) [...] a forecast General Government Sector Headline Net Operating Deficit of \$36.9 million in 2011-2012 (Australian Capital Territory Department of Treasury, 2011, p.7).
- (2) [...] the deficit for 2011-2012 becomes \$22.6 billion (Commonwealth Treasury, 2011a, p.9).

- (3) A key fiscal strategy of the 2011-2012 Budget is to re-establish and maintain sustainable operating surpluses (Government of South Australia, 2011, p.4).
- (4) [...] I am proud to announce a \$442 million surplus in the 2011-2012 state budget (Government of Western Australia, 2011, p. 1).
- (5) An operating deficit of \$718 million is therefore expected in 2011-2012 (New South Wales Treasury, 2011, p. 5)
- (6) The resulting effect is an [...] estimated cash deficit of \$387 million for 2011-2012 (Northern Territory Treasury, 2011, p.4).
- (7) In 2011-2012, a General Government Net Operating Balance deficit of \$113.8 million and a Fiscal Balance deficit of \$358.5 million are budgeted (Parliament of Tasmania, 2011, p. 1.1).
- (8) [...] the operating balance [...] is forecast to be \$4.06 billion for 2011-2012 (Queensland Government, 2011, p. 3).
- (9) [...] average surpluses of \$164 million over the forward estimates (Victorian Department of Treasury and Finance, 2011, p.3).

How comparable are the above budget balance numbers? When it comes to budget reporting, and as the above quotes illustrate, a seemingly straightforward concept such as a government's deficit or surplus "hides a minefield of ambiguities, questions of usage, and conflicting definitional issues" (Blejer and Cheasty, 1991, p. 1675). Any meaningful understanding of, and comparison between, the above budget announcements requires knowledge of the specific bases used to derive the budget balance numbers.

The study's general research question was stated earlier as:

RQ1. To what extent are the budget balance numbers headlined by the nine Australian Governments comparable and calculated in accordance with the relevant rules?

Four specific research questions are developed in the balance of this section to investigate this general research question.

In the presence of the GFS and GAAP frameworks, Wines and Scarborough (2006) documented an inconsistency in headline budget balance numbers in Australian Commonwealth, State and Territory Government budgets across the 2004-2005 and 2005-2006 financial years. As AASB 1049 was introduced after that time to harmonise the two frameworks, the introduction of a single standard would be expected to reduce the variation in headline budget balance numbers across the study's research period (that is, pre- and post-introduction of AASB 1,049). The study's first specific research question is therefore stated as:

RQ2. Has the variation in the basis for headline budget balance numbers across the nine Australian Governments reduced over the study's research period?

The study's RQ2 is based on the view that variation in headline budget balance numbers should have decline over the study's research period. In addition, it might be expected that, with the existence of a single AASB accounting standard, a single basis for the headline

budget balance number over the nine Australian Governments would have emerged by the final year of the study's research period. Accordingly, the study's RQ2 is stated as:

RQ3. Does a common basis for headline budget balance numbers exist across the nine Australian Governments in their 2011-2012 budgets?

In suggesting a common basis for headline budget balance numbers by the final year of the study's research period, the question arises as to what that basis might be. Given the move to a full accrual accounting system and the promulgation of AASB 1049, it would be expected that the budget balance number headlined by the nine Australian Governments would be a total (net) accrual accounting based surplus/deficit number. As explained earlier, Operating Result represents the total (net) AASB 1049 full accrual accounting surplus/deficit measure. The study's RQ3 is therefore stated as:

RQ4. Is Operating Result, representing the total (net) full accrual accounting based surplus/deficit number, the basis for headline budget balance numbers across the nine Australian Governments in their 2011-2012 budgets?

Wines and Scarborough (2006) documented the adoption by some of the nine Australian Governments of a basis for the headline budget balance number that departed from one of the bases specified in the GFS and GAAP frameworks applicable at the time. For example, the Tasmanian Government in its 2005-2006 budget headlined an "underlying fiscal surplus" of 44.5 million (Parliament of Tasmania, 2005). This was calculated by adding back \$50 million of "Special Capital Investment Funds Expenditure" to the net lending/borrowing (fiscal) deficit of \$5.5 million. Hence, a far more favourable budget balance number was portrayed (Wines and Scarborough, 2006). It would be expected that, given the existence of AASB 1049 as a formal, single accounting standard issued under the authority of the Australian standard setting body, governments would be less likely to present budget balance numbers that depart from those specified within the standard. Accordingly, the study's RQ4 is stated as:

RQ5. Do any of the nine Australian Governments use a basis for their 2011-2012 headline budget balance number that departs from one of the AASB 1049 measures?

5. Research method

The paper's case study research method is based on an examination of the budget balance numbers headlined in the general government sector budgets of the nine Commonwealth, State and Territory governments in Australia [8] over the eight annual budgets for the financial years 2004-2005 to 2011-2012. The research data were collected from the annual budget statements/papers of each of the governments over the research period, and the research method is based on a content/documentary analysis of the headline budget balance numbers in those budget statements.

Given that AASB 1049 became operable for annual reporting periods beginning on or after 1 July 2008 (AASB, 2006), the research period spans the years before and after the implementation of AASB 1049. The research period therefore enables observation of the period of transition from the previous GFS and GAAP (AAS 31) frameworks to AASB 1049.

By examining an extended (eight year) period following the move to accrual accounting, the study's research method allows both a cross-sectional examination of the budget reporting across the nine governments and a longitudinal examination over a period of time in which an important public sector accounting pronouncement was developed and promulgated.

Table II. Bases for headline budget balances

	Frequency 2004-2005	Frequency 2005-2006	Frequency 2006-2007	Frequency 2007-2008	Frequency 2008-2009	Frequency 2009-2010	Frequency 2010-2011	Frequency 2011-2012
<i>Panel A</i>								
Basis for calculation of <i>Headline</i> budget balance								
Cash	2	1	1	1	1	1	1	1
"Adjusted" underlying cash		1	1	1	1	1	1	1
AAS 31 (GAAP)	2	1						
GFS net lending/borrowing	3							
"Adjusted" (underlying) GFS net lending/borrowing		1	1					
Net operating balance (GFS/ AASB 1049)	2	5	6	7	7	6	6	6
"Adjusted" net operating balance						1	1	1
Total number of government budgets	9	9	9	9	9	9	9	9
<i>Panel B</i>								
Number of alternate <i>headline</i> budget balance measures adopted across the nine governments	4	5	4	3	3	4	4	4

6. Research findings

A frequency distribution of the bases for the headline budget balances across the eight financial years from 2004-2005 to 2011-2012 is presented in Table II. The bases for the headline budget balances for each of the nine governments in the first and final years of the research period (2004-2005 and 2011-2012) are presented in Table III.

Table III. Bases for headline budget balances: 2004-2005 and 2011-2012

Government	Basis for calculation of <i>Headline</i> budget balance	
	2004-2005	2011-2012
Commonwealth	Cash	"Adjusted" underlying cash
<i>States</i>		
New South Wales	Net lending/borrowing	Net operating balance
Queensland	Net operating balance	Net operating balance
South Australia	Net lending/borrowing	Net operating balance
Tasmania	Net lending/borrowing	Net operating balance
Victoria	AAS 31 (GAAP)	Net operating balance
Western Australia	Net operating balance	Net operating balance
<i>Territories</i>		
ACT	AAS 31	"Adjusted" net operating balance
Northern Territory	Cash	Cash

Panel A of Table II presents a frequency distribution of the number of Australian Governments adopting each of the alternate bases for their headline budget balance number, and Panel B summarises the number of alternate headline budget balance measures adopted in each financial year. For example, in their 2004-2005 budgets, Panel A reveals that two governments adopted a cash basis for their headline budget balance, two the AAS 31 measure, three the net lending/borrowing (fiscal) balance and two the net operating balance. Hence, and as shown in Panel B, four different measurement bases for headline budget balances were adopted across the nine governments in their 2004-2005 budgets.

In their budgets for the 2005-2006 financial year, Panel B of Table II shows that five different measures were used across the nine governments for their headline budget balances. This represented the highest number of alternate measures adopted for the headline surplus/deficit measure across the nine governments in a single year of the eight-year research period. However, Panel A of the table shows that there is a single measure, the net operating balance (from transactions), that has been adopted by a majority of the governments for the 2005-2006 financial year. Five governments had adopted the net operating balance for their headline budget balance [9], with each of the other four governments adopting an alternate measure.

The Table II figures for the 2006-2007 government budgets reveal a continuation of the trend toward the adoption of the net operating balance as the basis for the headline surplus/deficit number, with six governments adopting that measure [10]. Three governments, though, each used an alternate measure for their headline surplus/deficit number in their 2006-2007 budgets.

Across the research period, the lowest number of alternate bases for the headline budget balance occurred in the 2007-2008 and 2008-2009 budget years. These years also saw continuation of the trend towards use of the net operating balance, with seven of the nine governments now adopting that measure as the basis for their headline surplus/deficit number [11]. The two governments not adopting the net operating balance as their headlined measure in their 2007-2008 and 2008-2009 budgets were the Northern Territory (adopting the cash basis) and the Commonwealth Government (adopting an "adjusted" underlying cash basis). Hence, despite the move in the Australian general government sector to accrual accounting, these two governments continued to headline cash based budget balance numbers.

The “adjusted” underlying cash basis headlined by the Commonwealth Government requires explanation. This basis, summarised in Table IV for the 2009-2010 to 2011-2012 budget years, deducts earnings from the Commonwealth Future Fund from the cash based surplus/deficit number calculated in accordance with Australian Accounting Standards. The Commonwealth’s Future Fund was established in 2006 to “make provision for unfunded superannuation liabilities that will become payable during the period when an ageing population is likely to place pressure on the Australian Government’s finances” (Future Fund, 2006, p. 3). The net assets of the Future Fund at 30 June 2011 amounted to \$75.3 billion (Future Fund, 2011).

The Commonwealth Government has reported this “underlying” cash balance, excluding Future Fund earnings, from the 2005-2006 budget year based on the argument that the fund’s earnings “will be reinvested to meet future superannuation payments and are therefore not available for current spending” (Commonwealth Treasury, 2005, pp. 2-9). Further, the then Commonwealth Treasurer stated that:

The underlying cash balance is a fiscal aggregate that has been developed for macroeconomic policy purposes. It is not a statistical or accounting concept [12].

Whatever the government’s argument, the fact remains that, as with any other investment or asset within the general government sector, the Future Fund is part of the sector. The assets and liabilities of the Future Fund are included in the Commonwealth’s general government sector balance sheet, and, in fact, the Future Fund investments are not even held in a separate entity [13]. Moreover, deduction of the Future Fund earnings from the cash surplus/deficit in presenting the headline measure implicitly recognises that those earnings were, in the first place, a component of the general government sector’s total earnings. Hence, deduction of Future Fund earnings in deriving the underlying cash balance represents a case of the Commonwealth Government headlining a budget balance that is not calculated in conformity with the bases presented in AASB 1049. Further, the figures presented in Table IV indicate that this adjustment represents a material variation, for example, it results in a 14.9 per cent variation in the 2011-2012 deficit figure.

Table II shows that there were four alternate bases for the headline budget balance in government budgets for the three financial years 2009-2010, 2010-2011 and 2011-2012. This increase in the number of alternate measures from 2008 to 2009 occurred due to the Australian Capital Territory (ACT) changing from a net operating balance to an “Underlying Net Operating Balance” (UNOB) for its headline measure. This UNOB number, summarised in Table V for the 2009-2010 to 2011-2012 budget years, results by deducting the “net impact of stimulus initiatives” from the net operating balance. This measure represents a departure from AASB 1049 and, significantly, was not adopted by the other States and the Territories whose budget were similarly affected by the Commonwealth Governments stimulus spending in the wake of the global financial crisis at the time.

Table IV. Basis for Commonwealth’s headline budget balance

Budget balance	2009-2010 \$ million	2010-2011 \$ million	2011-2012 \$ million
Cash surplus/(Deficit)	(54,661)	(45,995)	(19,687)
Less future fund earnings	(2,932)	(3,374)	(2,931)
Underlying cash surplus/(Deficit)	(57,593)	(49,369)	(22,618)
Difference (%)	5.4	7.4	14.9

But to add further confusion to the ACT's budget balance numbers, and as depicted in Table V, a further adjusted net operating balance number, the "Headline Net Operating Balance" (HNOB) was introduced in the 2011-2012 budget. The basis for the HNOB is the net operating balance plus "expected long-term gains on superannuation investments". By adding expected long-term gains amounting to \$78.7 million to the net operating balance deficit of \$115.6 million, the amount of the HNOB deficit was reduced to \$36.9 million. Again, as for calculation of the UNOB, this adjustment was not made by any other government in Australia.

7. Discussion

Discussion of the research findings is presented in this section. Discussion focuses first on findings in relation to each of the specific research questions, followed by general observations.

7.1 Has there been a reduction in variation in the basis for headline budget balance numbers?

Findings show there has been a trend towards adoption of the net operating balance as the headline budget balance measure by a majority of the governments. Six of the nine governments, the six States, adopted this measure in the latter three financial years of the study period. However, the three remaining governments adopted different headline budget balance measures, resulting in four different measures across the nine governments in the latter three years of the research period. This was the same number of alternate bases as existed pre-AASB 1049 in the first year of the research period, 2004-2005. While there has been a trend by the six States to headline the net operating balance, the three other governments (the Commonwealth and the two Territories) headlined budget balance numbers prepared on inconsistent bases. Over the entire eight years of the research period, there has been no reduction in the variation in bases for headline budget balance numbers in terms of the number of alternate bases adopted, and this research question is therefore answered in the negative.

7.2 Is there a common basis for 2011-2012 headline budget balance numbers?

There has been some trend, as noted above, towards commonality with the six States adopting a common (net operating balance) basis. However, in their budgets for the three latest years of the study's research period, two governments (the Commonwealth and the Northern Territory) headlined cash-based, rather than accruals-based, deficit numbers, and two governments (the Commonwealth and the Australian Capital Territory) headlined budget balance numbers that represent a departure from one of the AASB 1049 bases.

Table V. Bases for the Australian capital territory's headline budget balances

Budget balance	2009-10 \$ million	2010-11 \$ million	2011-12 \$ million
Net operating balance (NOB)	(82.2)	(83.9)	(115.6)
<i>Plus</i> Expected long-term capital gains on superannuation investments			78.7
Headline net operating balance (HNOB)			(36.9)
<i>Less</i> Net impact of stimulus initiatives	(165.1)	(88.8)	(16.0)
Underlying net operating balance (UNOB)	(247.3)	(172.7)	(52.9)
Difference between NOB and UNOB (%)	200.9	105.8	54.2

Accordingly, this research question is answered in the negative. Despite the introduction of AASB 1049, a common basis for the 2011-2012 headline budget balance number of the nine governments has not emerged. A common basis in the 2011-2012 year exists only across the six States.

7.3 Is “Operating result” the basis for 2011-2012 headline budget balance numbers?

This research question suggested that operating result, representing the total (net) accrual accounting-based surplus/deficit number, would be the basis for headline budget balance numbers across the nine Australian Governments in their 2011-2012 budgets. However, on the contrary, research findings indicate that none of the nine governments in Australia headlined operating result in their budget, indicating that not one of these governments headlined a budget balance number representing a full accrual accounting measure.

7.4 Do any of the 2011-2012 headline budget balance numbers depart from one of the AASB 1049 measures?

As explained earlier, two governments (the Commonwealth and the ACT) adopted bases for their 2011-2012 budget balance number that departed from one of the AASB 1049 measures. The Commonwealth adopted an “adjusted underlying” cash basis for its headline budget balance, where Future Fund earnings were deducted from the cash surplus/deficit. The ACT adopted an “adjusted” UNOB basis in the three budgets for the 2009-2010 to 2011-2012 periods involving adjustments for the net impact of stimulus initiatives. Further, in its 2011-2012 budget, the ACT Government introduced a further adjusted budget balance number, the HNOB. This involved a further adjustment adding back expected long-term capital gains on superannuation investments.

7.5 General observations

Study findings indicate the adoption of varying measurement bases and some lack of inter-government comparability in headline budget balance numbers across the Australian general government sector. Despite the rhetoric that full accrual accounting has been adopted across the general government sector in Australia, none of the nine governments adopted operating result as their headline budget balance measure in the latest year of the research period, 2011-2012, nor indeed in any year since the introduction of AASB 1,049. The net operating balance measure headlined by the majority of the nine Australian Governments, the six State Governments, is not a full accrual accounting based measure but one based only on transactions. Further, two governments headlined cash based measures in their budgets.

The selection by governments between alternative budget balance numbers has parallels in the private sector. The reporting of non-statutory (non-GAAP) profit numbers by Australian public companies is becoming increasingly common. Companies are increasingly announcing and disclosing, often on an inconsistent and selective basis, additional non-statutory profit numbers using titles such as adjusted, underlying, normalised, core, economic and cash earnings/profit (Ernst and Young, 2007; Finsia and AICD, 2008, 2009; King, 2009; KPMG Australia, 2010a, 2010b, 2011) [14]. While companies argue that the non-statutory performance measures provide more relevant and understandable information, the lack of mandatory guidance has resulted in considerable variation in the quality of the reported figures and inconsistencies in how the measures are calculated, both between companies

and between reporting periods (Finsia and AICD, 2009; KPMG Australia, 2010b; Australian Securities and Investments Commission, 2011).

But there is a further dimension with respect to the headlining of budget balances by governments in Australia. A single basis exists for the statutory profit number for a public company in the private sector [15]. However, there are a number of alternative accrual and cash based measures within the government reporting framework from which governments can select. And, as starkly illustrated by the example of the Australian Capital Territory, governments are also free to make further adjustments to those measures. Hence, this study illustrates the greater scope for flexibility available in financial reporting and in the accounting numbers emphasised in the Australian Government sector in comparison to that in the private sector.

The question arises as to the possible explanation for the budget balance numbers chosen to be headlined by the nine Australian Governments. In the case of private sector entities, prior research finds that non-GAAP (non-statutory) numbers presented, in comparison to statutory numbers, tend to:

- show better performance;
- avoid the reporting of a loss; and
- beat strategic earnings benchmarks, such as analyst forecasts or the previous year's result[16].

What can be concluded from the budget balance numbers headlined by Australian Governments?

With the move to accrual accounting and the promulgation of AASB 1049, a commonality is that the surplus/deficit measures headlined by the nine Australian Governments comprise, or represent adjustments to, the net operating balance or the cash budget balance bases. The headline measures adopted by the nine governments, therefore, represent budget balance numbers based only on transactions. They exclude the effect of accrual accounting entries for other economic flows that would be included in the final accrual-based deficit/surplus number, being operating result. Examples of these other economic flows include impairment losses, fair value adjustments and other asset writedowns, foreign exchange gains and losses, superannuation fund gains and losses, and expenses recognised via accrual provisions. Importantly, these other economic flows are often, by their very nature, particularly material and unexpected.

There are two aspects to the headlining by the nine governments of budget balance numbers based only on transactions. First, that approach generally allows the headlining of the most favourable figure (i.e. the highest surplus or lowest deficit number). For example, an examination of Table I shows that, for the Queensland and Victorian State Governments, the net operating balance headlined by them presents the most favourable figure of the four alternatives.

Second, and probably more importantly, there is an associated benefit when the original budget balance number is compared with the actual final outcome at a later point in time. By headlining a budget balance number that excludes other economic flows, potentially large and unexpected items are more likely to be ignored or given less emphasis in any subsequent comparison of actual outcomes with the original budget. Moreover, a surplus/deficit measure based only on transactions will be less subject to fluctuation than one based on full accrual accounting, enabling a smoother long-term trend to be portrayed. A further observation is that the headline budget balance numbers of the nine Australian

Governments, in being based on transactions only and excluding other economic flows, are consistent with the GFS system rather than with full accrual accounting. In documenting the move from the earlier cash based version of GFS to public sector accrual accounting in the Australian State of New South Wales, Christensen and Parker (2010) referred to the competition between public sector economists and accountants. Our research findings point to the hybrid nature of accrual accounting as it has developed in the Australian Government sector in response to these types of influences. Even with an attempt to harmonise the previous GFS and GAAP frameworks, our study points to the continuation of the GFS transactions based methodology when it comes to Australian general government sector headline budget balance numbers.

This finding can be highlighted in the context of those of Kober et al. (2013). They surveyed the perceptions of public sector stakeholders on the appropriate accounting treatment and presentation of various financial items pursuant to AASB 1049. Findings indicated a mixed preference for GFS and GAAP accounting treatments across a number of different areas and a clear preference for GFS presentation methods. Also, prior researchers have stressed the view that the accounting information required in a public sector context is different to that in the private sector (Barton, 1999; Newberry, 2001; Ellwood and Newberry, 2006), and have advocated the continued usefulness of GFS information for the public sector (Challen, 2004; Barton, 2005). Thus, the GFS concepts continue to be prevalent and AASB 1049 allows for them to be flexibly integrated into the harmonised rules.

The GFS basis, as noted earlier, was developed by the IMF to enable international statistical comparisons for economic purposes. This emphasises that, in the Australian Government sector, the nature of the adoption of accrual accounting continues to reflect previous economic influences. The budget balances being headlined are consistent with the transactions-based framework favoured by economic bodies such as the IMF and, in Australia, the ABS. The study, therefore, illustrates the manner in which economic concepts can continue to have persistent effects despite the promulgation of a specific authoritative accounting pronouncement such as AASB 1049.

From an agency perspective, study findings suggest problems in terms of the electorate and general public (principals) using budget information to monitor the politicians (agents), and suggests concerns arising due to information asymmetry. Findings related to the nine Australian Commonwealth, State and Territory Governments can be summarised as follows:

- the different governments adopt varying bases for their headline budget balance number;
- individual governments can change the basis for presentation of their headline budget balance number over time;
- the headline budget balance numbers of the nine Australian Governments are cash or accrual transaction based numbers, and therefore, exclude many potentially large, unexpected and fluctuating items; and
- governments can headline a budget balance number that represents a departure from the measures presented in the relevant accounting standard, AASB 1049.

Monitoring and information asymmetry problems manifest themselves not due to the information is conveyed and presented. The headlining of alternate budget balance numbers results in the potential for the public to be influenced in their perceptions regarding fiscal management and fiscal responsibility. These are key aspects in analysing the

performance of the agents (politicians/governments). Uncertainty in assessing an agent's performance reduces the quality of the contract between the principal and the agent, with the potential for deterioration in accountability (Eisenhardt, 1989; Kasdin, 2010; Benito and Bastida, 2009).

Study findings indicate that analysis of government budget balance numbers in Australia would be extremely difficult for those without detailed accounting knowledge. This allows politicians to potentially conceal a full picture. Even for those with sufficient accounting knowledge, and for media reporters who report on government budgets, full understanding of budget numbers can only be ascertained by delving into the minutiae of the disclosures that are spread throughout the voluminous budget papers. This again emphasises the difficulty of fully understanding the budget balance number headlined by an individual government in an individual year. Understanding the full detail would be beyond the comprehension of the average voter, hence highlighting the ability of the politicians, who make the rules, to be selective in the budget information they highlight. From a principal-agent perspective, this again illustrates monitoring and information asymmetry problems.

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

Terms such as “budget surplus” or “budget deficit” are potent political symbols. Politicians claim success if they have “reined in” a deficit or “returned” a surplus, or “balanced” a budget.

However, findings of this study suggest considerable difficulty, in an agency context, of the electorate monitoring politicians in respect of government budget balance numbers despite the political importance of such figures.

Study findings suggest considerable scope for further research. The study has investigated the adoption and use of accounting numbers within a public sector economic and political setting. Further research could examine the final financial statements in which final budget outcomes of the governments are presented, and could particularly examine the nature of the comparisons to original budget that are made in those final financial statements. Further research could also investigate the political dynamics behind the headline budget balance numbers adopted by the various governments. This could be examined in association with various significant events, such as government elections. While this study examined the Australian situation, further research could examine the issue in other countries where accrual accounting has been adopted. The topic could also be examined from various theoretical viewpoints, especially that of “impressions management”. The manner in which the media reports government budget balance numbers also represents a fruitful area for future research.

8. Summary and conclusions

An important aspect of government budgets is the transparency of government reporting and the presentation of the overall budget surplus or deficit number. A commonality of all government budgets is that they tend to focus on a single budget balance number that is headlined, and given prominence, in the relevant budget speech and/or budget papers. An apparently basic concept such as a government deficit or surplus, though, is subject to

considerable ambiguity, questions of usage and conflicting definitions and measurement bases.

The study makes a theoretical contribution in highlighting the ambiguity in the government budget balance numbers presented and the monitoring and information asymmetry problems that can arise. Research findings indicate that different governments, in implementing the same standardised accrual accounting rules, can adopt varying bases for their headline budget balance numbers, including bases that depart from the relevant accounting standard, and can change the basis for presentation of their headline budget balance number over time. Findings also show that the headline budget balance numbers of the nine Australian Governments are more consistent with the GFS system than with full accrual accounting, highlighting the hybrid nature of accrual accounting as it has developed in the Australian Government sector. Attempts to harmonise the previous GFS and GAAP frameworks in Australia indicate the competition between public sector economists and accountants and the influence of guidelines developed by bodies such as the International Monetary Fund and the United Nations.

Findings point to the scope for governments to be selective in the manner in which they calculate and present important budget aggregates. Confusion and misunderstanding can therefore arise, and politicians can exploit the lack of clarity. This is a significant issue as the budget balance number is one of the most important measures, if not the most important one, used to evaluate a government's fiscal management and responsibility. The monitoring and information asymmetry problems that arise result in the potential for the public, as principals, being influenced in their perceptions regarding a government's fiscal management, thereby affecting analysis of the performance of politicians as agents for the electorate and the public more generally.

The study adds a further dimension to our understanding of government budgets and public sector accounting. The study illustrates the manner in which economic and political influences can continue to have persistent effects despite the promulgation of a specific authoritative accounting pronouncement such as AASB 1049. Also, while examining the Australian Government sector, research findings have wider relevance internationally in highlighting issues arising with the public sector adoption of accrual accounting.

Notes

1. These nine governments are the Australian Commonwealth (Federal) government; the six States of New South Wales, Queensland, South Australia, Tasmania, Victoria and Western Australia; and the two Territories, being the Australian Capital Territory and the Northern Territory.
2. See, for example, Robinson (2002), Barton (2007, 2009), Jensen and Wanna (2003), Wines and Scarborough (2006), Hawke and Wanna (2010) and Kober et al. (2010).
3. Bergman and Lane (1990, p. 339) identify the electorate as the principal of the political body of a democracy. Boston (1995, p. 10) explains that voters can be seen as principals who purchase various services from their agents, namely MPs and Parliament.
4. When originally introduced, the GFS adopted a cash- rather than accruals-based approach (Allan, 1993; ABS, 2003, p.5).
5. For example, accrual-based income and expense items, such as doubtful debts provisions, asset write-downs and impairment losses, foreign exchange gains and losses and superannuation fund gains and losses, are not included in the calculation of the GFS net operating balance.

6. See ABS (2005, chapter 7) for elaboration on the accounting policy differences between AAS31 and the GFS framework. Also note that recent amendments to the GFS framework have resulted in defence weapons platforms now being treated in the same way for GFS and Australian accounting standard purposes (ABS, 2011, p. 2). For a general discussion of differences between accounting and statistical bases of financial reporting in the public sector and recommendations for convergence, see International Public Sector Accounting Standards Board (2005).
7. In fact, the definitions for these three budget balance numbers in AASB 1049 indicate that they are directly based on the ABS definitions (AASB, 2009b, Appendix A).
8. These nine represent all the governments in Australia that are subject to AASB 1049.
9. These governments were the States of New South Wales, Queensland, South Australia, Victoria and Western Australia.
10. This was caused by the Australian Capital Territory changing from the AAS 31 basis in their 2005-2006 budget to the net operating balance for 2006-2007.
11. This resulted from Tasmania moving to headline the net operating balance.
12. Personal correspondence with former Commonwealth Treasurer The Hon Peter Costello MP, 14 July 2006.
13. The Future Fund was established pursuant to the Future Fund Act 2006 (Commonwealth of Australia, 2006). While the body administering the Fund, the Future Fund Board of Guardians, is a separate legal entity (body corporate) pursuant to the Act (s. 37), the Future Fund itself is not. The Fund consists of the Future Fund Special Account (the Fund Account) and the investments of the Fund (s. 11).
14. Major adjustments in deriving non-statutory profit numbers tend to be for significant one-off transactions and events and for expenses recording downward adjustments to asset values. Examples include adjustments for foreign exchange losses, initial public offering costs, merger, acquisition and restructuring costs, special provisions, lawsuits, intangibles impairment and defined benefits superannuation expense (Finsia and AICD, 2008, 2009; KPMG Australia, 2010a, 2010b, 2011).
15. Although there is, nevertheless, some degree of flexibility in accounting policy choice within accounting standards.
16. See Bhattacharya et al. (2003, 2004), Lougee and Marquardt (2004), Bowen et al. (2005), Marques (2006), Black and Christensen (2009), and KPMG Australia (2010a, 2010b, 2011).

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4. Research questions

A commonality of Australian Government budgets is that they tend to focus on a single budget balance number that is headlined in the relevant treasurer's budget speech and/ or in the budget papers. The term headline budget balance is used in this paper to indicate the budget deficit or surplus number that is given prominence in the budget papers, including the treasurer's budget speech, as the overall budget balance number. The headline budget balance is, in turn, the surplus or deficit number given prominence in the media's coverage of an individual government's budget, and is therefore also the measure of the government's surplus or deficit that the general public (the electorate) becomes most aware of. It is an example of an accounting-based number being presented in a political environment.