Innovations in Governmental Accounting

Edited by
Vicente Montesinos and José Manuel Vela

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Edited by

Vicente Montesinos
University of Valencia, Valencia, Spain

and

José Manuel Vela
University Jaume I, Castellón, Spain

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CONTENTS

CONTRIBUTORS

Philippe Adhémar	International Federation of Accountants FRANCE
Remco J. Admiraal	Dutch Association of Water Boards THE NETHERLANDS
Aad D. Bac	Tilburg University THE NETHERLANDS
María T. Balaguer	University Jaume I, Castellón SPAIN
Bernardino Benito	University of Murcia SPAIN
Mary Bowerman	Sheffield University Management School U.K.
Isabel Brusca	University of Zaragoza SPAIN
Carmen Caba	University of Almería SPAIN
Ana Cárcaba	University of Oviedo SPAIN
James L. Chan	University of Illinois at Chicago USA
J.R. Christiaens	University of Gent BELGIUM
Joao B. Da Costa	Universidade do Minho PORTUGAL
M.José Da Silva	Instituto Politécnico do Cávado e do Ave PORTUGAL
Patrick J. Devlin	Glasgow Caledonian University U.K.

Sheila Ellwood	Aston University U.K.
Iluminada Fuertes	University Jaume I, Castellón SPAIN
Gary Giroux	Texas A&M University U.S.A.
Alan D. Godfrey	Glasgow Caledonian University U.K.
Noel Hepworth	Fédération des Experts Comptables Européens U.K.
Christopher Humphrey	Sheffield University Management School U.K.
Manuel Illueca	University Jaume I, Castellón SPAIN
Gwenda Jensen	Victoria University of Wellington AUSTRALIA
Rowan Jones	University of Birmingham U.K.
Evelyne Lande	University of Rouen FRANCE
Sir Andrew Likierman	H.M. Treasury U.K.
Antonio López Díaz	University of Oviedo SPAIN
A. M. López Hernández	University of Granada SPAIN
Klaus Lüder	Speyer University GERMANY
Kristina Lundkvist	Swedish National Financial Management Authority SWEDEN

Helge Mauland	Stavanger University College NORWAY
Frode Mellemvik	Bodø Graduate School of Business NORWAY
Cherif Merrouche	Glasgow Caledonian University U.K.
Vicente Montesinos	University of Valencia SPAIN
Víctor Nicolás	Ministry of Finance SPAIN
Wojciech Nowak	University of Lodz POLAND
José Luis Pablos	University of Oviedo SPAIN
June Pallot	University of Canterbury NEW ZEALAND
Elvira Rodríguez	Ministry of Finance SPAIN
M.P. Rodriguez	University of Granada SPAIN
Marc A. Rubin	Miami University U.S.A.
G. Jan Van Helden	University of Groningen THE NETHERLANDS
C. Vanhee	University of Gent BELGIUM
Kiyoshi Yamamoto	Centre for National University Finance JAPAN

FOREWORD

In recent years, the field of Accounting has witnessed events of major importance and of a far-reaching nature, both from the perspective of business and the real economy, and from a financial viewpoint. The impact of these events is felt across the length and breadth of our economies, which are in turn intrinsically inter-linked to the international scene.

There can be no doubt that these events have stimulated an in-depth reflection within the sphere of accounting, in both professional, and academic and Accounting research circles. The extent and the depth of this Accounting crisis are of paramount importance, perhaps the most important to be seen since the times of the Great Depression. We can speak of "crisis" in terms of how it is popularly seen by the public, but also in the methodological sense so well presented by the master Karl Poper: a crisis which augurs a genuine scientific revolution in Accounting, or perhaps, at least a set of circumstances that might decidedly precipitate the transformation of the major lines of the paradigm on the use of accounting information into concrete results.

It is obvious that the spheres in which Business Accounting and Governmental Accounting are developed are quite distinct, and that the important distinctions between the two areas cannot be ignored or underestimated when it comes to proposing reliable and guaranteed research work into either one of these Accounting areas. However, we would also be committing an extreme error, and going against the very development of the events of recent years, if we were to ignore the conceptual common core shared by the two great branches of Accounting, and hence, their parallel evolution. A good example of the parallel evolution of Governmental Accounting and Business Accounting is to be found in the work of the International Federation of Accountants (IFAC), whose Public Sector Committee (PSC) publishes Accounting Standards (IPSAS) which are completely homologous with the Business Standards issued by the IASB (International Accounting Standards Board).

Furthermore, Governmental Accounting is playing a particularly significant role in the follow-up, control and discipline of Public Finance, for which a useful Public Sector Accounting is required to meet the new objectives set by public managers. This presupposes that governmental accountants and, by the same token, Government Accounting researchers have to be particularly alert to innovations which are constantly taking place in subjects related to management, information systems and control of public entities. In light of the above, the title "Innovations in Governmental Accounting" chosen for this volume seemed to be appropriate. The choice of this title is intended to highlight the importance and speed which accompany the complete range of changes typical of our modern day society: social and political, economic and financial, technological and cultural changes which, without the shadow of a doubt, are triggering a fast-moving and extensive evolution within Accounting in general, and particularly within Governmental Accounting.

This volume is based on the papers presented at the 8th Biennial CIGAR Conference, held in Valencia (Spain), on the 14th and 15th June, 2001, following which, considerable selection and restructuring work has been carried out on the original articles, in order to accommodate them to the objectives and structure of this book. Over recent decades, intense research work has been carried out into the subject of Governmental Accounting under the umbrella of CIGAR (Comparative International Governmental Accounting Research), research which has given rise to the formation of an international network of specialists who are undertaking a mounting volume of activity with an ever increasing impact.

The Biennial CIGAR Conference, held every two years, tackles the questions of greatest pertinence to this area of study, and thereby provides a platform for the fruitful exchange of ideas and experiences. The last three Conferences, held in Milan, Tilburg and Valencia, have resulted in the publication, by Kluwer Academic Publisher, of respective volumes, which has led to a greater circulation and advantage being taken of the papers discussed at each of these encounters.

The work we present here is divided into seven sections, which correspond to other current issues in the area of Public Sector Accounting. In our view, a simple glance at the names of the authors of the various chapters in the book is sufficient to guarantee the quality and interest offered in this volume. However, we should also stress that a careful selection of the papers to be included, an anonymous evaluation of the book, and finally an in-depth revision and maximum up-dating of the content of all the chapters contained in the book has been conscientiously carried out prior to publication. As editors of this edition, we wish to thank the authors most sincerely for their collaboration and understanding, which has made the presentation of this volume possible.

The first section of the book is entitled Governmental Accounting Research Methodology and includes four articles which set out the main lines of current research in Public Sector Accounting, considered from the international comparative perspective which constitutes the principal focus of the CIGAR network.

The first chapter presents the illuminating work of Klaus Lüder, President of the CIGAR network, on the achievements and problems of research in comparative governmental accounting over the last decade. The work analyses the development of the main comparative research work carried out in what, to a great extent, could be considered as the Professor Lüder school, and developed from the basis of his seminal works on the application of the contingency model to Governmental Accounting research and its subsequent revision. The analysis of innovations and the framework provided by the Financial Management Reform Process Model (FMR) for the evolution of Public Sector Accounting are equally outstanding aspects of this work, which to a certain extent, acts as a general framework for questions dealt with in later chapters of the book.

The second chapter covers the critical reflections of James L. Chan on the crucial questions facing research in International Governmental Accounting, such as the need to consider governmental sub-national levels as units of analysis, the appropriateness of introducing specific case studies and the use of dynamic models and positive methodology in Governmental Accounting research. Each one of these aspects is without doubt an important reference in the orientation of the current evolution of work and research in the subject.

The third chapter, by Patrick Devlin, Alan Godfrey and Cherif Merrouche, puts forward ideas on the vital issue of cultural impact on Governmental Accounting Innovations in Developing Countries, and employs contingency model methodology in its analysis, while reconsidering its application from a cultural perspective.

Finally, the first section concludes with an interesting contribution from Wojciech A. Nowak, which emphasises the need to take into consideration different government models when making comparisons between national models of government accounting.

Three chapters are included in the second section of the book under the general heading of International Accounting Standards, which focus on the experiences of accounting standardisation currently developing in the area of Public Sector Accounting, and the expectations arising out of these experiences.

The first of the chapters, the fifth in the book, is related to the development of standards by the IFAC Public Sector Committee and is by Philippe Adhémar. Never before has any project to publish international government accounting standards had such an impact, nor aroused so many expectations as that to come out of the IFAC. For many, the IPSAS represent the essential reference point in the process of the international harmonisation of Governmental Accounting. This volume would therefore not be complete without an analysis of this critical project, as Adhémar presents in this chapter, in which its most relevant characteristics are analysed together with the situation of the standards developed by the Committee up to the date of publication of this edition.

In chapter six, Noel Hepworth presents a fascinating overview of the European experience of and attitudes to the development of International Accounting Standards. This overview looks at the role of the Fédération des Experts Comptables Européens (FEE) and the accountancy profession in Europe in connection with the introduction of public sector accounting standards. It provides a brief summary of where the development of accrual accounting is at in the various European countries and sets out some of the particular problems that exist in Europe.

From a contrasting perspective, the work of Bernardino Benito, Isabel Brusca and Vicente Montesinos looks into the possibility of using the IPSAS as a useful tool for European accounting reform. The existing diversity of accounting to be found within European public entities is examined, the harmonisation of which the European Union could undoubtedly play a vital role, whether it be through the adaptation of its own accounting reports to international standards, or by effecting a more active policy in favour of greater comparability of accounting information issuing from the governmental entities of its member states.

The third section of the book is given over to International Comparative Analysis, and includes works which offer a comparison of the government accounting systems of two or more countries. Each one of these comparative studies employs a different analytical methodology, although all of them share a common approach in highlighting the analogies and differences between the various states of national accounting, and in providing explanations for these.

In the area of European local entities, Mª Teresa Balaguer, Iluminada Fuertes and Manuel Illueca present a study on the influence of environmental convergence on accounting harmonisation. According to the results of the study, the short-term adoption of a single government accounting system for all European countries is not on the immediate horizon. Since environments are converging at a regional level, it seems more logical for the harmonisation to occur first among countries of the same region.

Continuing in the European vain, in the ninth chapter, Mª José da Silva Fernandes and Joao da Costa Carvalho introduce a comparative study of the reforms undertaken in Spain and Portugal in the field of Public Accountability. These two countries share similar systems of accounting standards regulation, and have followed a parallel process leading up to their incorporation in the European arena, culminating in their full membership of the Economic and Monetary Union. The similitude between the cultural and juridical traditions of these two countries, and the coincident evolution of their political and economic situations have given rise to much the same governmental accounting models, which have also followed similar paths in their development.

The content of chapter ten, by Kiyoshi Yamamoto and June Pallot goes beyond the European stage to analyse the Japanese experience, which is compared with the governmental accounting systems to be found in Australia, Canada, New Zealand, the UK and the USA. The Japanese government has instigated significant reforms in governmental accounting in recent years, and has adopted management systems characteristic of the private sector which has entailed the introduction of accrual criteria in accounting and budgets, performance evaluation and the practice of management audits. This paper also suggests that the recent financial management reforms should be understood not just in terms of a management style adapted from the business sector (NPM) but in terms of different governance styles: reassertion, externalisation, devolution and self-governing/communitarianism.

The fourth section of the book is given over to the presentation and analysis of National Innovative Experiences in Government Accounting, and contains five chapters which analyse national experiences either from the perspective of innovation, or from that of a transformation from traditional public sector accounting systems.

The first chapter in this section, written by Andrew Likierman, describes and analyses the main features of governmental accounting and budgetary reform in the United Kingdom, through "resource accounting and budgeting". At the present moment, this experience is a compulsory reference point in the study of the innovation processes in public management, the study of which is imperative for all countries aiming to introduce the latest innovations into their public accounts and budgets. The author's own direct responsibility in the design and application of the new system lend this chapter undeniable interest and consequence.

Chapters twelve and thirteen are also of great interest, on account of the authors' first hand responsibility in the design and setting in motion of new governmental accounting systems. In chapter twelve, Kristina Ludkvist analyses the Swedish experience, which, in recent years, has placed a greater emphasis on performance than on resources and on the development of accrual based accounting and budgetary processes. Víctor Nicolás, in chapter thirteen, clearly outlines the central lines of Governmental Accounting reform in Spain, host country of the Conference on which this volume is based. The approximation of accounting principles from the business sector and the integration of financial accounting and budgetary accounting into a single system constitute the essential features of the Spanish experience in recent years.

The last two chapters of this fourth section deal with the cases of reforms and innovations undertaken in France and Belgium, and are described by Evelyne Lande and Johan Christiaens, respectively. The two countries share a Latin standards setting traditional system, with the legal regulation exerting a heavy influence. It is of great interest to compare the developments and innovations that have occurred in two countries with similar cultural and political traditions, but with distinct reform processes. In the first of these chapters, Lande analyses the main economic and financial events which condition the budgetary and governmental accounting innovations in France, which in this work, is dealt with at central level. In contrast, in his article, Christiaens focuses on an analysis of the evolution of accounting systems in the Belgian regions. He considers the combination of the traditional cameral accounting and the introduction of the accrual basis, with the aim of achieving the objectives of both systems within a common analytical framework. Accounting reform in the Belgian regions is considered in the light of new innovative proposals and presents an analysis of its advantages and disadvantages.

The fifth section comprises three chapters, each analysing various aspects of Government Financial Reporting. The first two of these are given over to the discussion of two questions which could be defined as "emergent" in the area of Governmental Accounting: firstly the inclusion of reports on Government social benefits and secondly, the use of the Internet as a tool for the dissemination of the financial information provided by public entities. The final chapter in this section discusses the communication of financial information by local government entities.

The first of the above mentioned chapters comes from Gwenda Jensen and considers whether present business enterprise (accrual) accounting concepts support increased recognition of the future costs of social welfare obligations in public entities, with an analysis of the positions on this issue adopted by Federal Accounting Standards Advisory Board and the New Zealand Treasury. Governments should expect to experience pressure to increase their recognition of future social welfare costs. That pressure will come from the momentum inherent in a change to business (accrual) accounting combined with present political concerns about the future costs of social welfare and social insurance programs.

The article by Antonio López Hernández, Carmen Caba and Manuel Rodríguez looks into the impact of the Internet in the presentation of financial information by public entities. Over the last few years technology has changed the way in which public organisations conduct their relationships with citizens. Public financial information has been affected by this transformation. This chapter examines to what extent and in what way governments are using the Internet as a means of providing the public with economic and financial information on their activities.

Finally, chapter eighteen of this edition is consists of a contribution by José Luis Pablos, Ana Cárcaba and Antonio López Díaz. This chapter analyses the role conferred to financial reporting in local governments, under the view that an effective disclosure would satisfy the demands posed by many segments of society. Certain recommendations are also put forward with a view to improving current information communication practices, with a particular focus on the situation of Spanish local authorities.

Accounting for Performance Evaluation forms the content of the sixth section of the book. It consists of four chapters that discuss the development of performance evaluation systems in certain other sectors of activity, and set in various geographical areas. The use of accounting information as a tool for performance evaluation is gradually revealing itself to be one of the most important challenges facing both governmental accounting research and practice, given the limitations of conventional financial statements such as the Profit and Loss Account, to obtain a reliable evaluation of the management of public entities.

The first of these articles is written by Remco Admiral and G. Jan van Helden and compares management activities within the same organisation, with the objective of improving these activities and the presentation of accounts by the entities concerned. The sector under consideration is that dealing with waste water treatment in the Netherlands. Balance Scorecards on two different levels were developed: at the highest level with a limited number of indicators for external accountability and at the lowest level, with a large number of indicators for learning and improvement. This chapter looks at the way in which the Balance Scorecard for external accounting has been developed. The way in which external and internal stakeholders have been involved in the development of this scorecard is also considered.

Sheila Ellwood is the author of chapter twenty of this volume, in which she compares healthcare systems in New Zealand and the UK. In the early 1990s both the UK and New Zealand embarked on an internal market approach to allocating healthcare financial resources. However, sophisticated case-mix costing systems have thrived in New Zealand but withered in the UK. The study uses event analysis and case studies to identify differences between the two countries in the development of case-mix costing and the pricing/ funding mechanism. This study, in particular, questions whether hospital cost accounting systems are influenced by observable national differences in the healthcare funding mechanisms rather than following an evolutionary path.

Helge Mauland and Frode Mellemvik study accounting and budgetary procedures in Norwegian university colleges (NUCs) when establishing new educational programmes. The purpose of the chapter is to describe and analyse whether changes in educational programmes and changes in Ministry of Education, Research and Church Affairs funding of new programmes influence accounting in NUCs. The main question raised is how accounting functions when programmes and funding systems are changed, and especially whether there are any innovations in NUCs' accounting/calculations.

Finally, the chapter by Marc Rubin is also concerned with the education sector, although its objectives and scope differ greatly from those of the previous chapter. Here, he describes and compares the current state of providing school accountability information for five English-speaking countries. These five countries are selected for comparison because they are similar in the type of government (democratic), the percentage of gross domestic product spent on education (five to seven percent) and in the ease of obtaining current information. The method of providing and financing schools in the five countries is first examined and then the process, if any, is described for holding schools and school districts accountable for the provision of educational services.

The seventh and final section of the book deals with the Public Sector Audit. It would seem to be generally accepted that the utilisation of accounting information depends to a great extent on the confidence inspired in the user by its reasonableness. Public sector auditing has certain peculiarities, both due to the object of its attentions, the accounting and management of public entities and services, and because of the auditor itself, which in many cases is a public institution.

Chapter twenty-three includes a rigorous comparative study of quality auditors in local entities in the US and the UK, carried out by Gary Giroux and Rowan Jones. There are significant similarities between the two regimes for local government auditing in the US and the UK. However, there are also important differences. One aspect of audit quality is the timing of the auditors' report. Based on a wide sample of local entities in the UK and the USA, the authors here present their findings on materially different average reporting times between the two countries, together with the corresponding interpretations of the results of their research.

In contrast, Mary Bowerman and Christopher Humphrey provide us with an interesting analysis of performance auditing in central governments, in which they examine the first of the distinctive aspects of public auditing mentioned above. The audit of performance information has become routine in countries such as New Zealand, Finland and Sweden yet the role of audit in evaluating performance remains a controversial issue. This chapter explores such controversies in a UK context, where the national audit bodies currently have different degrees of involvement in the audit of performance information. The paper concentrates in particular on a growing debate over the right of the UK National Audit Office (NAO) to audit the Public Service Agreements (PSAs) recently issued by central government departments.

Finally, Aad Bac examines the public entity auditor in his contribution to this volume. Thus, chapter twenty-five enters into a number of questions arising around the phenomenon now being seen in the Netherlands that a number of local governments and also provincial governments are considering installing or have recently installed Auditing Institutions in addition to the long existing financial audit. Questions arising are why such needs are felt; what ways of answering the needs are being seen; what a comparison of chosen solutions shows; what limitations are encountered; what solutions are at hand for smaller municipalities; or which legislation is considered to institutionalise this type of supervision. One of the most interesting aspects of this chapter lies in the fact that to a great extent, the events described represent a significant reform in the auditing system in both local and provincial entities in the Netherlands, with institutional auditors playing a more prominent role, as a formula which appears to provide an alternative to that of the private auditing firm.

The book also includes an Epilogue, written by Elvira Rodríguez, Spanish Secretary of State for Budgets and Expenditures of the Ministry of Finance, who offers some salient final reflections on the present moment and the foreseeable evolution of Public Sector Accounting. In clear and succinct language, without oversimplifying, the author concisely outlines the tendencies that characterise the reform and modernisation processes in public accountability, while bringing financial and budgetary information into line. The utilisation of information to improve public management, its approximation to business accounting norms and the role of National Accounts data are some of the questions raised in the final part of this edition.

The channels for reforms and the introduction of innovations have been opened and most probably will remain so indefinitely, as they are a response to the changing needs of living organisations, as are our societies and the public entities which are there to provide general services to society. Knowing how to respond to the needs disclosed by this permanent reform is the permanent challenge facing researchers and professionals from the fields of Accounting, Management and Control in public entities.

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We wish here to express our deep-felt gratitude to the authors of the chapters in this book, without whose work and absolute willingness to attend to the editors' suggestions, the preparation of this volume would not have been possible.

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In the final analysis, however, the responsibility for this book lies firmly in our hands, and we would be very grateful for any suggestion that might help to improve our task in the future. The work entailed in the preparation of this edition of the book is far out-weighed by the satisfaction and honour brought by the coordination of its content, and the contact maintained with such prestigious colleagues, friends and partners.

Valencia, July 2002
Vicente Montesinos and José Manuel Vela

KLAUS LÜDER

RESEARCH IN COMPARATIVE GOVERNMENTAL ACCOUNTING OVER THE LAST DECADE – ACHIEVEMENTS AND PROBLEMS –

1. INTRODUCTION

When James Chan, Rowan Jones and I wrote in 1996: "As an organized academic activity, comparative international governmental accounting research (CIGAR) is a dozen years old" (Chan et al. 1996, p.2), it was somewhat exaggerated. Even though the UIC Symposium of 1987 and the Speyer Conference of 1989 already focused on international aspects of governmental accounting, one might call the Birmingham Conference of 1991 the first ‚real' CIGAR conference. Thus, we now look back at a period of about ten years over which the CIGAR community has produced a great number of theoretical and empirical studies in a research field that virtually did not exist before.

As in most of our countries research in governmental accounting, financial reporting, budgeting and auditing is not mainstream research and only a few scholars are interested in it. Establishing international contacts and providing an opportunity for cross-national discussions was crucial for many of us and a prerequisite for fruitful research. Moreover, the governmental accounting reform ideas emerging in the late 1980s which gained worldwide attention as well as the beginning attempts to internationally standardize governmental accounting required also an extension of views of academic accountants beyond national borders. Therefore, establishing the CIGAR network was necessary and timely.

Evidence of the CIGAR community's accomplishments is provided by seven volumes containing essays which were presented at CIGAR conferences and workshops in the 1990s (Buschor/Schedler 1994, Montesinos/Vela 1995, Chan et al. 1996, Lüder 1996, Caperchione/Mussari 2000, Jones 2000, Bac 2001). "...researchers have engaged in wide-ranging discussions of how and why various nation's governmental accounting systems differ or resemble each other. A score of country studies have been produced along with several bilateral and multilateral comparative studies" (Chan et al. 1996, p. 2).

It is of course not possible to assess this body of literature in detail. The focus of the following discussion of the state of CIGAR is rather restricted to the variants of the

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 1-21.

contingency model, its applications and its problems. This seems legitimate since a great number of active CIGAR members have dealt with the model, either by using or by extending or by criticizing it.

2. THE CONTINGENCY MODEL

2.1. The Initial Model

The initial model, first published in German in 1990 (Lüder et al. 1990) and in English in 1992 (Lüder 1992), was a by-product of the Speyer Comparative Governmental Accounting Study focused on the features of (central) government budgeting and accounting systems of half a dozen industrialized countries, their communalities, their peculiarities and pending reform endeavours. The observed differences in practices and procedures as well as in the direction, the state and the pace of reform discussions and the implementation of reforms required an explanation. Experience from our empirical research suggested that the observed differences are at least partly due to differences in the national politico-administrative settings. The contingency model therefore was the attempt to specify the features of the politico-administrative environment prevailing in a country and to identify their likely influences particularly on the outcome of governmental accounting reform processes. Main components of the model are the stimuli of a reform process, the social structural characteristics of a country, the characteristics of its politico-administrative system and existing implementation barriers (for details see Appendix Fig. 1).

The main objectives pursued with the model were twofold: Firstly, it was intended to serve as a framework for empirical investigations into governmental accounting reforms and thus facilitate the comparison of research carried out by different researchers. Secondly, it was meant as complex hypothesis aimed at contributing to the explanation of context influence on a special reform or innovation process and thus triggering research in confirming, falsifying and amending it. Of course, the evidence that can be derived from applying the initial model is rather weak and confined to statements of conduciveness of national contextual conditions to governmental accounting reform. Conduciveness of environmental factors to government accounting reform, however, is certainly not a sufficient and maybe not even a necessary condition for successful implementation of such a reform (Lüder 1994, p. 3).

2.2. Modifications and Extensions of the Initial Model

1) Discussions of the initial model and additional empirical evidence led to a revised version mainly characterized by introducing broad behavioural variables as intervening variables between the contextual variables and the dependent variable (reform process outcome), by separating political and administrative structural variables and assigning them to two different clusters and by adding the existence of a "dominating doctrine" to the conceivable and observable stimuli (Lüder 1994, p. 6). The latter permitted for instance the distinction

between "accountabilism-driven"(or "transparency-driven") and "managerialism -driven" (or "EEE-driven") reform processes (for details of the model see Appendix Fig. 2).

2) Godfrey, Devlin and Merrouche (1995, 1996) have modified the contingency model for application to developing countries. Their main contribution was the introduction of international organizations' and donor agencies' influences on the governmental accounting change process. Demands of international organizations and donor agencies providing assistance can directly or indirectly stimulate the change process. If those demands do not meet the needs of a developing country, they stimulate the wrong change and thus result in a barrier to the implementation of an adequate accounting system. Moreover, financial resources and know-how provided by international organizations and donor agencies form an element of a developing country's social structure reinforcing the change process or even making it at all possible. The availability of external resources to a country is on the other hand supposed to be affected by its international reputation, i.e. "...the standing of a country on the international stage" (Godfrey et al. 1996, p. 199). Extending this thought, one might also expect that developing countries are tempted to change their accounting systems in order to meet perceived demands of the international community and thus improve their international reputation.

3) Jaruga and Nowak (1996) suggested incorporating "the consequences of the innovation process in the real world" as an additional component into the contingency model. Those consequences are behavioural changes of the public as well as of the political and administrative actors to be expected as a result of the accounting reform. The authors also expect changes of the structural variables in the long run. This in fact means the "dynamisation" of the contingency model since it is well conceivable that an accounting reform is not a one-time event but runs through several phases or cycles and that the result of a prior phase triggers subsequent reform steps. Such a dynamized model seems particularly appropriate for describing and explaining the accounting reform of slow, stepwise reforming countries (for details of the model see Appendix Fig. 3).

A dynamic extension of the contingency model has also been proposed by Godfrey, Devlin and Merrouche (2001, p. 280). The contingency module of what they call "diffusion-contingency model" is used to assess "organisational innovativeness". It is complemented by an implementation module aimed at characterizing the innovation decision process. The consequences of that process are then fed back to the elements of the contingency module (for details of the model see Appendix Fig. 4).

4) A number of scholars contributed to the completion and precision of the (initial and modified) contingency model by adding and specifying variables.

Budäus and Buchholtz (1996, p. 33) applying the contingency model to local government management accounting reform establish that the outcome of the reform depends on the significance of so-called hard and soft factors guiding the reform process. Dominating hard factors (procedures and instruments) over soft factors (change of behaviour and attitude) and vice versa is supposed to be a characteristic of the administrative culture of a government. Yamamoto (1997, 2000) pursues a similar but more comprehensive approach as he distinguishes different types of governance (specification of the contextual variable "political system") and different types of management (specification of the contextual variable "administrative culture"). He maintains that there is an unambiguous relationship between a specific type of governance, management and accounting system and concludes that the outcome of a government accounting reform must be unsatisfactory if the new accounting system does not fit the governance and management systems.

Pallot (1996) stresses that a successful implementation of an innovation "also depends on how well the process is managed" (Pallot 1996, p. 345) and consequently introduces variables relating to the management of the implementation process. The cluster of process variables comprises the timing of implementation, incentives for implementation and enacting the necessary legislation.

An important extension of the contingency model has been put forward by Laughlin and Pallot (1998). Refering to an article of Haas (1992) they stress the significance of so-called epistemic communities in triggering governmental accounting reform and influencing direction and outcome of a reform process. "An epistemic community is a network of professionals with recognized expertise and competence in a particular domain and an authoritative claim to policy-relevant knowledge within an area" (Haas 1992, p. 3). The particular characteristic of an epistemic community is that it is an informal, loose network of recognized experts with shared beliefs and convictions how to resolve a certain political or administrative problem. The epistemic communities "... approach is instrumental and their life is limited to the time and space defined by the problem and its solutions" (Adler/Haas 1992, p. 371). Laughlin and Pallot were able to identify more intellectual and more pragmatic epistemic communities as they reviewed the governmental accounting reform approaches and processes of eleven industrialized countries. Thus, it seems appropriate to add "epistemic communities" as another contextual variable to the contingency model.

2.3. Country Studies and Cross-Country Comparisons

For scholars interested in governmental accounting, the CIGAR conferences and workshops in the 1990s have certainly been an incentive to prepare studies on the state of governmental accounting ,financial reporting and auditing as well as on pending or ongoing reforms in their respective countries. A whole set of those country studies is now available and has been published. A considerable number of authors used the contingency model or elements of it to describe a country's contextual situation and/or explain governmental accounting innovations. The availability of the model might for some time have caused an emphasis on the context of governmental accounting over its content (Chan et al. 1996, p. 11). But whether this has been disadvantageous seems questionable given the accountants' usual negligence of contextual issues.

Countries covered by studies on national and/or local governmental accounting and financial reporting that used the contingency model or were "inspired" by it comprise the United States (Chan 1994), Switzerland (Mäder and Schedler 1994), Denmark, Norway and Sweden (Mellemvik and Monsen 1995), Germany (Lüder 1998), Italy (Mussari 1995), Poland (Jaruga, Nowak and Dixon 1995), New Zealand (Pallot 1996), Spain (Montesinos and Vela 1996 and 2000), several African countries (Godfrey et al. 1996; El-Batanoni and Jones 1996) and Australia, particularly New South Wales (Christensen 2001). Moreover, Lovell (1995) uses a variant of the model for explaining differences of structure, audit orientation and role of European Supreme Audit Institutions and Montesinos (2000) analyses the conduciveness of Spanish environmental conditions to external audit reform. Cross-country comparisons have been carried out by Budäus and Buchholtz (1996) covering British, Dutch, Finnish, German, New Zealand and U.S. local governments (one per country), by Godfrey, Devlin and Merrouche (1996) for Kenya, Tanzania and Uganda and by Vela and Fuertes (2000) who provide an overview of the conduciveness of environmental conditions to governmental accounting innovations on the basis of contingency model applications to 15 countries (Table 1).

Table 1. Contingency Model – Influence of Environmental Conditions on Governmental Accounting Innovations (Source: Vela/Fuertes 2000, p. 92)

Country	Stimuli	Social Vbles.	Political Vbles.	Admin. Vbles.	Implem Barriers	Overall Assesment
Germany	+	+	-	-	-	UNFAVORABLE
Canada	+	--	+	+	+	FAVORABLE
Switzerl.	+	+	+	-	-	FAVORABLE
Denmark	+	--	+	+	+	FAVORABLE
USA(Fed.)	+	+	+	+	-	FAVORABLE
USA (Sts.)	+	+	+	+	+	FAVORABLE
France	-	--	-	-	-	UNFAVORABLE
Italy	+	--	-	-	-	UNFAVORABLE
Japan	-	--	-	-	-	UNFAVORABLE
Kenya	-	+	-	-	-	UNFAVORABLE
New Zeal.	+	+	+	+	+	FAVORABLE
Poland	+	+	+	+	-	FAVORABLE
UK	+	--	-	-	+	UNFAVORABLE
Sweden	+	--	+	+	+	FAVORABLE
Tanzania	+	+	+	-	-	FAVORABLE
Uganda	-	+	-	-	-	UNFAVORABLE
Spain	+	--	+	+	+	FAVORABLE

2.4. Discussion of Critical Issues

Applications of the contingency model as well as theoretical reflections have revealed a number of perceived or actual weaknesses of the model referring to insufficient explanatory power, "black boxes", the notion of innovation and the role of fiscal stress. Before discussing these issues, it might be useful to reiterate the explanatory objective of the contingency model: It is exclusively aimed to permit an assessment of conduciveness of relevant environmental factors prevailing in a country to governmental accounting innovations. Its aim, however, is not to explain the whole reform process including all relevant factors.

The cross-country comparative studies carried out by Mellemvik and Monsen (1995) and Budäus and Buchholtz (1996) using the contingency model lead to the observation that changes of the accounting system diverge in spite of similar environmental conditions (Mellemvik and Monsen) and that technical differences in reform approaches could not completely be explained by differences in environmental conditions (Budäus and Buchholtz). Both results are not surprising and provide hints for further developments of the contingency model. If the model is to explain the whole innovation process and the selection of a specific reform approach, it has to include additional variables such as behavioural, attitudial and reform approach variables.

The introduction of reform approach variables and the identification of specific environmental configurations that are conducive to the implementation of specific reform concepts would of course improve the explanatory power of the contingency model. Since the introduction of an approach variable would require an unambiguous description of alternative reform approaches, it would necessarily have to fill in the black box "content" (Chan et al. 1996, p. 11). A first, but certainly insufficient attempt in this direction has been made by distinguishing an accountabilism-driven and a managerialism-driven reform approach (Lüder 1994, p. 10).

As the contingency model is aimed to assess the conduciveness of environmental factors to the implementation of governmental accounting innovations, the term "governmental accounting innovations" is central and has certainly to be clarified (Chan et al. 1996, p. 13). According to the organization literature "innovation is the successful bringing into use of an invention" (Khandwalla 1977, p. 555). "Invention is the act of creating something new and useful" (Khandwalla 1977, p. 551). It "may or may not originate in (the) organization" (Khandwalla 1977, p. 555). However, "innovation is not any new program or technology, but only those that involve the performance of new tasks or a significant alteration in the way in which existing tasks are performed" (Wilson 1989, p. 222). The definition of innovations for purposes of the contingency model as "conceptually not merely procedural changes of the accounting system to ensure the supply of comprehensive, reliable and meaningful financial information needed for appropriate financial accountability and sound financial management" (Lüder 1994, p. 1) certainly meets the criteria of the more general definition if (1) the traditional accounting system did not provide that information and (2) the information provided by the new system is useful. Information provided is useful if ensuring financial accountability and sound financial management are reasonable objectives to be pursued and the information provided is appropriate for achieving these objectives (this latter aspect is already contained in the definition). Such an innovation can also be called a reform.

"Often, the adoption of the accrual basis of accounting is taken as a measure of reform"(Chan et al. 1996, p. 14). This has been challenged by Monsen and Näsi (1997) on the grounds that "accrual accounting with its matching concept cannot generally be properly applied in governmental organisations ....Hence, the adoption of accrual accounting as the main accounting model.... does not represent a change for the better, and consequently it is no governmental accounting innovation" (Monsen and Näsi 1997, p 13). The statement of the second sentence on the basis of the first one is only conclusive if the private sector accounting matching principle is considered an indispensable element of accrual accounting, even if applied to public sector entities. But this of course is debatable. Whether accrual accounting in government means a change for the better or not seems to depend much more on a whole set of other factors such as the information needs, the features of the existing accounting system, the features of the accrual accounting system to be implemented, and the availability of human and physical resources to properly run the accrual system. Some confusion about innovation may be avoided, if a distinction is made between an innovative concept underlying an innovation process and the outcome of the process which can deviate from the concept and must not necessarily meet the requirements of an innovation.

Van Helden (2000, p. 83) has empirically tested what he calls the financial stress hypothesis ("financial stress as motive for the adoption of businesslike instruments in government") on the basis of eight Dutch municipalities and did not find it confirmed. This gives rise to a few more general remarks on the significance of single independent variables of the contingency model. (1) The lists of independent variables may be and presumably are incomplete. This is confirmed by several researchers' investigations and their demand for adoption of additional variables. (2) The significance of variables and thus their influence on the innovation process may differ and actually does differ. This means among other things that not necessarily all variables have to be present in every single innovation process. Significance of variables may also vary from country to country. (3) It is important to find out if the lists contain variables that have never been observed in any innovation process. These of course are candidates for deletion. Fiscal stress, however, does not belong to this set of variables in spite of van Helden's research results and for various reasons discussed by himself.

3. The Financial Management Reform Process Model (FMR Model)

3.1. The Model

The adoption of the above mentioned modifications and extensions as well as new ideas triggered by discussions and additional experience from a research visit to Australia led to a complete revision of the contingency model. The revised model called "Financial Management Reform Process Model" (FMR Model) still contains contextual variables characterizing the institutional arrangements of a country but it corrects "the emphasis of context over behaviour" (Chan et al. 1996, p. 11) of the contingency model and establishes a feed-back that ties behaviour and attitudes of key actors in the process to the process results and thus takes into account the possibility of a multi-stage reform process. It also aims to "shed some light into the process of generating governmental accounting innovations" (Chan et al. 1996, p. 12) by specifying the actors in the process .

The financial management reform process model (Lüder 2000, p. 3) consists of two clusters of contextual variables ("stimuli" and "institutional arrangements"), three clusters of behavioural variables ("reform drivers" "political reform promoters" and "stakeholders") and two clusters of instrumental variables ("reform concept" and "implementation strategy"). For links between the clusters refer to Appendix Fig. 5.

Stimuli: The stimuli remain by and large unchanged. Fiscal stress, however, has been replaced with "financial or economic crisis" which usually is an underlying factor of fiscal stress."Requirements derived from administrative reform" have been added to make clear that governmental accounting reform can well be embedded in administrative reform, and particularly in the case of developing countries, "endeavours to improve international reputation" are also supposed to be a relevant stimulus for governmental accounting reform.

Reform Drivers: These are recognized institutions and professionals in the reform field that promote the reform through advice, talks and publications aimed at making governmental accounting reform a political issue and influencing political decision makers in a specific way. They provide motives for the political actors to engage in the reform as well as conceptual ideas for the solution of the (actual or perceived) problems. Different reform drivers sharing views on the main features of the reform and thus form an epistemic community of experts can be assumed to strengthen the influence of the reform drivers on the reform process (Laughlin/Pallot 1998, p. 385). The reform drivers cluster is in essence a cluster of behavioural variables.

Political Reform Promoters: All administrative reforms need political reform promoters, i.e politicians who initiate a reform and have the power to enforce it. Those promoters are usually members of the government. Regarding governmental accounting reform, the minister of finance and the prime minister seem to play a key role. The role of the minister of finance (or more general of the "chief financial officer") is not only a political one but he is also the professional reform promoter in government. This means, that the ministry of finance is an or even the key player in shaping the reform concept seeking the advice of reform drivers. Less often are members of parliament political reform actors since this requires a strong parliament with the ability to enforce reforms even against the resistance of the executive. The political reform promoters cluster is again a cluster of behavioural variables.

Institutional Arrangements: This cluster contains the contextual (structural) variables of the contingency model, the societal as well as the political and administrative structural variables and even the implementation barriers. The categories are quite broad and of course need further specification for adequately describing the institutional arrangements of a country. Such specification is partly to be found in the contingency model literature. The following remarks are confined to a few additional explanations of the structural variables.

A broad classification of *Legal Systems* is into civil law and common law systems (Lüder 1992, p. 118). Linked to those systems are different types of governance, the Rechtsstaat model and the public interest model (Pollitt/Bouckaert 2000, p. 52). Under the Rechtsstaat model, the rule of law is the guiding principle for administrative action whereas under the public interest model the state "is regarded as something of a necessary evil" and "officials must constantly be held to public account" (Pollitt/Bouckaert 2000, p. 53). The less flexible Rechtsstaat model can be expected to be less conducive to reforms or at least slow down the reform process compared to the public interest model (Lüder 1992, p. 118; Pollitt/Bouckaert 2000, p. 53). But there are other features of the legal system that affect government accounting reform. They comprise the electoral system, and the flexibility of budget law.

The variable *State Structure* refers to such categories as "unitary/federal", "co-operative federalism/competitive federalism", "one chamber parliament/two chamber parliament" and the division of power between the electorate, the (executive branch of) government and the directly elected bodies and officials. The combination "unitary/one chamber" together with a more asymmetrical division of power in favour of the executive may be conducive to government-induced reforms. In contrast, inducing reforms by parliament or other state organs probably will be facilitated if the division of power is more balanced and elements of direct democracy play a significant role in the system (Lüder 1992, p. 116).

The *Administrative Structure* mainly refers to organizational characteristics (Lüder 1992, p. 117) of the administration and the division of power between organizational units such as "centralized/decentralized", "concentration/ fragmentation of financial management functions", "existence of central organizational units at the different administrative levels" that are able to promote the reform in their area and "formal power position of the heads of central units and the heads of line units". A decentralized structure with financial management functions concentrated in powerful central units should be particularly supportive to government accounting reform.

The qualification of *Civil Service* in general and of accountancy staff in particular are crucial factors for the mode, the duration and the cost of implementation of governmental accounting reform. A lack of certain general skills in the accounting field which cannot be eliminated in the short term may not only delay the implementation of the reform but it may also bring along an increased level of resistance that can even endanger reform success.

The national *Culture* (social, political, administrative) can be characterized by such categories as the general attitude towards risk and uncertainty ("risk-taking/risk-averse"), a prevailing inclination to "individualism/collectivism", the "degree of openness" of political and administrative processes and the "responsiveness" to the needs and demands of the general public. The combination risk-taking/individualistic/open/responsive is expected to create the most favourable reform climate.

Stakeholders: Stakeholders in the reform process are institutions or people positively or negatively affected by the reform that are neither reform drivers nor political reform promoters such as the general public, the parliament, the administration (primarily line departments and agencies) and the statistical offices. In the case that the audit institutions are not reform drivers, they also belong to the stakeholders in the reform process. Unlike the reform drivers' and the political reform promoters' views, the stakeholders' views of the reform may differ. Some of them may welcome the reform since they expect it to be in their interest. Others expecting rather negative effects, may oppose them. It is hypothesized that stakeholders' attitudes towards reform depend on the reform concept and the implementation strategy as well as on their chances to affect both and that these attitudes are susceptible to political reform promoters' influence. The ability of stakeholders to accelerate or delay the reform, to influence the implementation strategy and the outcome of the reform process differs according to their formal position in the reform process and their discretionary powers. Successful reform, therefore, requires the political reform promoters to lead opposing stakeholders, especially key stakeholders (those with strong formal position and considerable position powers), to take at least a neutral position.

Implementation Strategy: The mode of implementation of a reform (implementation strategy) of course matters and affects the probability of success or failure of a reform (Pallot 1996, p. 345) as well as deviations between the reform concept and the outcome of the reform. Features of the implementation strategy are authoritarian vs. participative, centrally guided or not, one- or multi-step, with or without pilot-testing, considerable vs. minimal user discretion, length of implementation period, with or without systematic staff training etc.

The outcome of the reform process - or a process stage if it is a multi-stage reform (what Jaruga and Nowak call "consequences in the real world", 1996, p. 30) - is then fed back to the behavioural variables. Depending on the size of a still existing gap between the outcome of the reform and the reform concept, the feed back either brings the process to an end or induces a subsequent reform loop with or without prior modification of the reform concept.

3.2. A Related Approach: The Pollitt/Bouckaert Model of Public Management Reform

In their recently published book ‚Public Management Reform – A Comparative Analysis", Pollitt and Bouckaert propose a model of public management reform (Pollitt/Bouckaert 2000, p. 24) that, even though not confined to financial management reform, bears a strong resemblance to the FMR model. Core of the Pollitt/Bouckaert model is the elite's perception of desirable and feasible (public management) reforms (see Appendix Fig. 6, boxes I,J). The elite usually consists of a political and an administrative elite group (Pollitt/Bouckaert 2000, pp. 31, 51) encompassing people that occupy power positions enabling them to decide on and launch reforms. In the FMR model, the ‚political reform promoters' assume this function. The elite's perceptions of desirability and feasibility of reform is affected by four clusters of variables: the socio-economic forces(A), chance events (K), the political system (E) and the administrative system (L) (see Appendix Fig. 6 for an overview of the model structure).

As socio-economic forces, the authors identify global economic forces such as globalisation of capital markets and socio-demographic change. These result in national socio-economic policies that again affect the elite's attitude towards public management reform. In case of financial management, the socio-economic variables can be assumed to create stimuli for reform: They may either trigger a fiscal/economic crisis or a public management reform that also requires financial management reform.

Chance events such as scandals, disasters or accidents may occasionally have a significant effect on reform (Pollitt/Bouckaert 2000, p. 33). This is a generalization of the stimulus "financial scandals" of the FMR model.

The political system is characterized by the rather dynamic variables "new management ideas", "pressure from citizens" and "party political ideas" and by rather static variables such as the state structure and the culture of governance ("Rechtsstaat" vs. public interest). In FMR model terminology, "new management ideas" would be a stimulus whereas citizen and party groups pressing for reform would be classified "reform drivers". The rather static variables on the other hand are part of the "institutional arrangements".

The administrative system again consists of rather dynamic and rather static elements. The dynamic elements "content of reform package", "implementation process" and "reforms actually achieved" refer to mode and result of the implementation process. They directly correspond to the variables "reform concept", "implementation strategy" and "outcome of the reform process" of the FMR model. The static elements such as the "nature of executive government" and the "relationships between ministers and top civil servants" are additional features of the institutional arrangements.

Despite all similarities, there are of course differences between the two models. Due to the differing subjects of reform that the models are intended to explain (public management in general and public financial management), and thus the differing relevance of the various variables in the reform processes, the focuses of the models consequently also differ. In addition to differences in the clustering of variables, in the Pollitt/Bouckaert model no distinction between political reform promoters, reform drivers and stakeholders with differing influence on the reform process is made, the existence of epistemic communities is at least not explicitly mentioned and the inclusion of very different types of variables in the same cluster, particularly the political system and the administrative system, may cause some ambiguity in applying the model and interpreting its results.

On the other hand, the degree of correspondence between the two independently developed models is amazing and this cannot least be taken as an indication for the empirical relevance of the financial management reform model.

4. CONCLUDING REMARKS AND FUTURE RESEARCH DIRECTIONS

Given the "infancy or at most adolescent development of CIGAR" (Chan 2000, p. 9), it is not at all surprising that the emphasis has been on descriptive country studies. The value of those studies, however, should not be underestimated since "powerful explanatory and predictive models.... (have to) build upon descriptive studies" (Chan 2000, p. 9). Moreover, since CIGAR is a multi-national network of scholars, the endeavours to describe national governmental accounting systems in a common language (English) have also contributed to terminological precision, a reduction of the language barrier and improved international understanding.

But there of course remain *desiderata* a few of which will be discussed here, based on four observations. They are (1) emphasis of "desk studies" over empirical studies, (2) emphasis of context over content, (3) emphasis of descriptive over explanatory contingency model applications, and (4) emphasis of soft over hard research.

Emphasis of desk studies over empirical studies: Empirical comparative governmental accounting research requires substantial funding which in most cases is not available and even national empirical governmental accounting research suffers from inadequate funding. Under these circumstances researchers have no choice but to draw on their personal knowledge and available written material. This results e.g. in a lack of studies on reform processes since academic researchers are only exceptionally involved in governmental accounting reform and strengthens their tendency to withdraw to criticising reform proposals and reform endeavours. What CIGAR therefore needs is funding for a (first) collaborative empirical transnational research project. If such a project is successfully carried out, it can be expected to provide a momentum for subsequent funding of comparative international governmental accounting research.

Emphasis of context over content: Chan et al. (1996, p. 11) observed an imbalance of studies concerned with the context of governmental accounting and its content. However, looking at more recent publications (e.g. Olson et al. 1998, Bac 2001), the focus seems to have shifted so that content issues are at least in addition to contextual aspects included in the studies. What is still not available is a common framework for describing a governmental accounting system in sufficient detail that would allow cross-country comparisons on the basis of individual country studies carried out by different researchers. The early approach of Lüder et al. (1990) for characterizing governmental accounting systems has not been picked up by others.

Emphasis of descriptive over explanatory contingency model applications: Most applications of the contingency model were aimed at describing a country's contextual situation in regard to its conduciveness to governmental accounting "innovations" in general and at identifying the primary favourable and unfavourable contextual variables. Moreover, Mark Christensen (2001) recently has submitted an empirical study of governmental accounting reform which is focused on behavioural variables.

A still open question is whether there are different contextual configurations with different conduciveness to different types of governmental accounting reform. Every attempt to answer this question would require typifying governmental accounting systems as a first step. Reform could then be defined as transition from one type of governmental accounting system (old or traditional system) to another type (new or improved system).

Such investigations into the relationships between contextual configurations and types of governmental accounting would not only enhance the explanatory power of the contingency and FMR models but also enable predictive statements as to the fit of context and (intended) reform.

Emphasis of soft over hard research: Comparative governmental accounting research so far is almost exclusively non-quantitative research. Statistical analyses of course would be desirable e.g. to find out differences in the significance of structural and behavioural variables for success or failure of governmental accounting reform. But it has to be cautioned against uncritical use of statistics resulting in trivial or empirically irrelevant findings. There are ample examples of this kind of quantitative "research" to be found in the accounting literature. Main pitfalls in applying statistics are insufficient sample size, insufficiently detailed description of empirical facts by variables, data-driven instead of problem-driven analysis and substitution of statistics for theory. The conclusion for future CIGAR activities would be to put the emphasis on theoretical and non-statistical empirical research for the time being and postpone formally sophisticated statistical analyses. This statement of 1991 (Lüder 1991, p. 14) is still valid.

In conclusion, the CIGAR community has achieved considerable progress over the last decade and the good news is that there are indications for collaborative research opportunities in the near future. Materializing of collaborative research would certainly mean a big leap forward for CIGAR as it would enable the network to address some of the above mentioned comparative governmental accounting issues that can only be resolved by international cooperative research.

APPENDIX

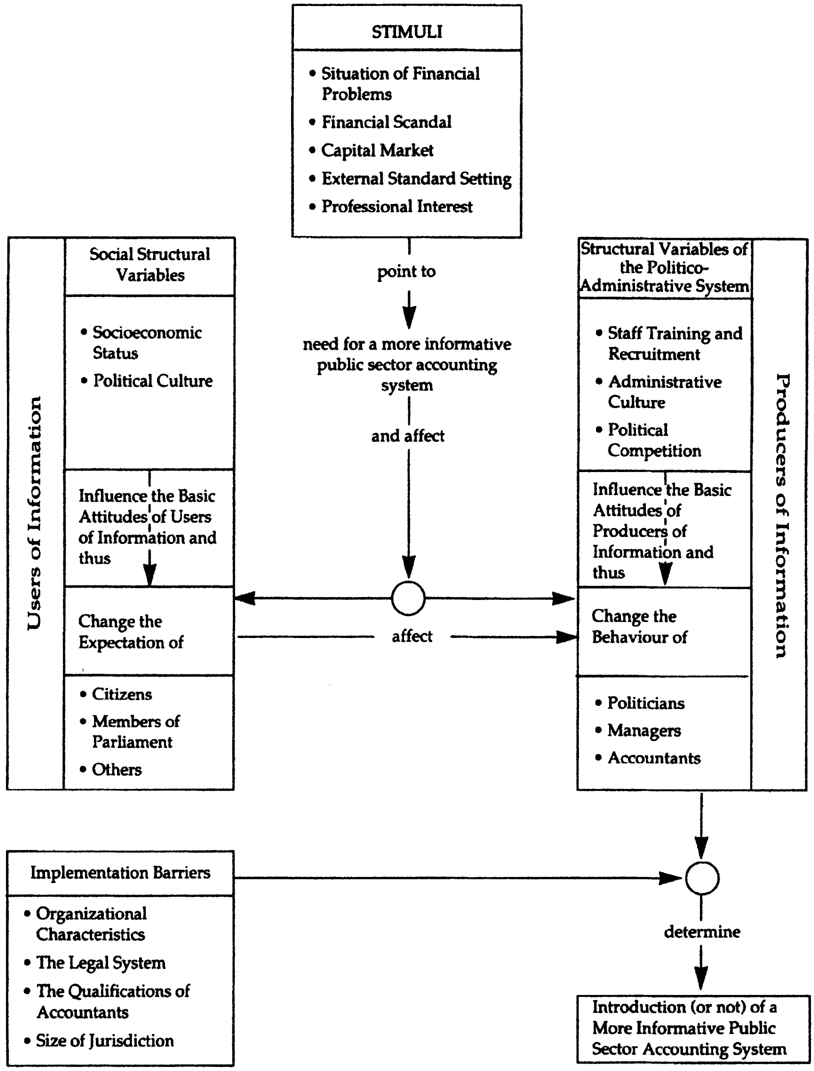

Figure 1: Contingency Model of Public Sector Accounting Innovations (Lüder 1992, p. 111)

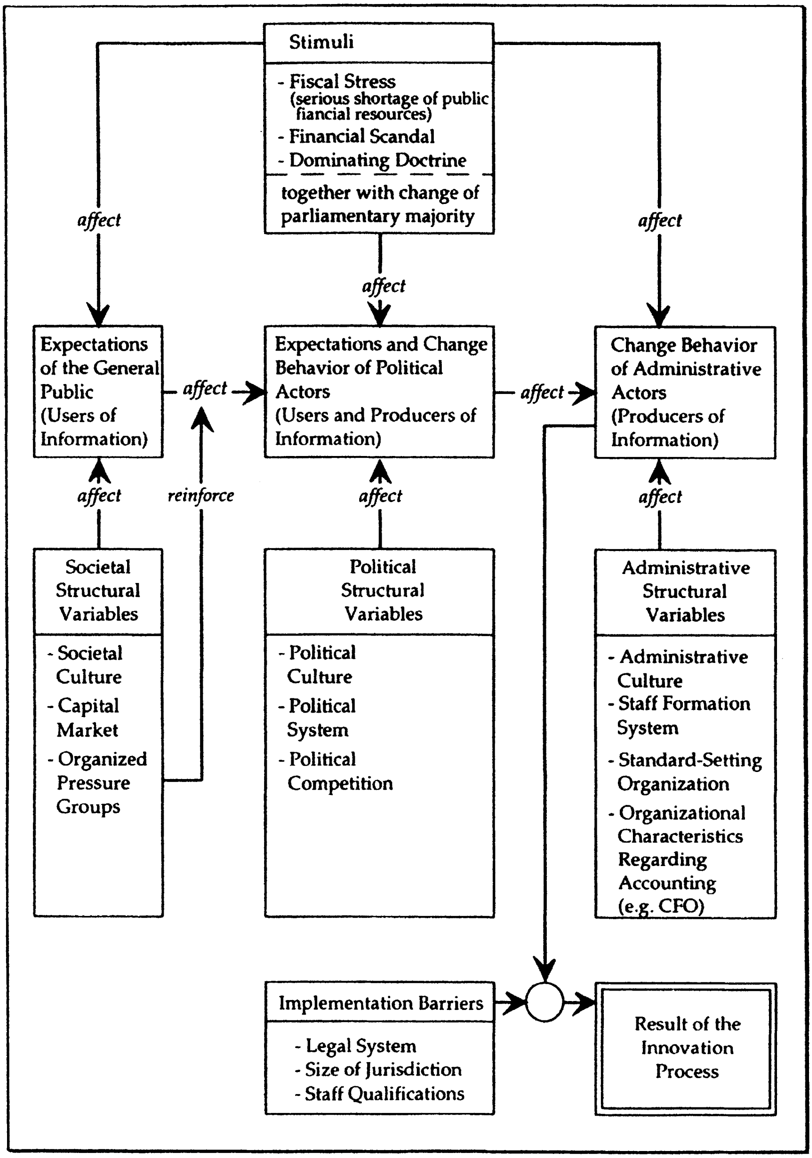

Figure 2: Modified Contingency Model of Public Sector Accounting innovations (Lüder 1994, p. 9)

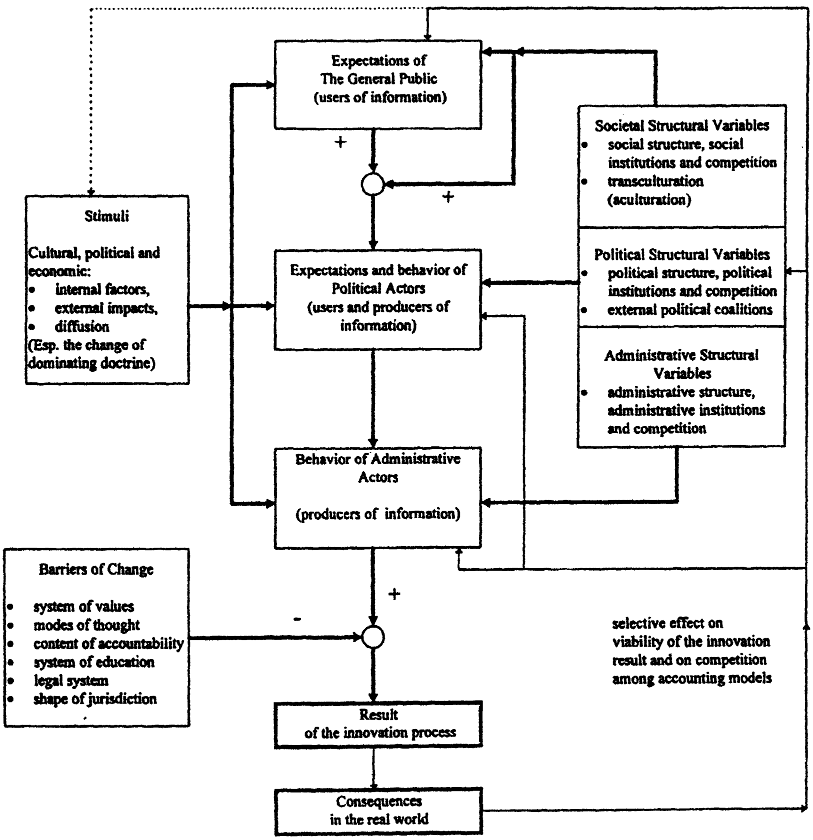

Figure 3: A General Model of Public Sector Accounting Innovations (Jaruga and Nowak 1996, p. 30)

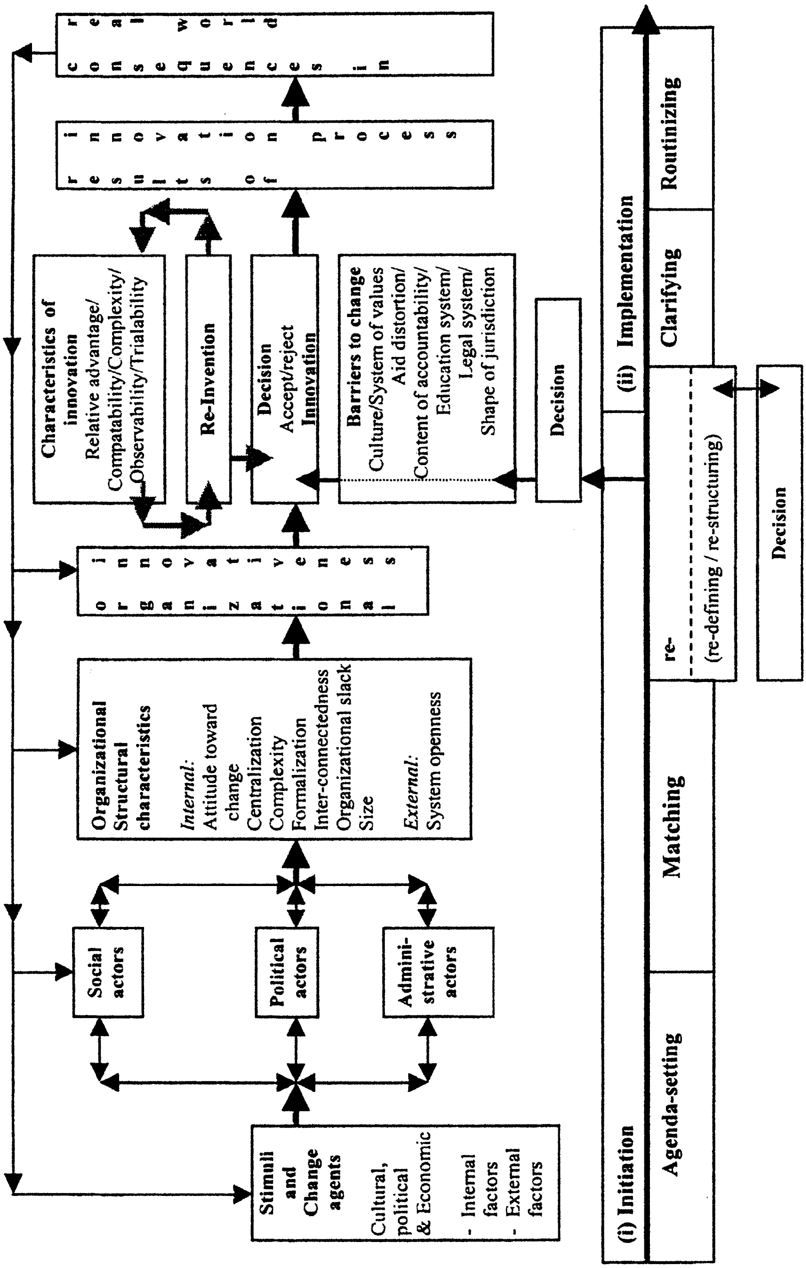

Figure 4: A Diffusion-Contingency Model for Government Accounting (Godfrey et al. 2001, p. 282)

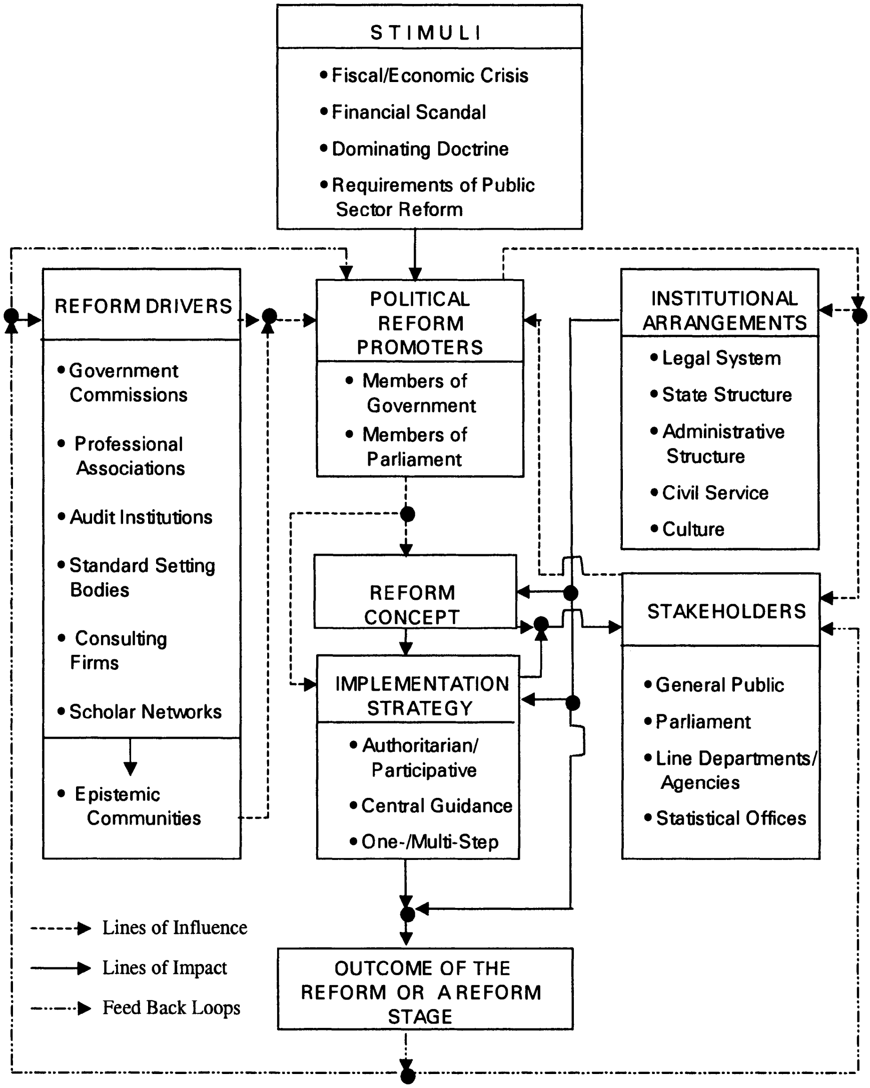

Figure 5: Financial Management Reform Process Model (FMR Model)

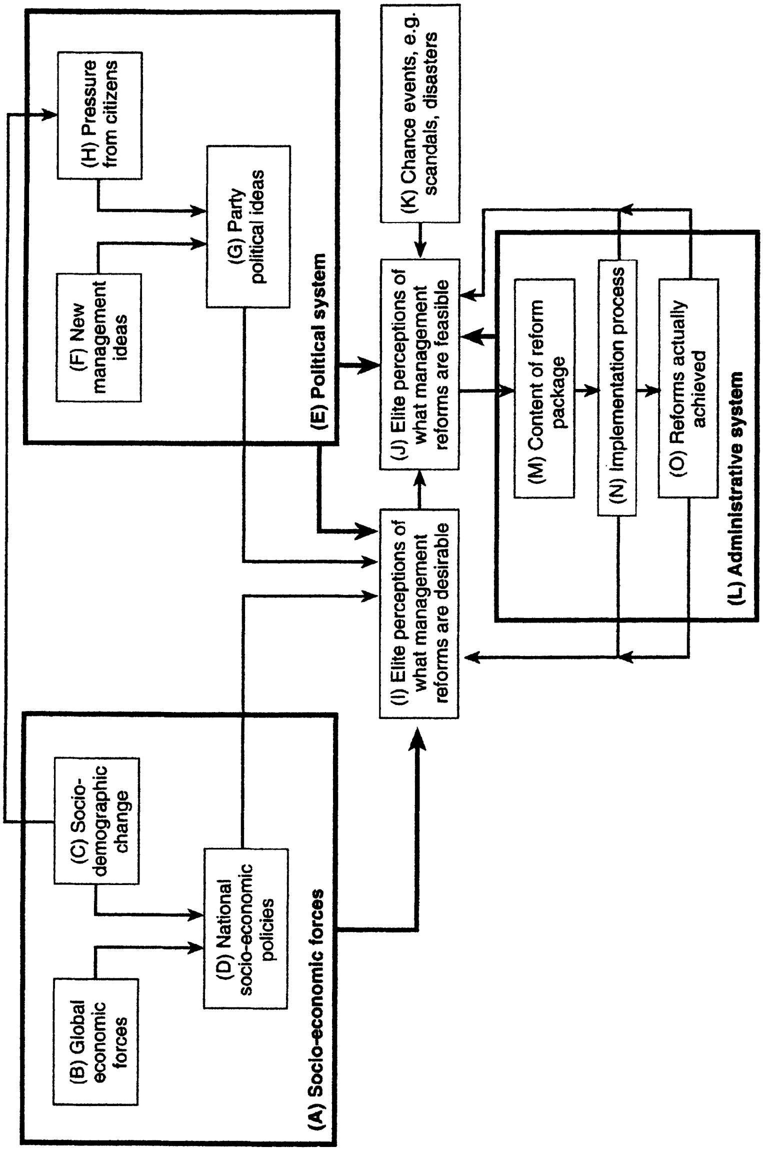

Figure 6: A Model of Public Management Reform
(Pollit/Bouckaert 2000, p. 26)

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JAMES L. CHAN

COMPARATIVE INTERNATIONAL GOVERNMENT ACCOUNTING RESEARCH (CIGAR) METHODOLOGY: ISSUES AND STRATEGIES

1. CIGAR: STATE OF THE ART

1.1 Accomplishments in Brief

The Lüder Contingency Model (Lüder, 1989, 1992, 1996) has served as the benchmark conceptual framework for comparative international government accounting research. The model seeks to explain why some countries have undertaken government accounting innovations while others have not. Lüder theorizes that those innovations are the result of complex interactions of contextual variables and behavioral variables that describe the users and suppliers of government financial information. For example, the general public may be influenced by interest groups (e.g. the accounting profession) and the capital markets, which serve as cost-reducing information intermediaries. Political culture (e.g. the norm of accountability) and political competition (e.g. between political parties or factions), along with occasional or frequent fiscal crises or scandals may affect the way political leaders view financial accountability. Similarly, the demand for administrative accountability and receptivity to private sector practices may influence the way the bureaucracy views the information it provides to the legislature and the public at large. In other words, societal, political and administrative structural variables are hypothesized to have significant effects on the expectations and behavior of those who demand and supply government financial information. When a particular configuration of these variables creates favorable conditions sufficient to overcome the implementation barriers, innovations are likely to occur.

The essence of the contingency theory is to explain the occurrence of government accounting innovations. The model has since been expanded and refined by Jaruga and Nowak (1996), by Godfrey, Devlin and Merrouche (1996). It has also been applied in different national contexts (e.g. Chan, 1994; Chan, 1995; Godfrey, Merrouche and Devlin, 1999).

The intellectual accomplishment of the CIGAR community is reflected in, besides individual journal articles, several edited proceedings of conferences (Chan and Jones, 1987; Buschor and Schedler, 1994; Montesinos and Vela, 1995;

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 23-29.

Caperchione and Mussari, 1999; Bac, 2001). In addition, Chan, Jones and Lüder edited a volume of Research in Governmental and Nonprofit Accounting in 1996.

1.2 Lüder's Critique

Lest complacency set in, at the conclusion of the 7th biennial CIGAR conference, Professor Lüder articulated what I have termed the Lüder critique (Lüder, 1999). The critique addressed several concerns. First, a majority of CIGAR studies were not explicitly comparative. Most papers were exploratory and did little more than describing current practices in various countries. Second, the selection of countries was usually not guided by theoretical considerations, but by individual access, knowledge and preferences. Differing in subjects, definitions and designs, their results were incomparable and could not form the basis for cross-country analysis. Third, the few cross-country studies were long on descriptions and short on a systematic analysis of international similarities and difference. Finally, there were few conceptual and explanatory studies.

On the basis of these specific criticisms, Lüder implored CIGAR scholars to conduct more studies like those in Column A in the table 1, and less of the studies identified in Column B.

Table 1

Column A	*Column B*
Conceptual and explanatory studies	Exploratory studies
Analytical exploratory studies	Descriptive exploratory studies
Multinational comparative studies	National studies
Systematic studies	Accidental studies
Common definitions and designs	Differences in definitions and designs
Collaborative research	Individual Research

2. METHODOLOGICAL ISSUES AND STRATEGIES

The transition from type "B" to type "A" research requires the resolution of a number of methodological issues and the use of different research strategies from those commonly used in CIGAR to date. The proliferation of the non-cumulative exploratory studies reflects the lack of a paradigm that states the discipline's agreed-upon aim and agenda, as well as the lack of consensus on key methodological issues. These issues may be framed in the form of the following rhetorical questions:

1) What are the proper units of analysis in CIGAR?
2) What are the critical variables to study?
3) How can the process of change be captured?
4) How does government accounting work?

These issues are briefly analyzed, along with the research strategies for dealing with them.

2.1. Proper Units of Analysis.

There are two sorts of issues here. Firstly, as the terms "international comparison" implies, the nation is the presumed unit of analysis. By definition, the task of CIGAR is to study how government accounting works in different nation-states. As such, little attention is paid to intra-national differences, or there is an implicit assumption that government accounting policies and practices are so similar within a nation that it is not necessary to inquire into those differences. This may be the case in unitary states, such as France and China, but it may not be case in countries with a federal system, such as the United States and Germany. This raises the possibility that some CIGAR studies might compare local governments in different nations; central governments might be similarly compared.

One interesting research area is "central-local relations." Here, we might hypothesize that the extent to which the central government's regulation or influence over local government accounting is a function of the "central-local relations." More specifically, the looser the relations, the more divergent central and local policies and practices are likely to be. Here "local" is a general term for sub-national governments, which may include regional, provincial (also American states, German Landers, and French departments), counties, municipalities/cities, towns and villages. The issue is that where there are significant intra-national differences, international comparisons should explicitly address those differences rather than simply assuming intra-national homogeneity.

The second "unit of analysis" issue pertains to what constitutes "government." Should we limit our research to the governmental bodies possessing legal authority in a geographical area, such a city, region or nation? Or should the scope of our inquiry include the entire public sector, namely all the activities and organizations created or financed by the nation-state or accountable to it? Again this issue has not been explicitly addressed in the CIGAR literature. But it is of fundamental importance because without a common understanding of the "accounting entity" or "reporting entity," it would be impossible to interpret government finance statistics. In addition, we may also miss the opportunity to study the effects of the different roles of government in the economy or society on government accounting. Specifically, we might hypothesize that the larger the public sector is relative to the whole economy, the less likely is government accounting to be similar to business accounting.

2.2. Critical Variables

The CIGAR literature has so far tended to stress "context" over "content" (Chan, Jones and Lüder, 1996). But content is important; it tells us about what a government accounting and reporting system does. For example, who supplies what financial information to whom? when? how? and to what ends? Answers to these questions in different national contexts would reveal the sources of the similarities and differences in the scope and function of accounting.

Specifically, we might hypothesize that the reporting characteristics of a government accounting system are influenced by user-orientation. User orientation may be managerial, legislative, or external. A managerially-oriented system would stress administrative control in the form of interim reporting of budget execution. A legislatively-oriented system would emphasize annual reporting to parliament for the discharge of government accountability. An externally-oriented system would pay more attention to the government's ability to service debt and sustain the delivery of services, which are the interest of creditors and the general public.

Given the crucial role of the budget in government, another way of characterizing government accounting is to formulate "models of government accounting" in terms of their divergence from the traditional – i.e. one-period, control-oriented - budget. In one model, government accounting could be dominated by the budget (as in the case of Germany, France and perhaps many Continental-European countries), In another model, government accounting is more or less co-equal with the budget (as in the United States). In the third model, accounting concepts actually influence the budget rather than the other way around (as in Australia, New Zealand, and increasingly so in the United Kingdom).

Since the traditional budget tends to focus on one period and is control-oriented, the greater the departure from such a budgeting system, the more a government accounting assumes a longer-term and a holistic perspective, as evidenced by the accrual basis and consolidated reporting. In other words, after accumulating a substantial number of narrative descriptive country studies, the next step is for CIGAR studies to selectively focus on salient features of government accounting, such as user-orientation and departure from the traditional budge, for further inquiry.

2.3 Modeling Dynamic Processes.

In addition to the academic scientific interest of knowing how nations and governments differ in their accounting, CIGAR also seeks to understand how innovations occur. In an earlier article (Chan, Jones and Lüder, 1996), we voiced the need to open the "black box" of government accounting changes. One possible strategy for understanding such changes is to identify external and internal influences. There exists some preliminary evidence that foreign-aid donor organizations and nations have played a role in promoting government accounting reform in developing nations (e.g. Godrey, Devlin and Merrouche, 1996). As is widely reported in the CIGAR and New Public Management literatures, the New Zealand model has exerted considerable intellectual influence on other nations in terms of framing the reform agenda of introducing the accrual basis and consolidated reporting. More recently, the IFAC Public Sector Committee's International Public Sector Accounting Standards (IPSAS) have generated a great deal of interest and discussions at least in academic and professional conferences. All of these indications point to external stimuli as a potentially important driver of government accounting reform.

However, with the exceptions of the countries that are the originators or promoters of government accounting reform, much less is known about the internal processes of government decision-making in the presence of such external stimuli. Such processes might be bottom-up in the sense of starting with experimentation by local governments, as is the case of the Federal Republic of Germany (Lüder, 1998). To some extent, that is the case with the United States, though the Federal Government has made more radical changes within a decade than local governments over a much longer period of time (Chan, 2001). Furthermore in the U.S. these policy changes were accompanied through reforming the standard-setting institutions by creating more powerful boards independent of the government, which has not taken place in Germany. In other national contexts, such as unitary states (e.g. China), one would predict the process to be a top-down one, in which the national Ministry of Finance sets government accounting policies for all levels of government. The general point is that we need carefully documented case studies covering a long -period of time to know whether and how governments change their accounting systems.

2.4. Positive Research

From its inception, CIGAR has had a normative tendency, believing, for example, in "a more informative public sector accounting" (Lüder, 1992). There seems to be a largely unexamined premise, that the accrual basis is superior to the cash basis, that whole-of-government reporting is better than fund-based reporting. An implicit goal of CIGAR is therefore to encourage the adoption of such a government accounting model. This kind of research may be termed normative research. In contrast, positive research seeks to answer the question "what is" and not "what ought to be." For example, if a government currently uses the cash basis of accounting, one would want to find out the reasons why it does that, rather than rushing to replace with it with the accrual basis of accounting. As in corporate accounting (Watts, 1992), one might study government accounting policy choices as products of political and market processes. Following the public choice view of human nature, one would assume that participants in these processes – e.g. public officials no less than managers – are motivated by self-interest. This line of inquiry therefore leads one to look at the incentive system that is conducive for certain type of behavior. For instance, politicians who have to compete in frequent elections can hardly be blamed for having short-term planning horizons. Nor should they be condemned for emphasizing short-term benefits or deferring costs to the future. In doing so, they are responding to the incentives provided by rules of the game in the political system. To the extent that government accounting is, as other types of accounting (Hopwood and Miller, 1994) are, viewed as a social and institutional practice, it can be understood as the product of rational calculations of costs and benefits by self-interested individuals who are its stakeholders.

The positive approach to CIGAR would be particularly timely in view of the strong advocacy for the global adoption of IFAC's IPSAS. It would supply policy makers and their advisors with factual information about the type of government accounting that is compatible with the political and governmental system in place. It would help us predict the acceptance or rejection of policy proposals such IPSAS. As stated in the previous section, we know relatively little about the internal processes that lead to the acceptance, modification or downright rejection of government policy proposals. What is needed is a robust positive theory could explain or, better still, predict the survival of new ideas in a particular environment.

3. CONCLUDING REMARKS

Further progress in comparative international government accounting research (CIGAR) requires resolution of several methodological issues. (1) The nation-state may not the appropriate unit of analysis when there exists significant differences between the national government and sub-national governments. Other alternatives include clusters of governments of similar political and economic characteristics. (2) Variable-oriented research can better reveal relationship between government accounting and its environment than case studies do. Narrative descriptions of country practices should lead to the specification of models of government accounting. (3) Dynamic models are needed to document the process of reform, especially the internal processes of government. (4) Positive research is needed to understand the incentives in the political system and government in order to explain and predict the acceptance of policy proposals.

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PATRICK J. DEVLIN
ALAN D. GODFREY
CHERIF MERROUCHE

THE IMPACT OF CULTURE ON GOVERNMENTAL ACCOUNTING INNOVATIONS IN DEVELOPING COUNTRIES

The Contingency Model Culturally Revisited

1. ENVIRONMENTAL DETERMINISTIC STUDIES

Early attempts to study accounting internationally resulted in countries being classified according to the factors that influence the nature and practice of accounting, with the focus of study being mainly on countries in the developed Western world.

Studies adopting a deductive approach distinguished between macroeconomic and microeconomic systems. In order to achieve the initial classification, a judgmental basis for analysing a country's group membership was adopted. Studies adopting an inductive approach were based on a statistical analysis of reporting practices in a sample of countries. These revealed that a clear distinction exists in most countries between measurement and disclosure practices (Fechner and Kilgore 1994).

A significant outcome of both the deductive and inductive approaches to understanding accounting differences internationally was the acknowledgement of the importance of environmental factors. This in turn led to serious attempts to identify both the relevant environmental factors and the manner by which such factors influence accounting (Perera, 1989). At the same time, classification studies were criticised for concerning themselves with predominantly economic factors, and for largely neglecting the influence of culture in shaping a country's accounting system.

2. CULTURAL DETERMINISTIC STUDIES

2.1. Early Cultural Deterministic Studies

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 31-42.

Hofstede's (1984) study – considered by many to be a landmark in the study of culture – used factor analysis and categorised countries into culture clusters based on four value dimensions: power distance; uncertainty avoidance; individualism; masculinity.

Building on Hofstede's work, Gray (1988) identified four distinguishable value dimensions of the accounting subculture which are related to societal values: professionalism versus statutory control; uniformity versus flexibility; conservatism versus optimism; secrecy versus transparency.

Hofstede (1984) defined culture as the collective programming of the mind which distinguishes the members of one human group from another, and stressed the fact that culture is learned rather than being inherited. Culture defined in this way includes the beliefs, values and traditions which are shared in a specific society at a specific time.

As Section 4 indicates, the term culture has a number of meanings. Moreover, it is often applied when referring to societies and/or ethnic groups and/or regional groups, but it is used also when referring to an organisation and/or a profession and/or a family. Thus, for some, religion, education, norms, customs and history are essential components of a society's culture (Ralston, Holt, Terpstra and Kai-Cheng, 1997).

2.2. More Recent Cultural Deterministic Studies

Following Hofstede's and Gray's studies, the relationship between culture and accounting was the subject of much debate in the late 1980s and the 1990s (Perera, 1989; Belkaoui and Picur, 1991; Hamid, Craig and Clarke, 1993; Fechner and Kilgore, 1994; Doupnik and Salter, 1995; Baydoun and Willett 1995, 2000; Harrison and McKinnon, 1999).

Perera (1989) combined Hofstede's and Gray's studies and proposed six hypotheses as to the relationship between cultural values and accounting values. He argued that there is a lack of consensus on what represents proper accounting methods because their purpose is cultural not technical. Referring to attempts to export accounting skills to developing countries, he suggested that skills transferred from Anglo-American countries might not work because they are culturally irrelevant or dysfunctional in the receiving countries' context. Starting from the proposition that accounting is culturally determined, critics of such transfers have argued that the act of importing foreign accounting systems is both irrelevant and inappropriate. As Harrison and McKinnon (1999, p. 485) describe it, based on such criticisms

> Advocates of cross-cultural research in the 1980s were calling for an 'unbundling' of the cultural variable into is sub-components, which could then provide the basis for theoretical explanations of relations between culture and other variables of concern.

Baydoun and Willett (1995) sought to examine the cultural relevance of Western accounting (specifically, the French Uniform Accounting System) to Lebanon.

While they found some use for the Hofstede-Gray framework, their difficulty was in not already possessing a definition of cultural relevance. They concluded (p.88) that

> In the absence of an independent definition there is a danger that testing hypotheses relating cultural values to accounting characteristics will degenerate into circular reasoning.

Hamid *et al.* (1993) assert that religion is admissible as a cultural factor, but note that its influence upon the development of accounting and business structures has not been explored in depth. They suggest that, unlike the nationally driven cultural elements that have dominated prior discussions of the impact of culture on accounting, religions such as Islam impose a code of ethics upon their followers transcending national boundaries. They conclude (p.147) that

> The potential influence of Islam on accounting policies and practices could inject analyses of national accounting difference with a cultural dimension more profound than that emanating from the impact of indigenous secular laws, general custom and commercial habit.

More recently, Baydoun and Willett (2000) argued that the presence of the Islamic religion as a cultural variable affects the way certain accounting measures are interpreted and the manner in which accounting information should be disclosed. As a result, they suggest a modification of the form of conventional Western financial statements to better serve the needs of users wishing to act in accordance with the Islamic code.

3. CRITICISMS OF CULTURAL DETERMINISM

In their review of cross-cultural research in management control systems, Harrison and McKinnon (1999) highlighted the almost exclusive focus in the literature on Hofstede's work. They identified three weaknesses in such studies. First, there is a failure to consider the totality of the cultural domain in the theoretical frameworks used by researchers. Second, there is a tendency to explicitly ignore the differential intensity of cultural norms and values across cultures. Third, there is an inclination to treat culture in a simplistic manner. Harrison and McKinnon (1999) also identified what they describe as a limitation of such studies, namely the excessive reliance on the value dimensional conceptualisation of culture. Baydoun and Willett (1995) questioned the extent to which Hofstede's concepts are applicable to the analysis of more specific social groups which may have significantly distinct sub-cultural characteristics, some of which may run counter to the apparent national values.

Similarly, Gray's (1988) study is perceived to suffer from the absence of an independent definition of cultural relevance. Furthermore, Boczko (2000) argued that, although Gray's classification study promised to depart from the predominantly institutionalist nature of previous classification studies, in the event it simply extended a relationship between the cultural environment and contemporary accounting earlier hypothesised in earlier studies.

4. THE MEANING (S) OF CULTURE

It appears taken as read that there is a relationship between culture and accounting – despite the fact that the accounting literature fails to acknowledge culture's complexity. Various perspectives on culture exist. But the accounting literature gives this impression that, in exploring the relation between culture and accounting, only one approach is appropriate: a value-dimensional approach to conceptualising culture emanating from the cross-cultural psychology literature.

Even the term itself has a diverse range of meanings. Williams (1983, p.87) suggested that culture is "one of the two or three most complicated words in the English language". Williams' writings indicate the complex history and diversity of meanings of the term 'culture'. In *Culture and Society* (1963), he argued that culture developed in response to industrialism. In *The Long Revolution* (1965), he identified the democratic potential of culture. His later writings adopted an explicitly Marxist orientation and founded what has been termed 'cultural materialism'.

Williams (1965) argued that culture could be defined in 'social' terms. His suggestion that culture is "a description of a particular way of life" (1965, p.57) was considered groundbreaking because it provided a perspective and approach for the emerging discipline of cultural studies. It is important to recognise, however, that Williams sought to stress the complexity of culture. Notwithstanding that it may be difficult in practice, it was important to "try to see the process as a whole", to relate cultural studies to "the actual and complex organisation" (1965, p.60). The result of this analysis is a description of the study of culture that is richer and more complex than anything to be found in the accounting literature:

> I would then define the theory of culture as the study of relationships between elements in a whole way of life. The analysis of culture is the attempt to discover the nature of the organisation which is the complex of these relationships. Analysis of particular works or institutions is, in this context, analysis of their essential kind of organisation, the relationships which works or institutions embody as parts of the organisation as a whole (1965, p.63).

Thus, Williams emphasised the concept of social totality. Understanding came from grasping both the whole social process and the interaction of different elements within this totality. Under this approach, economic, social and cultural forms are related. An approach where cultural practices need to be examined in terms of their interaction with other aspects of the social process is far removed from the conventional accounting approach based on assigning values to various dimensions of culture.

5. CULTURAL MATERIALISM

In his later work, Williams revisited the notion of totality from a more explicitly Marxist perspective. While rejecting a crude base-superstructure model, he was keen *not* to withdraw "from the claim that there is any process of determination" (1980, p.36). He argued that if 'totality' is simply taken to mean that there is a large variety of miscellaneous practices then the result is a concept "essentially empty of any content that could be called Marxist" (1980, p.36). For this reason, he concluded that the notion of totality could be used only if it was combined with the concept of 'hegemony'. When the two concepts are combined in this way, there is an emphasis on domination that is missing if totality is considered on its own.

5.1. A Tripartite Cultural Arrangement

The concept of hegemony is used to explain how a social group organises its rule through consent. It is concerned with how the legitimacy of leadership is established, with how shared ideas, beliefs, values and meanings are developed. Williams (1980) emphasised that any hegemony, however, is never total: it is only ever 'dominant'. As Anderson (1998, p.64) notes, any hegemony inevitably defines reality in a selective manner thus "virtually ensuring...the coexistence of 'residual' and 'emergent' forms resistant to it." In other words, any given social formation can be considered as comprising three cultural elements: dominant, residual and emergent. Moreover, because of the uneasy relationship of these elements, that social formation will exhibit a constantly shifting equilibrium.

5.1.1. An Effective and Dominant Culture

In discussing the contradictory mix of cultural forces, Williams (1980, p.38) argued that there is "a central system of practical meanings and values, which we can properly call dominant and effective." These meanings and values are not merely abstract but are "organised and lived". They constitute for Williams his notion of hegemony.

Moreover, for Williams, this system he was seeking to analyse was never static. Thus, in order to understand any effective and dominant culture, it was necessary to understand "the real social process on which it depends" – a process which Williams termed "incorporation" (1980, p.39). Williams highlighted the importance of "selectivity" to the continuance of an effective dominant culture. Here, he was referring to the way in which a dominant culture always portrays itself as "*the* tradition", as "*the* significant past". Thus, from a whole possible area of past and present, "certain meanings and practices are chosen for emphasis", while "certain other meanings and practices are neglected and excluded" (1980, p.39).

5.1.2. Residual Culture

In contrast, Williams defined 'residual culture' as "some experiences, meanings and values, which cannot be verified or cannot be expressed in terms of the dominant culture, [but] are nevertheless lived and practised on the basis of the residue - cultural as well as social - of some previous social formation" (1980, p.40). Here, the residual culture is seen as "usually at some distance from the effective dominant culture". Of course, at times the effective dominant culture will attempt to encapsulate ('incorporate') some practices of the residual culture within its domain so as to reduce any potential threat to its continuing supremacy. Nevertheless, "certain genuinely residual meanings and practices in some important cases survive" (1980, p.41).

5.1.3. Emergent Culture

An 'emergent culture' is described by Williams as the result of the process where "new meanings and values, new practices, new significances and experiences, are continually being created" (1980, p.41). Since it emerges from within the dominant culture, an emergent culture is part of effective contemporary practice. At the same time, because it is just that – emergent – it is not yet a defined part of effective contemporary practice. As a result, there is a much earlier attempt to incorporate an emergent culture – as Williams (1980, p.41) pointed out, it is significant "how alert the dominant culture now is to anything that can be seen as emergent".

5.1.4. Alternative and Oppositional Forms

In discussing this tripartite social formation, Williams (1980) introduced a further complexity. He drew a distinction between cultural practices which are "alternative" to the effective dominant culture and those which are "oppositional" to that culture. As a result, it is not merely the case that there is a "temporal relationship" between a dominant culture and (on the one hand) a residual culture and (on the other) an emergent culture. It goes deeper than that. An understanding of this relationship requires accurate differentiation between incorporated and non-incorporated forms of both residual and emergent practices.

Thus, the result of Williams analysis is a theoretical model of culture far removed from the simplistic approach adopted in most of the accounting literature. In this model, a social formation will comprise an array of cultural practices, experiences, meanings and values. It will comprise a dominant culture, a residual-incorporated and residual-not-incorporated culture, an emergent-incorporated and emergent-not-incorporated culture. Moreover, each of these elements will be in a constant state of flux. A major cause of this flux will be that a dominant culture cannot allow too much of the oppositional (the not incorporated) practices to survive – the risk to that dominant culture is too great. As Williams (1980, p.41) described it, "it is an important fact about any particular society, how far it reaches into the whole range of human practices and experiences in an attempt at incorporation".

6. CULTURE AND THE LÜDER CONTINGENCY MODEL

The dominant theoretical paradigm used by comparative international government accounting research (CIGAR) scholars has been Lüder's (1992, 1994) Contingency Model. This model itself has been the subject of research by CIGAR scholars and has evolved over a number of years (Chan, Jones and Lüder, 1996). It has been modified and applied to studies of the process of governmental accounting innovation in less developed countries (Godfrey, Devlin and Merrouche, 1996, 1999). It has been integrated with Rogers' (1996) Theory of Diffusion and used to study governmental accounting innovation in a transitional economy (Godfrey *et al.*, 2000).

Chan *et al.* (1996) identify several evolving models of the Lüder Contingency Model. Model 1B (Lüder, 1992) introduced variables such as socio-economic status, political culture, political competition and administrative culture. Model 2A (Lüder, 1994) identified societal culture and the concept of dominant doctrine together with changes in parliamentary majority. Model 2B (Godfrey *et al.*, 1996) added, in the context of developing countries, demand for political participation and regional culture as additional factors within the model. Finally, model 3A (Jaruga and Nowak, 1996) identified transculturation (acculturation) as societal structural variables, and systems of values and modes of thought as barriers of change.

Within the models there is little explanation of cultural variables. Williams' writings provide the tools to explore further such issues. His identification of the inherent tension within the dominant hegemony and the constantly shifting equilibrium amongst the three elements of social formation provides a rich source of insight into the social fabric within which potential innovations of governmental accounting take place. In so doing, it allows an unpacking of the social, political and administrative cultural variables of the Lüder Contingency model.

7. TOWARDS A BETTER UNDERSTANDING OF CULTURE IN DEVELOPING COUNTRIES: EAST AFRICAN CASE STUDIES

Table 1 maps changes over time of Williams' three cultural elements to highlight inherent tensions within the continually shifting cultural equilibrium. In these countries the effective dominant culture is heavily influenced by a history of colonial domination. Africa was a continent of tribal kingdoms. Such kingdoms were torn asunder and imported colonial cultures were imposed on the newly created 'countries' of the continent. During the period of early colonial dominance, a strong residual tribal culture continued to exist; at the same time a subjugated emergent tribal culture emerged. In terms of Williams' analysis, the residual tribal culture remained very strong, but in attempting to capture what was seen as 'oppositional', the dominant culture sought to use the tribal authority of village elders as agents of the colonial power. Later in the colonial period, the emergent culture moved to one of emerging nationalism. At independence, the countries of East Africa exhibited a dominant nationalist culture. The early post-independence period, with tensions growing between the new nationalist dominant culture and the continuing strong residual tribal culture, saw the emergence of a tribal-dominant national culture. In this case, it is possible that this emergent culture represented a learned response to realities of the former colonial-dominant national culture.

In contrast, the history of Uganda since 1986 has been built on a policy of non-tribal development where the central plank of the political system (no-partyism) seeks to replace divisive groupings with an all-embracing movement designed to guide Ugandans towards eventual full democracy (Financial Times 12 March 2001, p.7). The 'no-party' system of government effectively tolerates only one political organisation. It is likely that this has driven tribalism back into the residual culture domain, where tribal authority and loyalties are not considered part of the dominant culture and are viewed as 'alternative'. It is equally likely that emergent groups are gathering under the tribal-dominant national banner to challenge and to act as 'oppositional' to the existing dominant culture.

Table 1. Dominant, Residual and Emergent Cultures in East Africa

Period	*Residual Culture*	*Dominant Culture*	*Emergent Culture*
Uganda, Kenya, Tanzania:			
Pre-Colonial	Tribal	Tribal	Tribal
Early-Colonial	Tribal	Imported/ Imposed Colonial	Subjugated Tribal
Late-Colonial	Tribal	Imposed Colonial	Emerging National
Independence	Tribal	National	Tribal-dominant/ National
Post-independence	Tribal	Tribal-dominant/ National	Alternative Tribal-dominant
Uganda:			
Post-independence			
> Pre-1986	Tribal	Tribal-dominant/ National	National ('No-Partyism')
> Post-1986	Tribal	'No Partyism'	Tribal-dominant/ National

8. CONCLUSIONS AND DIRECTIONS FOR FUTURE RESEARCH

Williams' insights, particularly the tripartite cultural arrangement with its constantly shifting equilibrium, provide a powerful analytical tool and suggest a range of potential directions for future research.

8.1 Culture in North West Africa versus East Africa

Table 2 maps changes over time of Williams' three cultural elements to highlight inherent tensions within the continually shifting cultural equilibrium in the countries of North West Africa.

Table 2. Dominant, Residual and Emergent Cultures in North Africa

Period	*Residual Culture*	*Dominant Culture*	*Emergent Culture*
Algeria, Morocco, Tunisia:			
Pre-Colonial	Religious	National	National self consciousness
Colonial	Religious	National	Resistance Culture
Morocco, Tunisia:			
Independence	Religious (anti-colonial)	National	National
Post-Independence	Religious	National	Resistance Culture
Algeria:			
Independence	Religious	National	Strong National
Post-Independence			
> 1965-1988	Religious	Strong National	Resistance Culture
> Post-1988	Religious	Hybrid	Religious intolerant

8.2 Culture in Transitional Economies

Table 3 maps the cultural tensions within the transitional economies of Central and Eastern Europe. Here, similar to the situations pertaining in East and North Africa, the dominant culture has changed from a colonial-dominance to a national dominance. However, the present situation in the majority of transitional economies appears to be one of vacillation between national/democratic and national/reformed socialist or ethnic dominant cultures - with little or no 'capture' between these two extremes.

Table 3. Dominant, Residual and Emergent Cultures in Balkan Transitional Economies

Period	*Residual Culture*	*Dominant Culture*	*Emergent Culture*
Albania			
Pre 20th Century	Tribal/Ethnic	Colonial (Ottoman)	Subjugated Ethnic
Pre World War 2	Ethnic	National	Ethnic/National
Post World War 2	Ethnic	Colonial (Soviet Union)	Emerging National Democratic
Post-1990	Ethnic	National Democratic	National/Reformed Socialist or Ethnic-dominant
	← Alternating dominance →		

8.3. Differing Dynamics in Developing Countries

Developing countries may exhibit differing dynamics in the constantly shifting equilibrium among dominant, residual and emergent cultures. It may be the case, for example, that the dominant culture may be less tolerant of emergent and residual cultures than is the case in developed countries. Such movements may be seen as 'oppositional' in every sense, rather than 'alternative', and therefore must be 'captured'.

8.4. Differing Impact of Modes of Incorporation in Developing Countries

The impact of the modes of incorporation may be different in developing countries. Williams identifies educational institutions as the main agencies of transmission of the dominant culture. In many developing countries, particularly in Africa, there is an abject lack of basic education and high levels of illiteracy. This may engender a much stronger allegiance to tribal rather than the dominant culture for the majority of the population, with only the elite and privileged benefiting from a full educational experience and thereby dominating society. Similarly, a common feature apparent both in Africa and many of the European transitional economies is the cultural importance of 'the extended family'. The developed economies of the West have long dispensed with the need for the extended family, with the welfare state taking responsibility. It may be the case that in developing countries, including transitional economies, the extended family represents a significant part of the residual culture, which in turn is captured as part of the dominant culture.

8.5. Micro (Organisational Culture) Analysis

Williams' analyses can be applied equally to culture at the micro, or organisational level, with organisational innovativeness subject to the interplay operating amongst the dominant, residual and emergent cultures within the organisation. Constantly changing equilibrium and disequilibrium creates tensions within organisations, which may encourage, or discourage, innovation of accounting systems – including governmental accounting systems.

The foregoing provides further analytical tools for use with the Lüder Contingency Model in providing clearer insights into the potential for innovation in governmental accounting systems. Further, it suggests a number of directions for further research.

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WOJCIECH A. NOWAK

ON A BASIS FOR INTERNATIONAL COMPARISONS OF GOVERNMENTAL ACCOUNTING SYSTEMS: MODELS OF AN ECONOMIC ENTITY

1. INTRODUCTION

In the 1990s the research work carried out by persons engaged in the CIGAR initiative were largely focused on change in governmental accounting. This issue was analysed with respect to a model of change, measurement of the elements of accounting systems, and the structures of governmental financial reporting. Relatively little attention was devoted to the question of the nature, structure and function of the governmental sector reporting entity. These aspects were clearly regarded as self-evident. However, it seems that it is the nature, structure, function and social relations of governmental reporting entities that largely determine their accounting and reporting systems. Therefore definition of the nature, structure, functions and social relations of this type of entities ought to become a starting point in comparative studies on governmental systems of accounting and reporting.

The hypotheses put forward for subsequent considerations include the following statements:

1) A reporting entity of the governmental sector is an organisation viewed as a collection of persons and capital seeking attainment of a goal set by the creator of this collection.
2) Financial statements must represent fundamental attributes of an organisation and its elements.
3) Financial information conveyed by an organisation to its environment is determined by the state of social and political relations between the creator of a given organisation and its environment.

2. REPORTING ENTITY AND CLASSES OF ACCOUNTING INFORAMTION IN THE CONTEXT OF THE CONCEPTUAL FRAMEWORK OF GOVERNMENTAL ACCOUNTING

The importance of the issue of the reporting entity for shaping accounting and reporting is confirmed by the fact that it is included in conceptual frameworks of governmental accounting, which constitute a basis for its regulation. The treatment of the reporting entity in such conceptual foundations will be presented on the example of the conceptual framework of accounting regulation in New Zealand, the

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 43-59.

framework for the federal sector accounting regulation in the United States, and fundamental concepts set out in International Public Sector Accounting Standards. The choice of these three conceptual frameworks is not accidental – they can be regarded as milestones in the evolution of the governmental sector accounting and reporting. The presentation will be made in the chronological order of their publication.

2.1. Reporting entity in New Zealand's conceptual framework

New Zealand concept of the reporting entity will be explained on the basis of the conceptual framework for general purpose financial reporting published in 1993 by the New Zealand Society of Accountants [NZSC]. This is a unique framework globally, because it concerns both the private and the public sector, including the governmental sector.

It states [NZSC, para.2.1] that such an entity exits when it can be reasonably assumed that there are users of general purpose financial reporting, for whom the information provided by such reports will be relevant both to the evaluation of responsibility as regards administration of resources entrusted to the reporting entity, and to making economic decisions. This mainly relates to using information for [NZSC para.3.1]:

- evaluation of financial and service performance of the reporting entity, its financial position and its cash-flows;
- evaluation of compliance of the activities and situation of the reporting entity with the statute law and common law, other regulations and provisions of contracts, in so far as these laws, regulations and provisions relate to financial and service-providing performance, financial position and cash-flows;
- making decisions concerning providing the reporting entity with constitutive resources or conducting business with it.

The above statements [2] indicate clearly that principal attributes of a reporting entity are thought to be financial and service performance, financial position and cash-flows. As regards relations with the environment, the greatest importance is attached to economic relations with actual and potential suppliers of constitutive and productive resources and returnable financial resources, as well as with consumers of products. It is also stressed [NZSC para.3.2] that satisfaction of the information needs stated above is mostly achieved by publication of financial reports depicting fundamental attributes of a reporting entity, that is its financial and service performance, financial position and cash-flows.

It is interesting to note that New Zealand conceptual framework does not explicitly define a reporting entity, but implies its definitive separation and naming. A set of fundamental attributes of a reporting entity formulated in this framework clearly points to its being an object fitting the definition of an organisation, so it simply is an organisation.

2.2. Reporting entity in the conceptual framework of the US federal sector

The question of a reporting entity in the US federal sector is regulated by a standard entitled Statement of Federal Financial Accounting Concepts No. 2. Entity and display [US SFFAC No.2], prepared by the Federal Accounting Standards Advisory Board and issued in April 1995 by the Executive Office of the President of the United States. This standard is one of three standards constituting the conceptual framework of the US federal sector. It leaves no doubt as to the nature of a reporting entity, stating explicitly that it is an organisation [US SFFAC No.2, para.3.1]. An organisation also is obliged to prepare and present reports concerning the budget and programs (functions).

According to SFFAC No.2, US Federal Government is an extremely complex organisation, made up of many various components [US SFFAC No.2, para.11]. As far as accounting and financial reporting is concerned, this organisation may be viewed from three angles, i.e. organisational complexity, budgeting (planning) and functional (programs). A reporting entity has to be identified with all the three dimensions taken into account, along with the requirement of meeting all of the following criteria [US SFFAC No.2, para.29]:

1) Existence of management responsible for:
 - control and allocation of resources;
 - generation of products and other results of the existence and functioning of the entity;
 - execution of the politically determined budget or its part (if the entity is covered by this requirement).
2) Character of the entity, allowing to represent its operation and financial position by means of financial statements.
3) High probability of the existence of users of the entity's financial statements, who are interested in using the information provided for allocation of resources and making other decisions and for imposing upon the entity of the obligation to account for the allocation and use of these resources.

Objects fulfilling all of the criteria listed above may be identified only from organisation complexity perspective. Thus a reporting entity can be both an organisation that is an autonomous economic unit (which the federal government definitely is) and its constituent organisations [US SFFAC No.2, para.51]. It is, however, necessary to establish criteria of dependency between the organisations, that is criteria of inclusion of individual entities to the ultimate reporting entity [3]. In SFFAC No. 2 such criteria have been divided into conclusive criteria (para.41 and 42) and indicative criteria (para.43-46). A conclusive criterion relates to the existence in a relevant section of the federal budget of a provision stating that it covers a given object. With regard to financial reporting purposes this means that a given object comes in the composition of the final reporting entity. Indicative criteria relate basically to criteria of control of a given organisation and criteria of benefiting from its activity. Inclusion on the basis of indicative criteria takes place when it meets all of the adopted indicative criteria.

As regards relations with the environment, SFAC No.2 states that information about a reporting entity is mainly conveyed by means of financial statements, which make up the financial report [US SFFAC No.2, para.54]. According to this standard, financial statements are the main vehicle for communicating to external users both accounting information and information from sources other than accounting. But certain types of information about a reporting entity may be provided within the framework of a financial report by means of instruments that are not financial statements [ibid.]. In accordance with the purposes of financial reports of the US federal sector as formulated in US SFFAC No.1, such reports are to fulfil the following objectives [US SFFAC No.1, para.13-17]:

- Ensuring the integrity of the federal budget (budgetary integrity).
- Evaluation by interested parties of the operating performance of the federal government (operating performance).
- Evaluation by interest parties of the present and future effects of the operations and investments of the federal government on its financial position and the financial condition of the country (stewardship).
- Evaluation by interested parties of the degree of suitability of federal systems of financial management and federal instruments of accounting and administration for proper realisation of transactions, protection of the resources and supporting income measurement (systems and control).

As far as investigation into the nature of a reporting entity is concerned, the second purpose is of particular significance. Fulfilment of this objective is to be aided by supplying information which maks it possible to evaluate [US SFFAC No.2, para.6]:

- Management of its assets and liabilities;
- Its operations, costs and results;
- Ways of financing these operation and results;

As specified in [US SFFSC No.2, para.1], attainment of financial reporting purposes necessitates on the one hand statements representing in money terms the situation of a given entity at a given moment (stock statements) and its flows in a given period of time (flow statements), and on the other hand – specific statements containing additional information to supplement the financial statements (notes to financial statements and supplementary financial information) and presenting the reporting entity (management analyses and comments). According to [SFFAC No. 2, para.57], balance sheet is an example of a statement depicting the state of a reporting entity; examples of statements representing flows include a statement of operations [4], a statement of changes in net positions, a statement of custodial activities [5], and a statement of net costs of the different service functions (programs) [6], the last two statements being specific cases of a statement of operations.

2.3. Reporting entity in the conceptual basis of International Public Sector Accounting Standards

The first International Public Sector Accounting Standards (IPSAS) were promulgated in May 2000. They are based on IAS and the underlying conceptual framework but IAS were treated as the starting point for developing the conceptual structure of accounting appropriate to the specific character of the public sector. Elements of this structure are created by defining modifications of fundamental elements of accounting and reporting in promulgated standards and draft standards. This refers to the reporting entity, as well. In the IAS conceptual framework a reporting entity is an enterprise, [IASCF, para.8], that is an organisation, the metagoal of each is generating economic benefits going for the owner. Since IPSAS basically refer to entities other than enterprises, a reporting entity requires a separate definition. In the conceptual basis of IPSAS there is a term "economic entity" used synonymously with a reporting entity, defined in [IPSAS 1, para.6]. According to this definition, an economic entity is a group of entities comprising a controlling entity and at least one controlled entity [7].

It is stressed that the term "economic entity" covers both profit-oriented and non-profit entities whose goals are defined by social policy [IPSAS 1, para. 9]. It is also pointed out that an economic entity is sometimes called an "administrative entity", "financial entity", "consolidated entity" or "group". So, although IPSAS do not explicitly use the term "an organisation", the terms quoted above suggest clearly that an economic entity as defined in IPSAS is an organisation – moreover, an organisation that is made up of other organisations. The criterion of regarding a given organisation as part of an economic entity is the criterion of actual existence of control, which is established on the basis of existence in the set of interrelated organisations of active relations of superior authority and transfer of benefits [IPSAS 6, para 26-38].

The principal objectives of general purpose financial reporting [IPSAS 1, para 13] is provision of information on financial position, performance and cash flows of a reporting entity, which is useful to a broad rang of users in making and evaluating decisions on the allocation of resources of a given organisation. It should be stressed that thus formulated objectives comprise the decision-making usefulness aspects and the accountability aspect. This means that general purpose financial reporting can also play a prospective role with respect to prediction of the level of resources necessary for the continuation of activity and the level of resources that can be accumulated as a result of this activity, as well as with respect to the risk and uncertainly involved. Moreover, general purpose financial reporting can supply information on compliance in obtaining and using resources with a budget adopted in a legally prescribed way, and compliance in obtaining and using resources with legal and contractual requirements and financial limits set by competent authorities.

The authors of IPSAS are well aware that financial statements [8] alone do not suffice to satisfy information needs consequent upon the objectives formulated in [IPSAS 1, para.13], because the objectives of the governmental sector economic entities included service objectives, apart from financial purposes. In such cases financial statements ought to be accompanied by supplementary non-financial statements, presenting a broader view of an organisation's activity in a given period of time [IPSAS 1, para.16].

We wish to draw attention to the statement of the authors of IPSAS that non-financial and financial objectives are parallel and that financial information should be supplemented by information on non-financial performance. This can be regarded as a manifestation of the view that in order to achieve completeness of reporting on the state and performance of an organisation, financial statements represent a requisite condition and non-financial statements represent a sufficient condition.

3. REPORTING ENTITY AND CASSES OF REPORTING INFORMATION IN THE LIGHT OF MODELS OF AN ORGANISATION

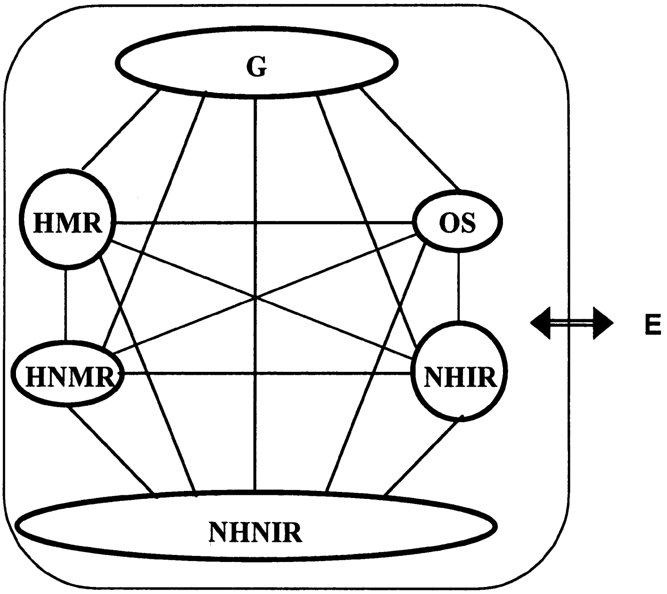
From the perspective of normative description of an organisation, of primary importance for the establishment of the manner of this description are models of an organisation and its relationships with the environment. From among the many possible metaphors and metamodels of an organisation, particularly relevant to financial reporting are: metamodel of its structure, metamodel of its behaviour, and metamodel of its social relations. Below will be presented these types of metamodels. For the sake of conciseness, their graphic versions will mainly be used.

3.1. Model of the metastructure of an organization

It follows from the definitions quoted earlier in the text that organisation as on object set apart from the environment comprises *explicite* a metagoal, human resources and non-human resources, and implicit structuring of the resources in a way that makes possible attainment of this metagoal. Consistent with this approach model of the metastructure of an organization is shown in *Figure 1*. This model suggests that resources ought to be described in the context of the purpose of their identification and structuring and their relations with the environment. For example, if generation of economic benefits is the aim of such identification, those of the resources ought to be described which are likely to bring benefits of this type in the future [9]. If resources have been allocated for purposes other than generating economic benefits, those of the resources ought to be described which are likely to generate those other benefits. If we assume – as has evidently been done in the case of IPSAS – that generating benefits other than profits is not possible without generating at least a small degree of the latter, it is necessary to describe those types of resources which are likely to generate in the future both economic and non-economic benefits [10].

3.2. Metamodel of the behaviour of an organization

The behaviour of an organization is of fundamental importance for its continuing in existence and development. Since organisations belong to the class of open systems [11], their continuance and evolution are determined by fundamental attributes of these systems. A metamodel of organisation as an open system is shown in *Figure 2*, and the fundamental attributes of an open system are set out in *Table 1*.



G	metagoal / metagoals,
HMR	human managerial resources (managers) – the first identified component of human resources creating a social subsystem,
HNMR	human non-managerial resources (staff) – the second identified component of human resources creating a social subsystem,
NHIR	non-human information resources,
NHNIR	non-human non-information resources,
OS	organisational structure, that is a set of relationships and interactions, including accountability relations,
E	natural, social and economic environment.

Figure 1. Metastructure of an organization

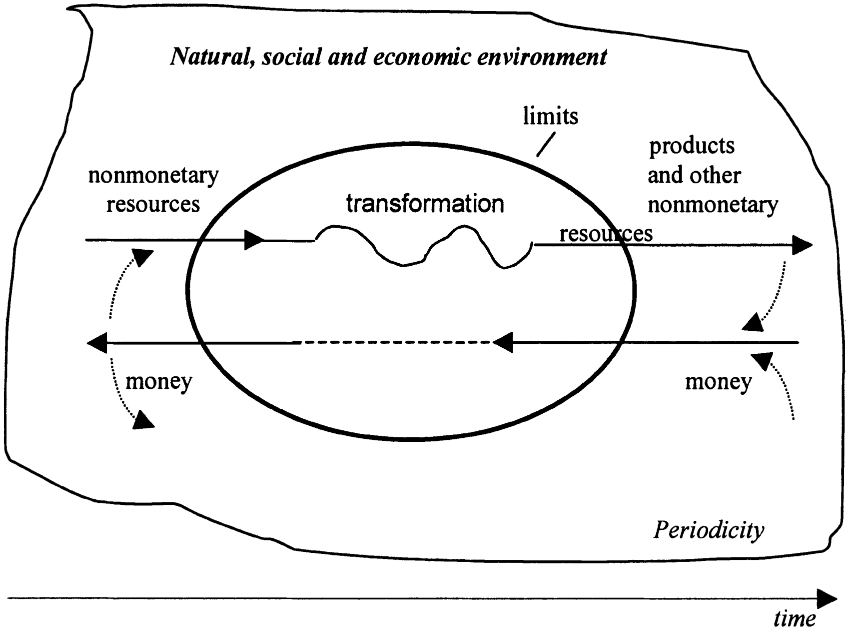


Figure 2. An organization as an open system with money as the determinant of exchange

On the basis of the systemic model of organisational behaviour and fundamental attributes of an open system it is possible to formulate the necessary and sufficient condition of continuance and development of the organization:

1) the necessary condition – existence of the ability for exchange appropriate to the volume of accumulated resources, that is adequate intensity and continuity of the flow of cash;

2) the sufficient condition – existence of the ability, appropriate to the volume of accumulated resources, to generate excess of imported resources over the resources that are being used and exported.

Table 1. Open system fundamental attributes

Chief attributes of each open system are

- separation,
- inputs,
- transformation processes,
- outputs,
- interactions.

Apart from the main characteristics, open systems have a number of specific features. According to [Katz, Kahn p. 23 -30] [12], in order to understand the nature of organisation it is essential to consider not only the main attributes of open systems, but also their other characteristics, especially such as:

a) Limits.

The possibility of the existence of limits is a necessary condition for the formation of a system. From the viewpoint of the organisation as an object comprising the human element, the boundary means the awareness of the environment and awareness of the influence of changes in the environment on the attributes of the system as well as the impact of system (attributes) changes on the environment.

b) Feedback.

Feedback means the return of part of the output (or information on the output) to its input. The occurrence of such transfer is a necessary condition of output control that is attaining and maintaining the required level of output. Feedback is a specific form of interaction between the system and its environment.

c) Cyclical character.

In terms of dynamics, open systems are formed by cycles of events, so cycles of events constitute the existence of an economic entity. Outflows through output enable inflows through input and repetition of transformations, which provides for the cyclical character of open systems. In the class of open systems, which are called organisations, certain categories of inflows and outflows as well as repetitions are usually co-ordinated by an agent of exchange, which typically is some form of money. It is important to note that the introduction of an agent of exchange results in the possibility of non-simultaneity in the movement of the basic object factor and the agent. Such a situation requires controlling not only the resources and the agents, but also related obligations.

d) Negative entropy.

An open system imports energy and information from the environment, which restrains the tendency to growth, which is inherent in entropy. The imports may exceed the exports. In the case of the organisation this means the possibility of preventing destruction and disintegration, allowing thus to maintain internal states (repairing and sustaining elements and relations, avoiding "death") and, when imports are in excess of exports, also the possibility of adapting the elements and structure to changes in the environment and the possibility of growth and expansion.

Table 1. (Continued)

e) Steady state (homeostasis).

Importation, which restrains entropy, requires a degree of steadiness in the level of exchange with the environment. The exchange denotes inflow and outflow, but the steadiness of the former and the stability of the latter lead to a dynamic balance, which ensures relative stability of the character of the system.

f) Movement toward growth and expansion.

The steady state is the feature of rather simple open systems. In order to survive, complex open systems acquire more energy than is immediately needed to counteract entropy. Owing to this surplus the system character preservation can occur through growth and expansion. The most common growth pattern of a complex system is merely a replication of the same type of subsystems or cycles. As a result of such a multiplication some new properties of a whole can emerge.

g) Balance of homeostasis and adaptive activities.

In order to balance the state of the open system it is necessary to reconcile two opposing functions – homeostasis (maintenance of the state) and adaptiveness. The purpose of the maintenance function is it assures internal balance and compatibility with the environment, whereas the adaptive function is aimed at shaping the elements and relations in such a way as to adjust them to changing internal and external requirements. The fulfilment of both functions is a condition of the durability of a system. Stable, well-managed systems will not endure for long if they do not have the ability to adapt to changes. Similarly, systems capable of adaptation will not survive if they are not capable to sufficiently stabilise their states.

h) Equifinality.

This attribute means that any given final state may be achieved even if the initial states and subsequent trajectories vary widely. It follows, then, that an organisation may attain its goals even if there is instability of inputs and transformations.

The necessary and sufficient conditions of continuance and development indicate that what ought to be described is the ability to carry on exchange with the environment and ability to generate surplus resources, as well as the effect of changes in sources generating a constitutive resource (arising thanks to the creator of the organisation) on the ability for exchange with the environment and the ability to generate surplus. When measuring in monetary units both types of the ability and the impact of sources generating a constitutive resource, representation of the necessary condition and sufficient condition will require a cash flow statement, an income statement and a statement of changes in equity.

3.3. Metamodel of social relations of the organisation

If we assume that social relations of an organisation are shaped by its role in satisfying the needs of its members *sensu largo*, the model appropriate to this perspective is a social agreement model, based on legal and constructive contracts between the organisation and its participants. The modern version of such a model, called a contract model of a firm, was developed by an American, Shyam Sunder [Sunder, p.14-20]. This model refers to the governmental sector organisation, too [ibid, p.186]. It is presented in *Figure 4* and *Table 2*.

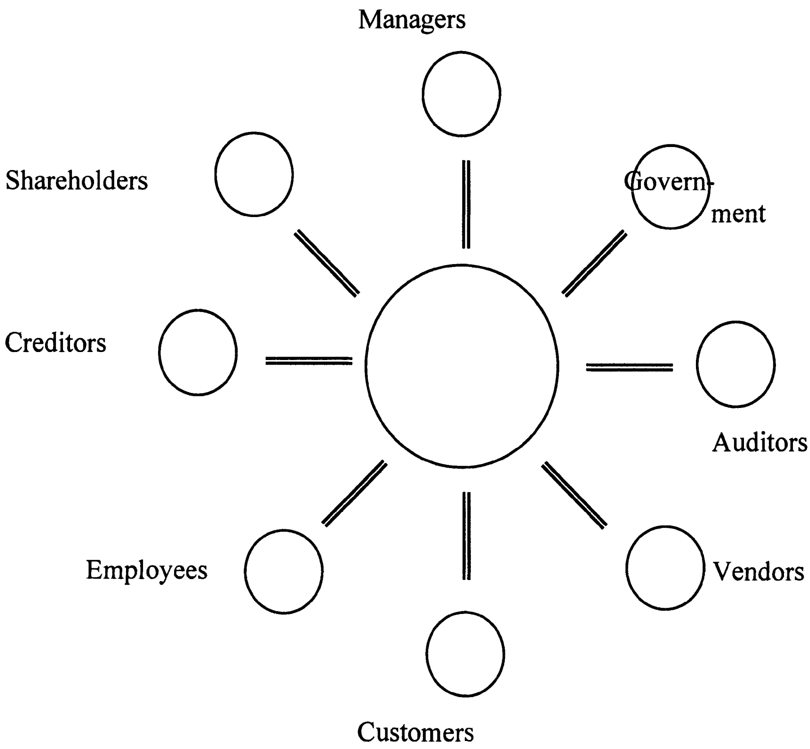


Figure 3. Organisation as a set of stakeholders and contracts (Contract theory of the firm)

Table 2. Contributions and entitlements of various agents (Contract theory of the firm)

Type of agent	*Contribution*	*Entitlement*
Shareholder	Equity capital	Dividend, residual value
Manager	Skills	Salary, bonus, benefits
Employee	Skills	Salary, wages, benefits
Vendor	Goods, services	Cash
Customer	Cash	Goods, services
Lender/Creditor	Loan capital	Interests, principal
Government	Public goods	Taxes
Auditor	Services	Fees

If we further assume that organisation participants *sensu largo* are equally entitled to know the description of its fundamental attributes, the contract model shows the range of potential receivers and users of information on these attributes [13]. This model also suggests that the cheapest way of reaching those users is making this information publicly known. It therefore suggests introduction of general purpose reporting.

3.4. The model of general purpose reporting in organisation metamodels perspective

In the context of organisation metamodels presented earlier, general purpose reporting ought to comprise representations of fundamental attributes of the organisation in both its financial and non-financial aspects. Fundamental attributes of the organisation include: resources, which are to be separated and structured, their interactions with the environment, ability to engage in exchange with the environment, ability to generate resource surplus, the impact on both abilities of changes on sources generating the constitutive resource, and the ability to create products (service potential).

If organisation participants *sensu largo* are equally entitled to obtaining information on its states, flows and performance, then representation of fundamental attributes of the organisation ought to have the character of a public good. From the financial reporting perspective only the accrual basis of measurement and the business reporting model meet the reporting requirements that follow from organisation metamodels.

It should be stressed that in the presented metamodels of an organization a distinction ought to be made between the fundamental attributes of an organization and its metagoal or metagoals. This refers in particular to the financial expression of the sufficient condition for continuation and growth of an organization, that is the financial result. This result reflects not only the organization's ability to generate surplus, but, being the source of economic benefits imported to the environment, is often the reason for the setting up and functioning of an organization, as is the case with business enterprises. Thus there may be two intentions in surplus (income) determination: establishment of an organisation's ability to survive and grow, and establishment of its ability to satisfy economic needs of its creator. The first one can be realised independently of the latter but the latter cannot be realised without the former. The first intention is also an expression of the wish to get to know the sources determining the possibility of surplus generation. It is particularly important in the case of the governmental sector accounting and reporting. *Eo ipso* it can be stated that the shaping of a given system of governmental accounting ought to be carried out with taking into account the required distance between the surplus as a metagoal assumed in the accrual approach and the metagoals of the governmental sector organization.

4. THE ACCOUNTING AND REPORTING SYSTEMS OF GOVERNMENTAL SECTOR ECONOMIC ENTITIES IN THE CONTEXT OF ORGANISATIONS METAMODELS AND KEY CONCEPTUAL FRAMEWORKS

The analysis carried out so far makes possible identification of the characteristics of a holistic model of accounting and reporting for governmental sector organisations and their comparison with the characteristics of some practical models. The results are presented in *Table 3*. This figure shows that the characteristics of a holistic model of accounting and reporting of public sector organisations identified on the basis of organisation metamodels can be regarded as an attractor for practical models. This seems to be a major argument for using organisation metamodels in the development and interpretation of practical systems of governmental accounting.

Table 3. Characteristics of a holistic model of accounting and reporting of governmental sector organisations

	Characteristics by organization metamodels	*Characteristics by conceptual frameworks*		
		New Zealand	*US FASB*	*IPSAS **
Measurement basis for financial representations	accrual	accrual	accrual **	accrual
Representation of fundamental attributes of an organisation	full	full	partial	full
Reporting by managerial bodies of an organisation to its participants at large on the effects of using entrusted resources (accountability)	yes	yes	yes	yes
Model of financial reporting	business	business	selected elements of the business model	business
Nonfinancial reporting	yes	yes	yes	yes
Equal entitlement of organisation participants to official information on its fundamental attributes	yes	yes	yes	yes
General purpose reporting as a public good	yes	yes	yes	yes

* In accordance with IPSAS promulgated by 2001.04.30. There has been the draft of International Public Sector Accounting Standard based only on the necessary condition for the continuance and development of an organisation, that is representation covering only cash resources [ED IPSAS 9].

** With possibility of modification depending on the expected use of the generated financial information [US SFFAC No 1. para. 197].

5. WHAT OUGHT TO BE COMPARED FIRST IN INTERNATIONAL COMPARATIVE STUDIES OF GOVERNMENTAL ACCOUNTING SYSTEM ?

The results of the analysis conducted hitherto justify the following statements:
- the characteristics of governmental accounting systems are comparable;
- it is possible to select a set of characteristics which ought to be compared;
- the real distance between the surplus as a metagoal of an organization assumed in the accrual approach and the metagoals of the compared governmental sector organizations ought to be taken into account.

The characteristics that should be compared first are those specified in the first column of *Table 3*. These international comparative studies ought to deal, in the first place, with:
1) Manner of identifying the organisation constituting a reporting entity.
2) Scope of representation of fundamental attributes of the organisation.
3) Measurement basis of financial representations.
4) Manner of reporting by managerial bodies of an organisation to all its participants on the effects of the use of resources (accountability).
5) Model of financial reporting.
6) Model of nonfinancial reporting.
7) Scope of entitlement of organisation participants to official information on its fundamental attributes.
8) Character of the reporting of governmental sector organisations: to what extent is it a public good ?

It should be noted at this point that carrying out this type of comparisons is relatively easy where there is a conceptual framework of accounting and financial reporting for the governmental sector. The existence of such a framework, however, is rather an exception than a rule, globally. Therefore it seems fully justified that, given the lack of conceptual frameworks, organisational models should serve as a base. We wish to stress that comparative research should embrace both the central and the local level.

6. PHILOSOPHY UNDERLYING ACCRUAL ACCOUNTING AND REPORTING OF THE GOVERNMENTAL SECTOR

Global developments over the past two decades seem to indicate that evolution of accrual accounting and business reporting model of the government sector is determined on the one hand by increasingly advanced accounting instruments and technology and increased risk of reaching in foreseeable time the limits of the possibilities of drawing on available resources, and on the other hand by the growing impact of fiscal burden on public authorities elections and the rate of development of democratic societies [14]. These factors broaden and restructure the responsibilities of politicians. As a result, politicians seek objectivisation in explaining their intentions and actions and therefore begin to expand and publicise the sets of financial information on the resources entrusted to them by the society and on the results of their use. This is the reason for the qualitative change in the ways of reporting to the general public - an entity almost exclusively political until now is becoming an accrual reporting entity and the business reporting model is being introduced.

From the point of view of governmental sector's accounting and reporting orientation, it means the change from the concentration on the imaging of a resource cricital for entity's continuance , i.e. on cash, to the imaging all of kinds of economic resources and all of results of their use.

7. CONCLUSION

The hypothesis formulated in the introduction, stating that a reporting entity is an organization, finds corroboration in all the three key conceptual frameworks of governmental accounting. These frameworks also confirm that the governmental sector organization should represent and disclose both the financial aspect of their fundamental states and flows and the major functions (programs) and intentions (plans). However, the final shape or the reporting model depends on the approach to selecting and structuring the economic resources and sources of their financing, adapted for financial imaging purposes ([Jones & Pendlebury, p.126-131], [Nowak, 1998b, s.60-78]).

The main reason for attempts by public authorities in developed countries aimed at definite determination of the shape and nature of the governmental sector reporting is the desire to assure the users of financial reports that they contain all essential information about a reporting entity, limited only by costs and time constraints.

A basis for international comparative studies on accounting and reporting systems of the governmental sector ought to be provided by both the metamodels of an organization and conceptual frameworks of accounting and reporting for this sector.

NOTES

1 For the way of defining an organization within accounting see for example [Atkinson et al., p.40].

2 Accepted as objectives of general purpose financial reporting.

3 It must be stressed that only an economically independent organisation can be a final reporting entity.

4 That is the profit and loss account.

5 These are activities such as collection and transfer of taxes, customs duties or excise duties.

6 It represents full cost of a particular service function, revenue from charges for its products and differences between these costs and revenues.

7 Therefore in a group of economic entities ought to be identified the controlling entity and at least one controlled entity, with control meaning here authority to control financial and operating policies of another entity in a way that enables the controlling entity to draw benefits from its activity.

8 According to [IPSAS 1, para.19] a complete set of financial statements consists of a statement of financial position, a statement of operations, a statement of changes in net positions, a cash-flow statement, a statement of accounting policies and notes to financial statements.

9 This approach is commonly adopted for defining assets in the conceptual framework of business accounting and financial reporting.

[10] See definition of assets in [IPSAS 1, para 6].
[11] See for example [Atkinson et al., p.442] and [Gordon. pp.17-19].
[12] After [Robbins, p. 15 - 19].
[13] On financial information theory from the perspective of a stakeholder see [Niskala M., Näsi S].
[14] It is important to note, however, that this refers mainly to the highly developed countries. In transitions economies and countries not classed among the developed ones, the current situation may be slightly different.

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PHILIPPE ADHÉMAR

THE PUBLIC SECTOR COMMITTEE (PSC) THE STANDARDS PROJECT

1. IFAC-PSC APPROACH

1.1. IFAC and the Public Sector Committee

The PSC is a standing committee of the Council of IFAC. IFAC is a non-profit, non-governmental, non-political, international organisation of accountancy bodies. At present, IFAC has representation from 153 member bodies in 113 countries. The mission of IFAC is the development and enhancement of the profession to enable it to provide services of consistently high quality in the public interest.

The PSC was established in late 1986 to address, on a coordinated worldwide basis, the needs of those involved in public sector financial management, reporting, accounting and auditing. The PSC members are drawn from the member professional bodies. They are appointed to the PSC because of their knowledge of and experience in public sector financial reporting, financial management or audit. Members of the multilateral lending agencies and certain other regional and international organisations are observers on the PSC with full rights of the floor (see Appendix 1 for PSC membership).

1.2. The Standards Project

The PSC's current activities are focussed on the development of International Public Sector Accounting Standards (IPSASs) for financial reporting by governments and other public sector entities. The PSC actioned the Standards Project in late 1996. The first stage of the project, has been funded by IFAC, the World Bank, the Asian Development Bank, the United Nations Development Project and the International Monetary Fund. Prior to that date the PSC had issued a number of Studies and other documents dealing with public sector financial reporting, auditing and accounting issues.

The Standards Project was established in response to concerns about the variability in the quality of financial reporting by many governments and their agencies. The quality of government financial information reported to external users and to managers is, in many cases, poor. Poor-quality financial information is often associated with poor standards of financial management, economic decision making and accountability. Such an environment contributes to a low standard of financial discipline and often leads to corruption and mismanagement.

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 61-71.

The relationship between good governance and better economic outcomes is also increasingly being acknowledged. Holding governments and their agencies accountable is a key element to good governance in the public sector and fiscal transparency is one (though by no means the only) necessary condition for the discharge of accountability. Important components of any governance system are: a) the preparation of financial reports in accordance with well understood and generally accepted accounting standards developed in the interests of the users of financial statements of public sector entities; and b) an audit that provides assurance that those standards have been complied with.

For users of financial statements of governments and their agencies and those concerned about financial transparency, the benefits flowing from the development and maintenance of IPSASs will include: a) the establishment of appropriate financial reporting practices; b) consistency in application of those practices (both between countries, as well as within a country from period to period); and c) the potential harmonization of financial reporting between economic and accounting bases.

The adoption of IPSASs will also provide for greater efficiency and effectiveness in the audit and analysis of governmental financial reports as common rules are adopted around the world for the financial reporting of similar transactions and events. It will also mean that financial reporting expertise, so often a scarce resource in the public sector, will become more mobile across national boundaries, with the expectation that, for example, developing economies will be able to access this resource at lower cost.

1.3. An International Public Sector Standard Setter

In the private sector, the International Accounting Standards Board (IASB) issues International Financial Reporting Standards (IFRSs) for application by business enterprises. These Standards support the efficiency of both international and domestic capital markets. The IFRSs are a necessary component of recent initiatives to strengthen financial transparency and enhance corporate governance. (The IASB has recently been established and replaces the former International Accounting Standards Committee (IASC) which issued International Accounting Standards (IASs). The IASs issued by the IASC continue in force until they are amended or withdrawn by the IASB.) The PSC has issued Guideline 1 Financial Reporting by Government Business Enterprises (July 1989), which explains that Government Business Enterprises should apply the same International Accounting Standards as private sector enterprises.

The development and maintenance of IPSASs will likewise enhance the quality and consistency of financial reporting by public sector entities. Such Standards will provide governments with a cost efficient means of ensuring that the financial reports of public sector entities in their jurisdiction include financial information of sufficient quality to discharge accountability obligations to Parliament or taxpayers and to support informed decision making by a wide range of external users. The IPSASs are as equally an important component of initiatives to strengthen government financial transparency and governance as their private sector counterparts are to the private economy.

The PSC is well credentialed to perform the role of International Public Sector Standard Setter. This is because it:

- has been established to operate in the interest of users, and is independent from control by those that would seek to influence the outcomes generated other than in the interests of users;
- possesses appropriate technical expertise, knowledge of institutional arrangements encompassed by its constituency and a membership mix that encompasses technical proficiencies of users, preparers and auditors and a broad geographical spread;
- adopts a formal due process, which provides stakeholders with the opportunity to contribute to the development process; and
- as a Committee of IFAC, possess sufficient authority for the development and implementation of pronouncements.

2. CURRENT ACTIVITIES

2.1. Background And Current Status of Stage 1 (1996 – May 2001)

As noted above, the PSC actioned the Standards Project in late 1996. The objectives of the initial stage of the Standards Project are extremely ambitious. They are to develop by the end of 2002

a) a Background Paper which provides guidance on issues to be confronted in financial reporting by public sector entities and approaches to their resolution and
b) a set of IPSASs based on International Accounting Standards (IASs) promulgated by the IASC and on issue in August 1997, to the extent that the requirements of the IASs were appropriate for public sector entities. Work on the development of Standards was commenced in late 1997.

2.1.1. The Background Paper (Study 11, issued May 2000)

The Background paper:

a) considers users of general purpose financial reports (GPFRs) of public sector entities and their likely information needs;
b) identifies the likely objectives of financial reporting by public sector entities; and
c) outlines common bases of accounting currently used by governments - being cash accounting (including modified cash accounting) and accrual accounting (including modified accrual accounting).

An Exposure Draft of the Paper was issued in March 1998 and the finalised Paper, Study 11 Governmental Financial Reporting: Accounting Issues and Practices, was issued in May 2000.

The PSC had previously considered some of these matters in publications such as Study 1 Financial Reporting by National Governments (1991), Study 2 Elements of Financial Statements (1993) and Study 8 The Government Financial Reporting

Entity (1996). Study 11 builds on the work previously undertaken by the PSC. It identifies issues to be resolved in preparing financial reports under the differing bases and considers the extent to which financial reports prepared under each basis satisfy the objectives of financial reporting. The Study focuses on the cash and accrual bases. However, it is intended to assist governments in the preparation of their financial reports whichever basis is adopted. To this end it includes examples of financial statements prepared by governments under a wide range of bases.

The Study also considers the objectives of the System of National Accounts (SNA) and the International Monetary Fund's Government Finance Statistics (GFS). It notes that while the frameworks adopted for SNA, GFS and GPFR are similar, they focus on different reporting entities and their objectives differ.

2.1.2. Development of International Public Sector Accounting Standards

This stage of the Standards Project includes the development of a comprehensive standard for the cash basis and a core set of IPSASs for the accrual basis of accounting. Initially, this stage of the project also encompassed the development of Standards for the modified cash and modified accrual basis. However, many PSC constituents argued strongly, and convincingly, that it was not appropriate to develop Standards for the modified cash and modified accrual bases. After issuing an Invitation to Comment on this matter in 1999 and receiving an overwhelming response in support of developing Standards for only the cash and accrual bases, the PSC refocussed the Project on developing Standards for only the cash and accrual bases.

The Cash Basis. A single comprehensive IPSAS dealing with the cash basis of accounting is being developed by the PSC. Exposure Draft 9 Financial Reporting Under The Cash Basis of Accounting was issued in May 2000 for comment by 30 November 2000.

The ED prescribes the manner in which the general purpose financial statement prepared under the cash basis of accounting should be presented. It includes requirements relating to the structure and content of the financial statement, the identification of the reporting entity and proposes the separate disclosure of movements in cash and cash equivalents from operating, investing and financing activities. The ED also

a) deals with accounting for foreign currency cash flows, reporting in hyperinflationary economies and the presentation of a consolidated financial statement; and
b) requires disclosure of key information including the accounting policies adopted for significant transactions, the major classes of operating cash flows, and interest and dividends received.

It is intended that application of the requirements of the IPSAS that is developed from ED 9 will ensure that cash basis financial reports issued by governments and other public sector entities are prepared on a consistent, appropriate and well understood basis. This will enhance comparability with the entity's own financial statements of previous periods and with the financial statements of other entities. The application of an IPSAS on the cash basis will facilitate a better understanding of the cash position of governments, changes in that position and the major sources and uses of cash.

The PSC has now commenced the process of reviewing the 41 responses to that Exposure Draft. A number of respondents noted that ED 9 adopts a broader notion of the reporting entity than is currently adopted by most countries that report on a cash basis. Some respondents expressed concern about the ability of some of these countries to adopt an IPSAS based on ED 9. Consequently, the PSC has decided to extend its due process by including a further period of targeted consultation. In co-operation with the World Bank, the PSC has approached a number of developing countries to consider their views on the proposals in the ED and to gain a better appreciation of the practical difficulties that may be encountered in complying with the proposals in the ED. The period of extended consultation has been to be completed and the Standard will be finalized in 2002. This approach provides the PSC and its constituents with the opportunity to better understand

a) the requirements of any proposed IPSAS on Financial Reporting Under The Cash Basis of Accounting; and
b) the issues that will be faced by differing jurisdictions in implementing that IPSAS.

The document has been restructured in order to identify minimum mandatory requirements on one side and encourage, but not require, on the other side a range of other matters like disclosures of :

- major categories of receipts and payments by nature and function either as part of the primary financial statements or as notes;
- undrawn borrowing facilities
- extraordinary items
- certain disclosures about controlled entities…etc

While this approach has slowed down the Standard development process, it provides the potential for a better implementation in the short term and more consistent application of the Standard in the long term.

The Accrual Basis. A core set of IPSASs for application in the preparation of accrual based financial reports has already been developed. They are, where appropriate, based on IASs promulgated by the IASC as at 31 August 1997 or their subsequently revised versions. August 1997 is the date at which the Standards development stage of the Standards Project became active. At that date 22 IASs had been issued. The PSC determined to defer consideration of the IASs dealing with business combinations and employee entitlements until the other IASs had been dealt with.

Considerable progress on the development of the initial set of IPSASs has been made. The PSC issued the first eight IPSASs in May 2000. They are:

- IPSAS 1 Presentation of Financial Statements
- IPSAS 2 Cash Flow Statements
- IPSAS 3 Net Surplus or Deficit for the Period, Fundamental Errors and Changes in Accounting Policies

- IPSAS 4 The Effect of Changes in Foreign Exchange Rates
- IPSAS 5 Borrowing Costs
- IPSAS 6 Consolidated Financial Statements and Accounting for Controlled Entities
- IPSAS 7 Accounting for Investments in Associates
- IPSAS 8 Financial Reporting of Interests in Joint Ventures

At its meeting in May 2001, the PSC approved an additional four IPSASs for publication in June 2001:

- IPSAS 9 Revenue from Exchange Transactions
- IPSAS 10 Inventories
- IPSAS 11 Construction Contracts
- IPSAS 12 Financial Reporting in Hyperinflationary Economies

At its May 2001 meeting the PSC also approved IPSAS 13 and at its november 2001 meeting issued a further 5 IPSASs dealing with specific issues under the accruals basis of accounting. The following IPSAS and ED were issued in december 2001:

- IPSAS 13 Leases
- IPSAS 14 Events After Reporting Date
- IPSAS 15 Financial Instruments: Disclosure and Presentation
- IPSAS 16 Investment Property
- IPSAS 17 Property, Plant and Equipment, and

And IPSAS 18 Definition of a segment has been adopted in PSC march 2002 meeting.

The PSC hasl issued two more Exposure Drafts of proposed IPSASs in June 2001, and received comments by 31 October 2001. These Exposure Drafts are:

- ED 20 Related Party Disclosures
- ED 21 Provisions, Contingent Liabilities and Contingent Assets

The PSC will review the comments for adoption of these standards in 2002.

The PSC issued an Invitation To Comment in July 2000: ITC Impairment of Assets. The comment period for this ITC closed on 30 January 2001, at its last meeting the PSC considered the responses to the ITC and the PSC is now in the process of preparing an exposure draft on Impairment of Assets.

Transitional Guidance – Cash Basis to the Accrual Basis. Many of the PSC's constituents, including some currently reporting on a cash basis have expressed support for application of the accrual basis of accounting for governmental financial reporting. This support is based on the view that the accrual information includes, supplements and enhances the cash information currently provided and would provide benefits to both internal and external users. Many of those constituents also sought guidance from the PSC on the process of transition from a cash to the accrual basis. The preparation of transitional guidance was also advocated by many constituents as a necessary adjunct to the proposal to establish Standards for only the cash and accrual bases of accounting. While not originally factored into the Project work program, the PSC is of the view that it is important and is proceeding to develop a document which will provide transitional guidance. PSC has approved the publication of this document as a study in the first quarter of 2002.

2.2. PSC Standards Project Projected Achievements - 2002

It is anticipated that by the end of 20021 the PSC will have issued, or finalised:

- IPSASs dealing with 20 of the 22 IASs identified as the basis of the core IPSASs;
- the IPSAS on the basis of accounting; and
- transitional guidance to assist governments in making the transition from a cash basis to the accrual basis.

Progress will also have been made on the development of a standard on Impairment of Assets for application by public sector entities. While outside the initial set of "core" Standards, guidance on accounting for an impairment of public sector assets is central to the ongoing application of the accrual basis of accounting for governments and many public sector entities, and a key transitional issue for those moving to the accrual basis. Detailed authoritative guidance on this issue has not been promulgated by national or international standards setters. The PSC is of the view that the matter is of such significance that it needs to provide some leadership.

3. FUTURE ACTIVITIES

3.1. The Future Standard-Setting Work Program For The PSC

The initial stage of the Standards project was established with specific limited objectives to be achieved within a limited timeframe. As part of the Standards development process, the PSC has identified a number of specific public sector issues not addressed, or not adequately addressed, by the IASs. In addition, the PSC and many of its constituents have recognised the need to develop a framework for financial reporting by public sector entities to explicitly identify the underlying concepts adopted in the standards setting process. Such a framework will also provide broad guidance to preparers and auditors on the resolution of specific issues not yet the subject of specific Standards. The PSC believes it should deal with conceptual issues on a case by case basis as they relate to its ongoing work program. It is aware that development work on frameworks is occurring in a number of jurisdictions and is exploring whether it can play a useful role as a conduit to coordinate the development of a public sector framework.

To be effective over the long term, Accounting Standards cannot be static documents – they need to respond to the economic, institutional and management environments within which governments and other public sector entities operate. Frequently, as members of the community gain experience with application / operation of any Standard, areas for modification or improvement are identified. In addition, circumstances and transactions not contemplated by the existing body of Standards often arise. The "care and maintenance" of the existing body of Standards, and the need to develop new Standards to deal with additional issues not addressed by the existing body of authoritative literature, shape the long term work program of national and international standards setters.

3.2.Public Sector Specific Issues not Dealt With in the IASs

3.2.1 Three Priorities Have Been Retained by the PSC. They will first be dealt with in new specific steering committees put in place early 2002.

*Taxes and Other Non-Reciprocal Revenue.*The IAS which deals with accounting for revenue (IAS 18, Revenue) is restricted in scope to revenue generated through exchange transactions. However, taxes and other forms of non-reciprocal revenues represent the major form of revenues for most governments. There is a need to develop appropriate accounting treatments for tax revenues (by the recipient) and other non-reciprocal revenue (by both the recipient and the transferor).

Provisions Arising from Social Policy Initiatives. IAS 37 Provisions, Contingent Liabilities and Contingent Assets was issued in 1998, but represented an updating of parts of IAS 10 Contingencies and Events After Reporting Date which was on issue in August 1997. IAS 37 is therefore within the scope of the first stage of the PSC's Standards Project.

However, IAS 37 was developed in the context of an exchange environment and does not address issues related to whether a government's commitment to social policy programs such as health, education, welfare and pensions gives rise to obligations that should be recognised in financial statements, and if so at what point should they be recognised and how should they be measured. In developing its exposure draft on Provisions, Contingent Liabilities and Contingent Assets, the PSC has excluded obligations that arise from social policy initiatives. This reflects the PSC's view that these public sector specific issues require more study before their recognition and measurement is prescribed by an IPSAS and may be dealt with within a separate standard.

Government Budget. Budget execution and financial statements. Most Governments issue financial budgets usually, but not exclusively, prepared on a cash or near cash basis, at least annually. These budget financial statements are widely distributed and promoted and serve as base for the financial reporting of public entities activities. They are also used for analysis of the governments plans and their consequences for the economy. In many respects, and for many users, they are the most important financial statements issued by governments. They are central to ensuring transparency of the government's financial intentions.

The core IPSASs are concerned with the presentation of general purpose financial information. However, they do not address the presentation of budgetary/forecast financial information, nor provide information that enables users to determine whether actual financial results are broadly consistent with previously issued budgets or forecasts and their execution. Given the widespread practice in the public sector of reporting budgetary information, a strong case can be made that there is a need for Standards on at least reconciliation between budget execution and accounting financial statements , or if it appears to be useful on minimum requirements for the budget reporting. Such requirements would be directed at enhancing the comparability of those reports over time, between governments and with the entity's historical financial reports encompassing the same period (or to identify the sources and effects of differences). If no IPSAS on budgets is developed, a case can be made that the PSC could provide guidance or rules on what information should be included in the financial statements to explain the relationship between the budget figures and the financial statements for the same period.

3.2.2 Other Matters Will Need to Be Looked at

Non-Financial Performance Reporting. IPSAS 1 Presentation of Financial Statements, IPSAS 2 Cash Flow Statements and Exposure Draft 9 Financial Reporting Under The Cash Basis of Accounting contain requirements for the presentation of financial information under the cash and accrual bases of accounting. However, there is little coverage in either Standard of semi-financial or non-financial performance reporting.

Financial information is only a subset of the information necessary to allow an adequate assessment of the performance of most public sector entities. Governments and their agencies are required to achieve service delivery and social and economic policy objectives. The performance of governments, and the financial information reported about that performance, needs to be assessed in the context of the achievement of those service delivery and policy objectives. As such, the disclosure of semi- or non-financial information as well as information about the financial characteristics of performance will be necessary for accountability and decision making purposes. In some jurisdictions, requirements/guidance on non-financial performance indicators is in place – for example, disclosures about "service efforts and accomplishments" are required by GASB Standards and "Statements of Service Performance" are published by public sector organisations in New Zealand. At the international level, there is a need to develop guidance to ensure that the linkages between financial information (for example costs) and non financial information (for example, nature, volume and quality of services) are recognised.

Public/Private Sector Arrangements. Accounting for asset construction and financing arrangements between the private and public sectors has raised a number of controversial accounting issues in countries such as Australia, Canada and the United Kingdom. The PSC could usefully draw on the experiences in these jurisdictions and develop requirements for the accounting treatment of these arrangements.

Harmonisation of IPSASs with GFS and SNA. The International Monetary Fund (IMF) is redrafting its Government Finance Statistics Manual to harmonize with the 1993 System of National Accounts. The PSC has provided input on drafts of the revised GFS Manual and is monitoring the progress of it. It should be recognized that these two systems of reporting support different uses, and whilst much of the information required for their different uses is the same, some of their information needs may differ. This project could usefully examine whether differences in the data generated by each system are justified by the different objectives of those systems and identify a process to eliminate or reduce any unnecessary or unintended divergences.A reconciliation of this type would be of particular importance for countries members of European Union whose rules on financial reporting on budgets and debts are linked to SEC 95 (Système Européen de Comptes intégrés), the european version of United Nations SNA.

Measurement of Infrastructure and Heritage Assets. In the process of developing IPSAS 17 Property, Plant and Equipment the PSC acknowledged the difficulty public sector entities will face in reliably measuring certain types of heritage and cultural assets. Respondents to the ED emphasised the practical difficulties inherent in recognising and reliably measuring heritage and cultural assets. While the PSC currently holds the view that in principle all assets, including heritage and cultural assets, should be recognised in the financial statements it acknowledges that more work may need to be undertaken in determining the relevant measurement basis for these assets and valuation issues. IPSAS 17 has excluded heritage assets with the understanding they will be dealt with separately by a later standard and provided a five-year transitional period for application of its requirements to recognize property, plant and equipment.

3.3. IASs that Have Been Developed Since 31 August 1997

The "core" set of Standards that is currently being developed by the PSC is based on IASs extant as at 31 August 1997. There are however a number of IASs that have been developed since then and which the PSC is not currently dealing with.
They include:
- IAS 34 Interim Financial Reporting
- IAS 35 Discontinuing Operations
- IAS 38 Intangible Assets
- IAS 39 Financial Instruments: Recognition and Measurement
- IAS 41 Agriculture

The PSC is assessing the priority it should give to developing IPSASs based on these IASs. In making that assessment the PSC will need to consider the following: i) its constituents have identified several urgent public sector specific issues that the Committee needs to consider; and ii) the new IASB may seek to review at least some of these standards in the short term.

3.4. Implementation of International Public Sector Accounting Standards

The PSC may develop guidance to assist preparers with the implementation of particular International Public Sector Accounting Standards. A number of standard-setters have developed implementation guides when introducing a new standard or to clarify the operation of an existing standard. Whilst implementation guidance may be very useful to constituents it is likely to place a considerable burden on the PSC's resources and activities. The PSC will consider whether implementation guidance is required on a case by case basis with its standards, and will develop guidance as the need arises and as resources allow.

Future works in PSC will also attach a particular importance to IPSAS translation in other languages than english in order to ensure an implementation as large, geographically, as possible.

NOEL HEPWORTH

THE EUROPEAN EXPERIENCE OF AND ATTITUDES TO THE DEVELOPMENT OF INTERNATIONAL ACCOUNTING STANDARDS

1.THE ROLE OF FEE

The Fédération des Experts Comptables Européens (FEE) is the representative organisation for the accountancy profession in Europe. It groups together 38 professional bodies from 26 countries, including all 15 Member States of the European Union and the 3 main member countries of EFTA. Between them, these bodies have a combined membership of 400.000 individuals, of whom approximately 95% are from EU countries. Roughly 45% of the accountants represented in FEE work in public practice, providing a wide range of services to clients. The other 55% work in various capacities in industry, commerce, government and education. FEE also co-operates with the professional organisations of Central and Eastern Europe, some of whom are already observer members of FEE.

FEE commenced operations on 1 January 1987. It took over responsibility for the activities previously carried out separately by the Union Européenne des Experts Comptables, Economiques et Financiers (UEC) and the Groupe d'Etudes des Experts Comptables de la CEE (Group d'Etudes). Both organisations had served the European accountancy profession, since 1951 and 1961 respectively.

The main concern of FEE is with the European Commission, representing the profession's interest to that body and latterly encouraging the Commission to adopt international accounting standards rather than develop a separate European set of standards or even adopt US GAAP. In February 2001, the Commission published a proposal for a regulation on the application of international accounting standards. This proposal requires listed companies to apply IAS in their consolidated accounts from the financial year 2005 onwards[1]. This may also have implications for the application of international accounting standards to the public sector.

FEE has had a public sector committee since it was established in 1987 and that Committee has been concerned to ensure that it complimented and supported the work of IFAC, rather than replicated it. With the emphasis of the IFAC Public Sector Committee on the development of international public sector accounting

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 73-83.

standards, FEE has seen one of its roles as a commentator from a European point of view on those standards.

In terms of its own agenda, the FEE Public Sector Committee has concentrated on those activities that help to make the public sector work better from a management point of view. This is in contrast to the value of accounting standards whose aim is to ensure that the public sector reports in a clear and understandable manner.

Therefore, the FEE Public Sector Committee has been concerned, for example, with corporate governance (or to use the Dutch term 'Government Governance), performance measurement, benchmarking, business planning in the public sector and the role and responsibilities of auditors towards fraud. It has also sought to identify good practice from different European countries and make that more widely available. An example of that was the German approach to the audit of management where a report was required from the auditors if the public sector held 25% or more of the shares in a business[2].

2. THE ACCOUNTANCY PROFESSION AND THE PUBLIC SECTOR IN EUROPE

There is a particular problem for FEE that needs to be borne in mind in considering its work in the public sector. Although the accountancy profession does have members who work in the public sector and some members who audit the accounts of public sector entities, this membership is concentrated in very few countries. The largest public sector membership is in the United Kingdom and the Netherlands. In some other countries the profession may have a limited responsibility for audit, as in Italy where its members can audit the accounts of municipalities. In other European countries the profession has only a very limited public sector role. In some countries, the regulations affecting the profession make it very difficult for members either to carry out any work other than auditing, France and Germany for example. In others they may require a complete separation of the professional activity between auditors and accountants (as in Belgium) with no opportunity to operate a joint practice.

Where the profession may have an extensive role in these countries is in the audit of government business enterprises. These enterprises in the main will be using accrual accounting[3].

Where regulations exist governing the role and responsibilities of the profession, the profession has difficulty in becoming involved in the public sector and therefore in obtaining an understanding of how the public sector works, except as a consultant. It also consequently means that the profession has considerable difficulty in influencing those responsible for the setting of accounting standards in the different countries.

What also has to be borne in mind is that the approach to public sector audit in Europe falls into two main groups. One is the group heavily influenced by the Anglo Saxon accountancy based approach to audit, and the other is heavily influenced by the legal approach to audit. The former countries are identified generally by the appointment of 'Auditors General' and the latter by the appointment of 'Courts of Audit' with the auditors technically being magistrates. Again that distinction creates difficulty for the accountancy profession in trying to influence the development of national public sector accounting standards in some countries.

Another factor that also needs to be taken into account is that an accountancy qualification is often not recognised as a route to preferment in the public sector and, even where it is preferment, it has been limited to financially oriented areas like internal audit rather than general management.

Nevertheless, the profession in Europe does have a major contribution to make to the development of international accounting standards for the public sector and generally speaking has common interests on many issues, and that interest is expressed by FEE. The approach that has been adopted within the European accountancy profession is that the national accountancy bodies in individual countries comment on the detailed issues that may be raised in the development of draft standards and FEE comments on issues of principle that may emerge. (Individual national accountancy bodies may comment on these as well if they wish)

3. ACCOUNTING ACADEMICS AND THE EUROPEAN ACCOUNTANCY PROFESSION

The responsibility for appointing members to the committees of FEE lies with the national accountancy bodies. Over the period of the existence of the Public Sector Committee very few academics have been appointed. At present two are members of the Committee, but this is exceptional. However, in the context of the European accountancy profession's generally limited role in the public sector, the main academic interest would need to be consistent with the activities of the Committee, that is with management rather than technical accounting issues. However, academic input into the consideration of the draft accounting standards is potentially very important. FEE would like to see a closer relationship with the accounting academic community.

4. ACCRUAL ACCOUNTING IN THE EUROPEAN PUBLIC SECTORS

Table 1 sets out the current status of accrual accounting for the financial reporting purposes of the central government in the countries of the European Union. The information has been drawn mainly from information gathered by the OECD.

In some of these countries accrual accounting is used at the municipal level, at the regional level of government and in government business enterprises and agencies, even where cash remains the reporting method of the central government.

Table 1

Country	Full accrual basis	Cash basis except certain transactions on accrual basis	Full cash basis
Austria			X
Belgium			X
Denmark		X	
Finland	X		
France		X	
Germany			X
Greece			X
Ireland			X
Italy			X
Luxembourg			X
Netherlands			X (1)
Norway			X(1)
Portugal			X
Spain			X
Sweden	X (2)(4)		
United Kingdom	X (3)(4)		

(1) *The Netherlands and Norway are exploring the possibility of a switch to accrual accounting.*

(2) *Central government activity in Sweden is mainly carried out through agencies, all of which account on an accrual basis. In the consolidated accounts, certain liabilities are not treated on a full accrual basis.*

(3) *In the United Kingdom, an aim is to move to a consolidated whole of government reporting by 2005.*

(4) *The United Kingdom budget is also on an accrual basis and Sweden is currently considering a switch to accrual budgeting.*

Table 2 sets out who is responsible for determining central government accounting standards. This table illustrates the dominant role of the Ministries of Finance and the accounting profession generally has little influence on or input into those ministries.

Table 2

Country	Finance Ministry	Finance Ministry after consideration by Formal Advisory Board	Finance Ministry appoints independent Board to determine them
Austria	X		
Belgium		X	
Denmark	X		
Finland	X		
France		X	
Germany	X		
Greece	X		
Ireland	X		
Italy	X		
Luxembourg	X		
Netherlands	X		
Portugal			X
Spain	X		
Sweden	X		
United Kingdom		X (1)	

(1) In the United Kingdom, the profession is involved in the setting of standards at the local government level. The move to whole of government reporting will ultimately have an impact upon this.

5. ISSUES RAISED BY THE STANDARDS PROCESS THAT HAVE A PARTICULAR EUROPEAN CONTEXT

There have been four issues of general concern to European countries (as expressed through the accountancy profession) that have caused FEE to take a particular stance.

5.1. The Bases of Accounting

FEE was opposed to the idea that four bases of accounting should be defined: cash, modified cash, modified accrual and accrual. FEE argued strongly for the use of only two bases. The principal reasons for this were the practical difficulties of defining the two intermediate bases and that, even if such bases could be defined, the practical effect would be to discourage governments from moving 'up' the scale of accounting achievement. This was because it would be very difficult for European countries (and others) to meet the accrual standard and hence they would only be able to prepare accounts on either a modified cash or a modified accrual basis. Politically this was unacceptable.

5.2. The Language of the Standards

FEE is concerned that the language of the standards is not familiar to public sector managers or indeed to those who are responsible for the setting of accounting standards. This is well illustrated by the detachment of the European governmental accounting standard setting process from the profession as illustrated above. A particular example is the use of the term 'going concern'. This is a well understood term in the private sector but is one that appears to have little or no relevance to a public sector management that has little contact with the accountancy profession. It is true that reorganisation of public organisations may lead to their functions being abandoned or merged with others. This usually occurs for reasons that have nothing to do with the financial viability of the organisation. This should not be regarded as a 'going concern' matter even if the event becomes known after the preparation of the financial accounts but before their publication. In these circumstances, the values of the underlying assets and liabilities are most unlikely to change. Only if there were a complete abandonment of an activity would the values be at risk and even this would be most unlikely. In the view of FEE, the 'going concern' issue should only be in question if the organisation is, in the view of the management, financially unable to continue in operation. Given the nature of public sector organisations, circumstances where this might occur are difficult to imagine. However in the European context there is, at present, one such and immediate circumstance and that is the introduction of the euro. Unless a public sector organisation is able to operate externally in the euro from 31.12.2001, it will not be able to continue to fulfil its statutory obligations, i.e. continue as a 'going concern'. It will not be able to collect revenues, nor pay its suppliers or staff, nor pay benefits or make any other form of payment.

The view that the FEE Public Sector Committee took was that the language of the public sector standards should be such that the implications of not abiding by a standard should be couched in terminology that is relevant to the operating environment of the public sector. Public organisations have statutory responsibilities and, therefore, the consequences of a failure to act or to act improperly should be defined in similar terms. 'Going concern' is a key term, and one that probably should be adopted by the public sector as it becomes more familiar with accounting standards through the gradual introduction of accrual accounting. However, FEE considered that the term (and others as appropriate) needs an explanation which would set it firmly in a public sector context. At least, the explanatory or introductory material should include an explanation of the term, in this case 'going concern', in a public sector context. Thus this explanation should define 'going concern' in a public sector context as a 'continuing ability to fulfil its statutory obligations'. As public sector bodies derive their powers from statute and as 'compliance' is an important element of audit, such an explanation would be helpful to understanding.

5.3. Transitional Periods

The view of the IFAC Public Sector Committee generally is that transitional periods should be kept short. This shortness would apply to standards affecting both assets and liabilities. In Europe this can pose particular problems. Historically, over time, European countries have developed extensive ownership of many classes of assets, not least infrastructure and heritage assets. Accrual accounting will require that such assets are identified and valued (although to some extent, the requirement can be modified by building 'escape' clauses into the standards and, with present IFAC PSC proposals, this is likely for heritage assets). The alternative to 'escape' clauses is longer transitional periods, of perhaps say 10 years. FEE has taken the view that this would be the more desirable approach, because it would provide a reasonable and practical time limit and therefore encourage the wider adoption of the accounting standard. Exactly the same applies to liabilities and the best example of this is unfunded pension liabilities that several European governments have incurred over time and which are difficult to properly account for in a relatively short period of time. (A further advantage of longer transitional periods is that it should encourage political commitment because the risks associated with the decision are delayed often beyond the immediate political horizon).

5.4. Cash Standards

When the decision was made to focus on the accrual basis, it was also decided to deal with the cash basis through the development of one unified standard. The principal reason for this is that there is no private sector equivalent. Yet as the analysis above shows, cash is the dominant basis for European government financial reporting and it is the way in which the greatest impact could be made in Europe. The draft that has now been prepared is however, in the view of FEE, complex because it deals with both the definition of the cash basis and the consolidation of cash accounts. FEE suggested that these two features should be dealt with in separate standards and would like to see the development of this standard given added urgency.

6. CONDITIONS PRECEDENT TO THE INTRODUCTION OF ACCRUAL ACCOUNTING

There do seem to be indications that, over time, there will be a more sympathetic response by European governments to the adoption of accrual accounting. This ought to draw closer the European accountancy profession to the relevant public sector decision makers. However, both they and the profession need to consider what structural conditions should exist before the adoption of accrual accounting. These also are issues with which the academic community should perhaps be concerned. They include the following:

6.1. Capability, Judgement and Scrutiny

Accrual accounting is far more complex than cash accounting and it requires the exercise of relatively sophisticated judgements. Therefore, the change should only be attempted if the cash accounting system is working effectively and has been doing so for some time. In addition, because of the need for a greater range of judgements, systems do need to be in place that will ensure that these judgements are subject to independent and equally sophisticated scrutiny. This scrutiny needs to have both a political and a technical content. Governments are sovereign and therefore the temptation is to set in place accrual rules that allow the system to be manipulated. Success will depend very much upon how far the government of a country is willing to accept the need for rigorous independent scrutiny, criticism of the standards that are being applied and the results which flow from the application of those standards.

6.2. Culture of Conformity with Rules

More so than with cash accounting, both politicians and managers need to be willing to understand and accept the accounting rules. This should be the norm and divergence should be the exception. There needs to be a central agency that specifies the rules, and that the rules are regarded as fair and equitable, though they may not be liked. (Ideally, this central agency should enjoy a measure of independence from the Ministry of Finance.) The rules must be obeyed, with appropriate punishment if they are not. Until this culture of conformity exists, because of the added complexities of accrual accounting, the cash system should remain.

6.3. Accounting and Budgeting Integration

Accrual accounting and budgeting should go together. Unless the budgeting system is on the same basis as the accounting system, the scope for mismanagement and a loss of financial control are considerably enhanced. There will be confusion about the meaning of information and the actual financial information about previous years' activities will always remain, for most operations, the basis of future budgets.

6.4. Outputs Over Inputs; Performance Over Control

There has to be a willingness to accept significant changes to the methods of control and the distribution of responsibility. The nature of control and budget making should also change in order to achieve the full benefits of accrual accounting and budgeting. The emphasis should be upon the control of outputs rather than inputs. Traditional controls may be relaxed in order to provide managers with the opportunity to manage effectively. A manager is not able to manage outputs unless he/she has relatively greater freedom over inputs, such as staffing and capital, than most public sector control systems presently allow. On the other hand, this also means more rigorous disciplines being exercised over managers who fail to deliver the performance expected. This degree of cultural change also requires investment in the training of managers and even the employment of those who have an entrepreneurial type ability. In turn, the system of check, most notably of internal control and external audit, needs review and strengthening.

6.5. Political Commitment and Perseverance

The introduction of accrual accounting and budgeting takes time. Unless there is a widespread intellectual and political acceptance of the desirability of introducing the reform, the risk is that, with a change of political control or of personalities, the reform will not be brought to fruition. The consequence would be most unsatisfactory and considerable investment would have been wasted.

6.6. No Gains Without Sacrifice

The nature of the change and the need for widespread intellectual acceptance requires broad initial discussion of the proposals to convince the responsible officials. They are the ones to operate and ensure the effective use of the system. In order to realise the benefits of the change, they may have to make difficult decisions. These decisions may include closing or reorganising operations, removing staff, changing delivery arrangements, introducing user charging and competitive and regulatory arrangements.

6.7. Ascendancy of Accounting

Considerable accountancy skills are required to introduce and maintain the system and proper processes of financial management. This will mean changes within the official administrative power structures and the growth in unaccustomed influence of accountancy which, as explained above, is not well understood at present. Where are these accountants to come from and will the public sector offer sufficiently good pay and conditions to attract and retain them? Substantial investment in training of existing administrative staff is also required to secure an understanding of the information being provided and the new management arrangements. This applies equally to the staff of the external auditor; otherwise the auditor will act as a 'drag' on progress.

6.8. Institutionalisation of Change

As the accrual accounting process is a dynamic one driven by both developments in accounting practice and the circumstances of government, a capacity is needed to ensure that there is a systematic arrangement to incorporate change into the accounting and reporting processes.

6.9. Information, Technology, Capability

Without an information technology (IT) capability, it will be difficult to assemble the information required and provide the information necessary for or efficient management of operations. More complex IT systems will be required than those associated with a traditional cash system.

Obviously the importance of these preconditions will vary from country to country. Those who are interested in the development of accrual accounting should consider how far these preconditions in a particular country should be met. If they are not met then the risk is that whilst technically it may be possible to introduce accrual accounting, there is the question as to whether the change is worthwhile in terms of achieving tangible benefits in the improvement of the management of the public sector. The latter should be the aim and concern should not be focussed on the technical change as an end in itself. However it should also be pointed out that the weakness of the European accountancy profession in terms of its commitment to the public sector in many European countries, may make it difficult for those countries to only make the change. If though the change is made there then remains the problem of ensuring that it both remains a dynamic process and is used to support improvements in the management of public sector resources (i.e. in assessing efficiency and effectiveness in the performance of public services).

7. SUMMARY

There is a European view to the development of public sector accounting standards. That view is essentially the view of a pragmatist rather than the view of one concerned to challenge the technical approach. The European view evolves from the history of the development of the European public sector.

However, another feature of the European public sector is that in most countries it is relatively distant from the accountancy profession. The influence of the profession is limited in most countries. This detachment has disadvantages to both governments and the profession and these disadvantages will become of more significance if the move to adopt accrual accounting becomes stronger.

Accrual accounting is as much about effective management as financial reporting and therefore the introduction should be accompanied by parallel reforms rather than being seen as an end in itself. This too perhaps creates opportunities for greater involvement by the profession in the public sector than has historically occurred. However, the profession itself has to recognise the implications of this for itself. In many countries, knowledge and interest in the public sector is very limited and at best seen through the limited eyes of the auditor. Again, professional training encourages that and reform or adaptation of professional training is likely to be an essential feature of a more determined involvement in the public sector by the profession.

Academics can act as a catalyst. However, to do so, they do need to move outside their traditional concerns for the technical aspects of accounting and into the more managerial aspects involving, not least, the development of techniques that will more closely link financial information and non market performance.

NOTES

[1] 'Proposal for a Regulation of the European Parliament and of the Council on the application of international accounting standards – COM (2001) 80.' This proposal after amendment was adopted by the European Parliament on 12 March 2002. It currently requires approval by the Council of Ministers.

[2] See FEE PSC paper published by CIPFA 1991, 'The Audit of Management – *Ideas from Germany.*'

[3] For a complete summary of the arrangements for state audit in the European Union see State Audit in the European Union, published by the national Audit Office 2001, available free of charge.

BERNARDINO BENITO LÓPEZ
ISABEL BRUSCA ALIJARDE
VICENTE MONTESINOS JULVE

THE IPSAS APPROACH: A USEFUL TOOL FOR ACCOUNTING REFORM IN EUROPE?

1. IFAC STANDARDS

Present characteristics of governmental accounting in Europe must be analysed against the background of the evolution that has been taking place in worldwide accounting harmonisation in recent years. To this end, special reference must be made to IFAC Public Sector Committee (PSC) work; various studies, guidelines and accounting standards have already been published, while other projects are still under way. The impact of of this work on international governmental accounting will no doubt be decisive. Other institutions are also working on governmental accounting, as is the case of INTOSAI, although their pronouncements have had a very limited influence.

In 1996 the IFAC-PSC embarked upon a project to develop a set of accounting standards for public sector entities referred to as the International Public Sector Accounting Standards (IPSASs) based on the International Accounting Standards (IASs) issued by the International Accounting Standards Board (IASB). The objective of the Committee was to develop programs aimed at improving public sector financial management and accountability including: developing accounting and auditing standards and promoting their acceptance, as well as encouraging and facilitating the exchange of information among member bodies and other interested parties.

Furthermore, IFAC accounting projects are closely co-ordinated with those of the IASB in the development of standards for business accounting. This gives pre-eminence to IPSASs over any other pronouncements on governmental accounting as the most effective way to build up international standards. The aim is not to divide efforts, but to focus them on a single set of pronouncements, with common roots with business international accounting standards issued by the IASB. Through the standards issued so far, the IFAC is extending the IAS to public entities, with some minimum adaptations to their particularities. This provides evidence of the interest in approximating the public accounting system to the business accounting system in such a way that homogeneity can be achieved both between the two types of entities and between the entities of different countries. It is an extremely important decision

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 85-97.

in the international context of public accounting, which has already been adopted by many regulating bodies at national level.

Together with the pressure of business accounting standards, another aspect of IFAC's harmonisation efforts must be highlighted, that of the pre-eminence of the Anglo-Saxon tradition. These two aspects are a logical result of IFAC's organic composition, of the cultural traditions most influential in its work and of the explicit objective of developing governmental accounting standards as close as possible to IASB business accounting standards.

These two main characteristics raise an essential question regarding the international harmonisation of governmental accounting standards: can or should the IFAC accounting principles and standards set up by IPSASs be considered as international generally accepted accounting principles? In our opinion, it is too early to make such an statement, since governmental practices and traditions are still highly divergent in the international context and in particular in the European context, as will be seen in the next section.

2. GOVERNMENTAL FINANCIAL REPORTING IN EUROPE

As in the case of business accounting, governmental accounting systems can be classified as Continental or Anglo-Saxon accounting systems. The Continental accounting tradition can be associated with the family of German and Roman legal systems, while the Anglo-Saxon accounting tradition is normally linked with the "common law" legal system family (see Salter and Doupnik, 1992).

Continental accounting systems have a macroeconomic basis, connected with a more bureaucratic design of accounting principles and standards, which public bodies have set up as legal or administrative rules. The main objective of financial statements within this tradition is the compliance with legal and administrative rules when reporting financial information. This is the case of Germany, France, Belgium, Spain, Italy and Portugal, in Europe, and most of the countries with economic influence in Latin-America, such as Argentina, Brazil, Chile and Colombia (see Montesinos and Vela, 1996; 2000).

In continental European countries, the budget has been traditionally almost the only element in governmental accounting and the influence of business accounting has been absent until recently. In the same way, accountability has not really been developed, as financial statements are prepared as a result of compulsory legal requirements. Hence, they are more oriented to inner departments of the public administration itself (accountability closed approach) than to a broader range of mainly external users (accountability open approach). Little attention has been paid to efficacy, efficiency and economy indicators. The external audit has not been sufficiently developed and in some cases, as in Spain (Montesinos, 2000), very few municipalities have a periodic external, independent audit (in fact, of all Spain's major cities, only Barcelona has an independent annual audit).

On the other hand, Anglo-Saxon accounting systems have a microeconomic basis, connected with a non-bureaucratic design of accounting principles and standards, set up by private professional accounting bodies. The main objective of financial statements is the faithful representation of the entities' economic and financial reality, in such a way that transactions and events are accounted for and presented in accordance with their economic substance and not merely their legal form. This is the tradition in the United Kingdom and Ireland in Europe, and the United States, Canada, Australia and New Zealand in the rest of the world.

Unlike the continental countries, the Anglo-Saxon European countries, and especially the United Kingdom, have reported to users in a more open way (open approach), which includes non-financial information. Business accounting has had an important influence. External independent audits have a very long tradition in these countries.

This duality in accounting models still remains, and if possible is even more pronounced among public entities than in the business field (see IFAC, 2000). Therefore, while globalisation in economies has intensely fostered the harmonisation of business accounting, European public administration accounting has not evolved correspondingly, and consequently, substantial diversity still exists.

Thus, a European governmental accounting model does not exist. The Continental and the Anglo-Saxon systems are therefore the two models we can describe in Europe, bearing in mind that only the basic characteristics are then taken into consideration when grouping the different systems into just these two models.

Although this harmonisation may be considered less important than in the case of business accounting, since the requirement for international markets information does not arise, in our opinion, other reasons support the relevance of governmental information comparability, especially for the countries belonging to the European Union.

Governmental accounting harmonisation can therefore generate similar outcomes to those of the business sector, as accounting diversity in public entities leads to a lack of comparability of financial information. This in turn, makes the interpretation of financial statements difficult, even for users with an awareness of accounting principles and practices and much more so for non-expert users of public entity financial reports.

The IFAC international public sector accounting standards (IPSASs) have now come onto the European stage in full force. At the end of the day, these standards are currently the most relevant factor in the realm of international accounting standards for public entities, as the other variables traditionally considered when analysing international accounting harmonisation have not really worked as a useful tool to approach public sector financial reporting in Europe.

3. THE IPSAS APPROACH AND THEIR ADOPTION INTO EUROPEAN ACCOUNTING SYSTEMS

The application of international accounting standards to the public sector could obviously contribute significantly to the provision of comparable, relevant and understandable financial information by European governments. However, to what extent are IPSASs really a useful tool now or will they become so in the near future, in the transformation of current governmental accounting systems?

In other words, although the efforts of the IFAC are of great importance, national governments actually need to adopt its standards. To this end, IFAC is developing an active policy towards national governments and international institutions to bring about real Government Generally Accepted Accounting Practices (GGAAP) and IPSASs identification in the medium term.

In carrying this out, several factors can affect the process, and various policies can be implemented, of which the following could be noted:

-Firstly, the world-wide economic, political and cultural influence of Anglo-Saxon countries.

-Public administration reform and the application of business management techniques contribute to extending the influence and prestige of business accounting practices.

-The knowledge and diffusion of IFAC accounting standards among international financial, economic and political institutions, such as the World Bank, the International Monetary Fund, the Interamerican Recovery and Development Bank, European Institutions, etc., make IFAC standards a clear and useful reference when requesting reliable financial information from countries and public entities. This is a powerful tool for gaining a certain influence on the evolution and reform of financial reporting in countries that benefit from financial aids or loans (especially underdeveloped countries), as well as on public entities audited by supranational audit bodies, such as the European Union (EU) Court of Auditors.

-The technical, organizational and cultural traditions of big public administration audit and consultancy firms are grounded in the business enterprise field. A consequence of this fact is that these firms tend clearly towards business accounting standards as the basic reference and framework for public sector entities. Indeed, this is precisely the methodology used in IPSASs development.

-Finally, IFAC work can make it easier for national governments to update their organizations and information systems. Even when a previous opposition to reforms exists, the availability of a broadly accepted set of accounting standards such as the IPSASs can contribute to overcoming this opposition.

The efficacy of the abovementioned factors and the pace at which IFAC standards are introduced will doubtless depend on the more or less decisive role that IASB standards play in the accounting policy of North-American financial markets. A decline in the role and influence of IASB standards would weaken IPSASs and would slow down their implementation, as they are closely linked to international business standards.

There are however, important stimuli for the updating of accounting systems at central, regional and local government levels, but these stimuli and factors of change do not work steadily and innovations often follow periods of deadlock. On the other hand, few stimuli can be detected which support the convergence of the European accounting systems. In the case of Anglo-Saxon countries, preconditions for adopting IPSASs are doubtless more positive, especially because of the world-wide influence of other countries with this cultural background which are working hard to promote the development of IFAC international standards.

4. A PARTICULAR CASE: THE ADOPTION OF IPSAS BY EUROPEAN UNION INSTITUTIONS

4.1 Accounting Principles and Financial Reporting in European Union Institutions

Budgetary information currently occupies a prime position in the information system, with the objective of demonstrating that the limits of expenditure established have been respected, as well as reporting the budgetary result. In addition, accounting information is prepared in order to enable an evaluation of the Commission's financial management and to make public the net worth of EU Institutions.

Before May 1st, the European Commission submits the Analysis of Financial Management, the Revenue and Expenditure Account and the Balance Sheet to the European Parliament and to the Court of Auditors.

The accounts are consolidated using the full consolidation method. They cover the accounts of the European Parliament (including the Ombudsman), the Council, the Commission (including the Publications Office and the Joint Research Centre), the Court of Justice, the Court of Auditors, the Economic and Social Committee and the Committee of the Regions. The operations that are not included in the Budget are not entered either in the Consolidated Revenue and Expenditure Account or the Balance Sheet, with the sole exception of the lending and borrowing operations.

Prior to November 30th, the Court of Auditors submits a Statement of Assurance (Declaration on the reliability of the accounts and the conformity with legal dispositions), which is published in the Official Journal of the European Communities.

Using the double-entry method the general accounts are prepared on the Modified Basis of Accounting, although it is becoming more similar to Full Accrual accounting. Specifically, the yearly balance is obtained by following the Modified Accrual Basis, as the general procedure is to record operations when the payment is made or the revenue is received, although appropriations carried over are considered as expenditure in calculating the balance for the year. However, the Balance Sheet shows the assets and liabilities of the European Union, including fixed assets.

Council Regulation (EC, ECSC, Euratom) No 2548/98 of 23 November 1998 which amended Financial Regulation of 21 December 1977 applicable to the general budget of the European Community (hereafter referred to as R/98) introduces the possibility of applying full accrual accounting. New accounts for non-budgetary revenue and expenditure are established and it requires the writing-off of assets. This full consideration of all revenue and expenditure is still to be further developed. Moreover, in the 1997 Accounts some value adjustments were made to certain assets.

According to the Regulation on Inventory and Management of the Property of the European Commission (hereafter referred to as Inventory Regulation) which came into effect on the 1st January 1997, the Commission must allow for depreciation of assets. Nonetheless, since depreciation is not compulsory for the other Institutions and with a view to presenting a consistent Balance Sheet, depreciation has not been included in the Annual Accounts. The 1999 Accounts only show the aggregated depreciation for the Commission, the Publications Office and the Court of Auditors.

As stated in the regulations, all financial accounts will be prepared according to the accounting principles, especially those laid down in the European Directives. The Commission sets down the way in which these principles are applied in practice.

The general accounts are based on the following principles: Going concern (i.e., continuity of activities), prudence, continuity of methods, no-netting between assets and liabilities.

4.1.1. Financial Statements and the Relationship between Financial and Budgetary Accounting

As in continental European accounting systems, accounting must allow for the calculation of the budgetary balance as well as the evaluation of the Comision's Management.

The Revenue and Expenditure Account is prepared under the Modified Cash basis of accounting, and the general criterion is to record operations when they are actually paid or money is received. However, assets and liabilities appear in the Balance Sheet, with fixed assets also being included.

Assets involve a budgetary expense on purchase, but they are entered in the Balance Sheet, using Own Capital as a contra-entry. This is the link between budgetary and financial accounting.

The budgetary balance appears as a yearly balance in the Balance Sheet. Since it has not been prepared on the Accrual basis, some adjustments have to be made to the Own Capital in order for the Balance Sheet to show all European Union assets and liabilities.

The Revenue and Expenditure Account shows the yearly budget balance, as well as the yearly breakdown of the revenue and expenditure. It is presented in the same way as the budget, and is also divided into the same parts. It shows the amounts for the closing year and the preceding year.

In 1997 the structure of the Balance Sheet changed to offer a more concise presentation. Headings were reclassified following the format in the IV Directive. Figures are given for the closing year and the preceding year. In the explanatory notes, more detailed information can be found on assets and liabilities.

As mentioned above, Council Regulation R/98 introduces new accounts for non-budgetary revenue and expenditure, thus allowing an Enlarged Accounting Result to be obtained. Adjustments are now made to the Own Capital heading in order to bring their variation closer to the total economic result for the year. The Enlarged Result comprises all these adjustments, i.e., part A (economic adjustments for value corrections) and part C (surpluses of loan proceeds over borrowing/lending costs) of the Own Capital heading. As a result, the Own Capital heading will have two components, the Accumulated Enlarged Result and the Budgetary yearly balance.

This Enlarged Result will be added to the budgetary result in order to obtain the "overall economic result" for the European Community. It should be borne in mind that the budgetary result includes the previous year's result as revenue, so in fact it is effectively an accumulated result.

The Commitments not included in the Balance Sheet are shown together with the Revenue and Expenditure account and the Balance Sheet. These commitments refer to potential liabilities and obligations. They include guarantees made or received, leasing and long-term rental commitments on the acquisition of tangible fixed assets, stock, foreign currency and potential liabilities.

The Financial Management Analysis is published together with the Revenue and Expenditure Account and the Balance Sheet. It sets out the salient features of budgetary implementation in the year. It indicates the economic situation in the European Union and the financial perspectives foreseen. All the income and expenditure items are described and their estimated evolution is indicated. The aims and objectives of the main Community policies are set out.

4.2. Weaknesses in the Current Accounting Model and the Need for Change

A critical analysis of the most important features of the accounting model used by the European Commission reveals certain weaknesses that need to be changed. For example, the use of the accrual basis for public administration financial statements within a consistent accounting framework in line with GAAP seems to have become a requisite feature in recent years. Most western countries are currently working on this. This, together with the Court of Auditors recommendations, requires a complete and consistent accounting framework to be formulated to eliminate the coexistence of two mutually incompatible accounting bases.

The European Court of auditors has highlighted the lack of comparability between the criteria applied and the financial statements prepared by European institutions. From the point of view of materiality, it is true that the European institutions' budget, with the exception of the Commission, is fairly irrelevant when seen as a part of the EU budget as a whole. However, that should not imply that the accounting information and control of these institutions ought not to be comparable to those of the Commission itself. There are several reasons for this: i) the democratic responsibility for the management of the institution and the rendering of accounts, ii) the self-motivation and identical behaviour as other public servants, and iii) the need to develop a culture of control and information transparency in EU organs.

The financial accounts prepared by the Commission have gradually come closer to the information content required by GAAP. Nonetheless, their structure and information content still has to be developed further to bring them in line with EU Accounting Directives and the proposals put forward by several international organisations. Among the latter, the International Federation of Accountants (IFAC) must be mentioned.

In fact, conscious of the problems that the present EU accounting system presents and the need to adapt it to the IPSASs of the IFAC, the Commission is presently working very hard to modernise its accounting information system in an attempt to put into effect the suggestions made by the European Court of Auditors in their latest reports. The Commission has expressly stated its interest in adopting the IPSAS.

4.3. Principal Changes for the Adaptation of European Union Institution Reporting to IPSAS

An analysis of the differences between the European Union accounting system and the IPSASs of the IFAC has enabled us to determine the nature of the changes that should be introduced in the EU model, if it is to be brought into line with the model recommended by the IFAC.

Firstly, a substantial difference arises with regard to the recognition criteria or measurement approach. Although the international organisation recommends the full accrual basis of accounting, the EU model still does not use it. Efforts have recently been made to move closer to it, but there is still a long way to go.

A mechanism must be established to account for all accrued revenues and expenditures, regardless of whether they have been collected or paid. The key issue here is to find a suitable link between budgetary information and financial accounting. The latter cannot be based only on budgetary revenue and expenditure. Council Regulation R/98 allows for the application of full accrual accounting and establishes new accounts for non-budgetary revenue and expenditure. It also provides for the writing-off of assets. This comprehensive consideration of all revenue and expenditure should be further developed.

No important differences have been detected in the other accounting principles, mainly because all those recommended by the IFAC have already been introduced into the EU system. Slight differences appear regarding the Principle of relative importance and data aggregation, because they are not explicitly stated. Nevertheless, we understand that both principles are applied in practice.

In the European Union the principles of legality and regularity are of utmost important. Indeed, the Court of Auditors must base its pronouncements on these two principles, as well as the reliability of the accounts. However, legality and regularity are not treated as principles as such within the international sphere although it is understood that annual accounts must prove compliance with the restrictions set down for funds management. This issue is especially relevant to all public administrations where funding comes from the taxpaying public as a whole, and to whom accounts must therefore be rendered on the proper use of those funds.

Recognition criteria and valuation rules used by European institutions do not differ substantially from those recommended by international standards or applied to governmental accounting in the most developed countries. Nevertheless, there are differences in some standards and accounting practices that may be significant for certain items (see Table 1).

Table 1. Comparison of recognition criteria and valuation rules

Items and operations	*EU criteria*	*IFAC criteria*
Fixed tangible assets	▪ Acquisition value ▪ Periodic revaluations	▪ Acquisition value ▪ Periodic revaluations, through reserves
Intangible assets	▪ Acquisition price ▪ Only compulsory for the Commission´s assets	▪ Acquisition price
Leasing	▪ Fixed Tangible Assets are recognised at the resale value or actual value of payments, and also recognise debts outstanding. ▪ Only compulsory for the Commission´s assets	▪ Fixed Tangible Assets are recognised at the resale value or actual value of payments, and also recognise debts outstanding.
Depreciation	▪ Only compulsory for the Commission. It is disclosed in the notes to the accounts.	▪ Recognition in the balance sheet and revenue and expenditure account for all the items included in the fixed assets, tangible and intangible assets with a limited useful life.
Long Term Assets	▪ Recognised at the claimed amounts value. ▪ A breakdown of the amounts granted is shown in the explanatory notes to the balance sheet	▪ Acquisition value, recognising the debts outstanding
Receivables	▪ Face value	▪ Face value
Own Capital	▪ Adjustment item linking budgetary accounting and financial accounting.	▪ The residual interest in assets that remains after deducting liabilities
Valuation Accounts	▪ Fixed Tangible Assets ▪ Intangible Assets ▪ Financial Investments ▪ Disposable assets ▪ Cash	▪ All the items included in the Assets side of the balance sheet, especially bad debt.
Advances and Payment by instalments	▪ They are treated as revenues and expenditures for the year with certain exceptions	▪ They are treated as items from the balance sheets (assets or liabilities)
Foreign currency	▪ Non realised gains appear in the balance sheet. Realised gains and losses are results for the year ▪ The budgetary balance includes realised gains and realised and non realised losses	▪ Result for the year

Consequently, the depreciation of fixed assets must be accounted for, i.e., tangible and intangible fixed assets of limited useful life. Accumulated depreciation will reduce the amount of fixed assets on the assets side of the balance sheet. Provisions regarding receivables must also be accounted for, so that the balance sheet shows the net amount of receivables, once provisions have been deducted.

The Own Capital item presents the most peculiar recognition criteria. These criteria should be aligned with generally accepted practice, so as to improve the clarity and comparability of its information content. A revision should be made with regard to the account showing adjustments to the result, because it does not really fit into place in the model we propose here.

The lack of comparability between the information rendered by different European Institutions should be pointed out, which is due to the diversity in accounting principles used. The assets acquired through financial leasing, and the non-existent accounting policies on the depreciation of fixed assets might be highlighted as the most significant examples of this defect.

It should be reiterated that budgetary information is of paramount importance within the annual account of the European Union, which is not normally the case in the international context. Although budgetary information has been of great importance in the public accounting system of all countries, this kind of information is gradually giving way to the more robust position of financial accounting. In this context, we think that the budget has and will continue to play a vital role in EU finances. We therefore consider that any accounting system must include and link budgetary and financial accounting.

In the consolidated accounts, we follow the criterion of a single budget in order to set the consolidation perimeter. Only the basic institutions are included in the consolidated accounts. According to international standards, the criterion is the existence of control, and consequently the policy employed up to now should be revised to include all the decentralised entities which are under the control of a basic institution. The method used is full consolidation, which is the right one for the entities in which decisions are under the mother institution's control.

There is no doubt that the Budgetary Revenue and Expenditure Account must be included as a component of the accounting statements that the Commission is obliged to file with the Court of Auditors. In fact, the IFAC itself recommends disclosure of information that may prove the compliance with the restrictions imposed on public administrations.

The balance sheet presented at the moment is rather similar to that preferred internationally, since more or less the same items are disclosed. Nevertheless, a large number of data and informations are introduced as Off-Balance Sheet items, which allows for a format which looks like the one we would obtain if full accruals were used, yet with some peculiarities. Hence, some accrued revenues and expenditures, together with depreciation have still not been registered. Moreover, this way of calculating the amounts can lead to misunderstandings, especially in the Own Capital item. The meaning of Own Capital can be decidedly jeopardised by the application of so many corrections.

The chief consequence of not using a full accruals model is the absence of the income statement. It is true that the annual economic result has a very different meaning in the context of public administration. Nevertheless, this has not led to the suppression of the income statement as an annual statement. Indeed, all the countries that use full accruals include this statement in the annual accounts. The IFAC and INTOSAI also share this view, and encourage the presentation of an income statement showing the annual revenue and expenditure, as well as the result for the year, making a distinction between ordinary and extraordinary results.

The presentation of the revenues and expenditures in the Budgetary Revenue and Expenditure Account is necessary but not enough, since apart from these items, some other non bugetary elements may exist, as a result of full accruals. The inclusion of this information in the accounting system will prevent any further adjustments off-balance being made, which will imply higher reliability of financial information. In short, we would like to see a statement that links the Financial Balance Sheet and the Budgetary Revenue and Expenditure Account. The Court of Auditors itself has also advocated this position and recommends its presentation.

A cash-flow statement should also be presented within the consolidated accounts. At present it is not required, although the Commission does prepare one. The cash-flow statement is important in that the entity's cash availability and its ability to generate cash flows must be known. Moreover, the presentation of payments and collections is not sufficient as they should be classified in line with international trends. A distinction should be made between cash flows arising from operating activities, investing activities and financing activities.

A further statement recommended by international standards is that showing the Variation in Own Capital, which is to a certain extent, presented by the European Union now, in a note to the Balance Sheet regarding Own Capital. In this note, Own Capital is broken down to show the variation of its components produced during the year, i.e., initial balance, change and final balance.

In this respect, the main difference from the international trends is in the items that belong to Own Capital, because of how the amounts are obtained. In addition, only the net variations are now shown whereas the international trends show all the increases and decreases in the Own Capital components.

Finally, the accounting regulation in the European Union does not require notes to the accounts to be presented, although in 1997, the Court of Auditors recommended that they be presented. As a result of the adaptation of the balance sheet to the model set out in the IV Directive, notes to the balance sheet are now formulated and disclosed. Nonetheless, some differences remain with regard to the notes currently presented by the European Union, such as those on income, expenditure and cash flows.

5. CONCLUDING REMARKS

In seeking to improve government accountability, the IFAC Public Sector Committee has undertaken a multi-year initiative to develop a series of recommended public sector accounting standards. The standards are applicable to all levels of government and are intended to provide governments around the world with a platform on which to base improvements in their financial management and reporting practices.

Nevertheless, at the moment it can be concluded that diversity in governmental accounting is still fairly significant in Europe and very much more entrenched than in the business accounting field. Different political, economic and cultural traditions give rise to great diversity between national governments and even between regions and local authorities in the same country. These differences also lead to opposition to reforms, and consequently the changes which must be made to accounting reporting appear to be of great importance.

The IPSAS perhaps provide an opportunity for European Accounting, and in future, national governments should attempt to adapt their accounting systems to the IPSAS. Perhaps it will be easier for Anglo-Saxon countries than for European continental countries, given the characteristics of the standards. In any case, the efficacy of the pace of implementation of IFAC standards will doubtless depend on the more or less decisive role that IASB standards play in the accounting policy of North-American financial markets. A decline in the role and influence of IASB standards would weaken IPSASs and would slow down their implementation, as they are closely linked to international business standards.

In this context, the position of EU Institutions is quite relevant, especially in the case of the Commission, which essentially represents the executive power in the Union. It is likely that accounting in European Institutions will soon be reformed according to IPSASs requirements, bearing in mind the advice and recommendations of the European Court of Auditors. In this sense, we believe that this could have an impact on the national governments of the member countries. Indeed, the Commission may benefit from higher credibility in order to undertake a process of harmonisation of public sector accounting and budgetary information within the European Union.

During the last few years, substantial efforts have been made by the European Commission to approximate its accounting policies to international standards, following the advice and requirements of the Court of Auditors. Nevertheless, further steps must still be taken before the final objective of this reform can be achieved, i.e., the introduction of an accounting model based on full accrual.

Moreover, as is the case of the Western continental countries(,) where there is a long tradition of the importance of the administrative procedures, within the European Union the budgetary information is also especially relevant. This means that budgetary accounting must be included as a subsystem of the general system accounting, with financial accounting being the other subsystem. Data from financial accounting must be properly connected to budgetary accounting. In fact, reconciliations between these two magnitudes may be of substantial interest, especially the reconciliation between the budgetary balance and the financial result for the year.

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Mª TERESA BALAGUER COLL
ILUMINADA FUERTES FUERTES
MANUEL ILLUECA MUÑOZ

HARMONISING THE ACCOUNTING SYSTEMS OF EUROPEAN LOCAL GOVERNMENTS: THE IMPORTANCE OF ENVIRONMENTAL CONVERGENCE

1. INTRODUCTION

Recent years have witnessed deep reforms in the accounting systems of the European local governments (LG). In general terms, the different countries have decided to introduce the accrual accounting. In that sense, the reforms have become the first stage of a harmonising process, which is still incipient but surely irreversible, given the process of economic and monetary integration that the European countries have been undergoing for decades.

Actually, the main problem of the accounting harmonisation lies in determining the speed at which the process must progress. With respect to this question, there are two options. The first consists in replicating the model that was used at the time in the European Union to harmonise business accounting. This would require designing common accounting standards that would have to be assumed by the member states of the European Union in the short term. As opposed to this possibility, there exists a second alternative, which consists in dividing the harmonisation process into two stages. First, neighbouring countries with similar models of local administration would harmonise and, in the second stage, which would be implemented once the European countries achieved a greater degree of economic integration, the harmonisation process would be culminated by devising a single accounting model.

To be able to opt for one alternative or another, it is necessary to take into account the different interests that hide behind the harmonisation processes. In this regard, as opposed to what happens in the private sector, the external users of the governmental accounting do not exert any pressure to accelerate the harmonisation process. After all, the operations of the local governments lack international scope and, therefore, neither the supranational organisms, nor the potential lenders, nor even public opinion need to compare the accounts of local governments that operate in different countries. In these conditions, the speed of the harmonisation process will depend, not only on the political will of the nations involved, but also on the

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 99-113.

resistance to change of the local governments themselves. Undoubtedly, the resistance would be less if the political, economic and cultural differences that characterise the European countries waned. Without them, it would be easier to design a common accounting system that all the countries involved in the harmonisation process accepted as their own. From this perspective, the harmonisation of the accounting and the convergence of the environments are closely related in this case.

Accordingly, the main purpose of this paper consists in identifying the pattern of convergence of the environments that characterise the different European local governments. Specifically, our study tries to determine whether an absolute convergence is evolving towards a common European environment, or if, contrarily, convergence is only proceeding in specific geographical areas, each made up of a small group of politically, economically and culturally akin nations. In the event of absolute convergence, it will be simpler for the harmonising process to advance, designing a single accounting system that could be accepted by all in the short term. In contrast, if the convergence of environments is limited to specific geographical areas, it will be better to start with regional harmonisation that will lead to a common accounting system in the medium term.

Unfortunately, we have not been able to analyse the whole list of variables that characterise the environment, simply because many of them are not quantifiable and others, in spite of being quantifiable, are not systematically measured by any international organism. Accordingly, it has been necessary to focus on those economic aspects directly related to the model of local administration existing in each country. Specifically, our study has focused on three key variables related to the economic activity of local governments: their per capita expenditure, their degree of autonomy and their deficit.

The rest of the paper is structured as follows. In the second section, we justify the selection of the three indicators just mentioned, based on the literature published on this matter. In the third section, we describe the database used and include some descriptive statistics of the variables analysed. The fourth section presents the methodology used for the analysis of the convergence, based on Quah's contributions [1993]. The results derived from the empirical study are analysed in the fifth and sixth sections. Specifically, in the fifth section, we test whether the indicators converge at the European level, while, in the sixth, we check whether or not there is convergence at the regional level. Finally, the seventh section presents the main conclusions of the paper.

2. HARMONISATION AND ENVIRONMENTAL CONVERGENCE: BACKGROUND

The role played by the environment as a cause of the differences between the accounting systems has been analysed quite assiduously within International Accounting, albeit more in the sphere of business accounting than in that of governmental accounting. Generally, the studies follow two different approaches: a deductive approach [Mueller, 1968; Previts, 1975; Nobes, 1983] and an inductive one [Da Costa et al., 1978;Frank 1979; Nair & Frank, 1980; Amenkhienan, 1986].

The deductive approach consists in identifying the main factors of the environment and relating them with the way in which the accounting systems have been developing in the different countries. In turn, the studies that follow an inductive approach use empirical methods to test whether or not a direct relationship exists between the factors of the environment and the distinctive features of the nations' accounting systems. Independently of the approach adopted, none of the studies question the importance of the environment as a determinant of accounting diversity. What is more, the environment not only conditions the way in which the information is produced but also how it is interpreted.

Accordingly, the relationship that links the convergence of the environment and harmonisation is no more than the corollary of the results presented in all these studies. If the environment explains the differences that exist among the accounting systems, the convergence of the environment will facilitate harmonisation and the speed of the convergence will determine the pace of the process. Therefore, the fundamental problem facing us is not theoretical, but rather operational. To analyse the convergence of the environment requires having periodical information available on all the political, cultural, social and economic variables that are related to it.

Since, in practice, this exercise is impossible, because some variables cannot be quantified or, simply, because no organism provides periodical data on them, we decided to focus on the economic aspects of the environment and, specifically, on those directly related to the information needs of the internal users of accounting. The indicators finally selected were three: the per capita expenditure of the local governments, their degree of autonomy - grants/total revenue - and their deficit - total expenditure / total revenue -.

The per capita expenditure largely explains the degree of complexity of the management of a local entity. The fewer the resources available, the simpler the management and the smaller the volume of necessary information to carry it out. Insofar as this ratio tends to converge, it is logical to think that the appropriate management solutions or strategies will be more similar to each other and it will be easier to initiate the harmonisation process.

The local authority's degree of financial autonomy conditions the amount of control that the central government exercises on the local governments and, therefore, its influence on the objectives of the public accounting information. As the autonomy of the local governments increases, their direct accountability to the society increases, as well as their concern for having a suitable information system to empower their decision-making.

This is reflected in the unequal orientation that the accounting reforms in Scandinavia have followed. While the Swedish and Finnish accounting reforms have responded to the need to improve efficiency and effectiveness, in Norway, the reforms focused on satisfying the central government's demand for greater control of local finances. Monsen and Näsi (1996) attribute this circumstance to the fact that the Finnish and Swedish local governments have historically enjoyed greater financial autonomy than those of Norway.

Accordingly, insofar as the degree of autonomy tends to converge, the objectives of the public accounting information will tend to come closer and it will be simpler to devise a single accounting system that satisfies the set of countries that make up the European Union.

Lastly, the third environmental variable to be analysed in this study is the local governments' deficit. The relationship of this variable with management practices has been analysed with relative frequency in the sphere of governmental accounting. Some studies suggest that the greater the social awareness of the need to reduce the deficit and indebtedness, the more prone the local authority will be to adopt management strategies that allow efficient allocation of the resources [Lüder, 1994]. Obviously, the implementation of these strategies, which are part of the New Public Management, require reorientation of the accounting information system, in order to be more useful for management decision-making.

Therefore, as the reduction of the deficit gradually builds a common management objective for the European local governments, the design of the accounting systems will evolve in the same direction. In this regard, we have tested in this paper whether the deficit of the LG with a greater tendency to indebtedness has been converging over time with that of those that have always felt the need to adjust their expenditure to the resources available.

3. DATA

In view of the objectives of the study, we have used statistical information from the International Monetary Fund corresponding to the period 1978-1995. This institution provided us with individualised budget data of the European Union countries for the whole period considered, except Greece (which had to be excluded from the sample), Italy -- for the periods 1978-1984 and 1990-1994 -- and Portugal, the data of which are not available from 1978 until 1987.

To facilitate the analysis of convergence, we decided to transform the indicators by dividing them by their annual average. Accordingly, in table 1, which presents the descriptive statistics of the variables, the arithmetic mean does not appear because, by definition, it equals 1. Table 1 reveals that the indicators are not always distributed like normal variables. The variables display a high degree of asymmetry.

Table 1: Descriptive statistics (1978-1994)

	Std	Asymmetry	Kurtosis
Per capita expenditure	0.73	1.25	3.56
Autonomy	0.46	0.38	2.17
Deficit	0.05	0.41	3.38

4. METHODOLOGY

Given the non-normality of the indicators, we used the empirical approach suggested by Quah [1993] to test whether or not there is convergence between the different countries under study. This approach focusses on the evolution over time of the entire cross section distribution of the indicators. This evolution involves two kinds of dynamics occurring simultaneously: changes in the exterior shape of probability density functions (PDF) and intra distribution mobility.

4.1 The Exterior Shape Of Probability Density Functions

The most intuitive way to see if there is convergence in a specific indicator consists of checking if the probability density function (pdf) tends to be concentrated at a single point over a period of time. In order to show this, density functions of indicators at different moments in time must be estimated. Obviously, if the indicators are distributed as normal variables, it is sufficient to observe the evolution of their standard deviation in order to monitor whether or not the observations are found to be getting closer to the mean [Barro and Sala-i-Martin, 1992].

However, a prior analysis of the descriptive statistics of the indicators reveals that the variables analysed in this study are not normal. Their marked asymmetry, together with their scarce kurtosis could constitute evidence of multimodality. In these conditions, even distributions of four parameters such as Fisher's Beta or the Ramberg Schmeiser distribution proposed by Lau, et al. [1995], could be inadequate to monitor whether or not the pdf tends to be concentrated at one point over time. In this situation, Quah [1993] proposes estimating the density functions of the indicators using non parametric techniques.

To be precise, the estimation is based on the technique known as kernel smoothing which consists of estimating density functions of the following type:

$$\overline{f}(x) = \frac{1}{nh} \sum_{i=1}^{n} k\left(\frac{x - x_i}{h}\right), \tag{1}$$

where n is the number of observations, x_i are the different sample observations of the x variable, h is the smoothing parameter and k is the kernel function.

In this study, we have estimated the density functions of the indicators for three different periods: 1978-1983, 1984-1989 and 1990-1995. Looking at the density estimates is very intuitive but the distributions are just point estimates for the sample period and cannot be assumed to reflect out-of-sample patterns. To cope with this problem and test whether or not the current process leads to a long-term convergence, it is necessary to consider the intradistribution mobility.

4.2 Intradistribution Mobility And Ergodic Distribution

Assuming that λ_t is a measure of probability associated with the distribution of a variable in a particular year, the simplest probability model which describes the transition from one year to another is:

$$\lambda_t = T^*(\lambda_{t-1}, u_t), \tag{2}$$

where u_t is a random variable and T* is an operator that encodes information on the changes from t to t+1 at the relative positions of the individuals analysed. If we ignore the random disturbance and we iterate [Quah, 1996], it is possible to write:

$$\lambda_{t+s} = T^* * T^* * ... * T^* \lambda_t = (T^*)^s \lambda_t. \tag{3}$$

This expression would allow us, when s tends towards infinite, to characterise the ergodic or long term distribution as a specific indicator from the annual transition matrixes onwards.

Actually, transitions do not necessarily have to be annual. A year can be an excessively short period to capture certain economic phenomena. In fact, it is customary to complete the analysis by considering the transitions that occur over a longer period. Accordingly, in this study, we have considered three types of transitions: annual, from t-1 to t; and quinquennial, from t-5 to t.

In order to estimate the annual transition matrix T* and the ergodic distribution, the space E of the possible realizations of the indicators must be divided into r states. In this way, T* can be estimated, by calculating the Q matrix (rxr) which includes the probabilities of passing from one state to another each year.

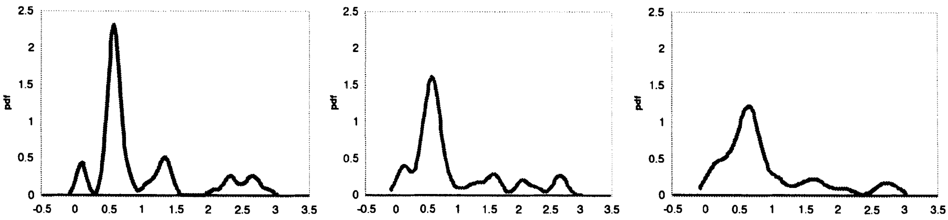
Usually, the stationary states are defined so that the probability of a country pertaining to each of them is identical and equal to 1/r. In this context, long-term convergence appears if the ergodic distribution attributes a probability greater than 1/r to the central stationary states. Divergence appears if they are attributed a probability of less than 1/r.

5. HAVE ENVIRONMENTS TENDED TO CONVERGE IN EUROPE?

5.1 Per capita expenditure

Per capita expenditure is an indicator of the degree of complexity of the action of local governments, which, among other aspects, depends on the amount of competences that they assume and on the relative wealth of the nation in which they carry out their activity. If countries converge in terms of this indicator, the information needs of their local governments are more likely to tend to converge and, therefore, it is easier for them to be willing to assume a single accounting system.

The results corresponding to this indicator are displayed in graphs 1 and 2 and in table 2. Specifically, graph 1 shows the evolution of their density function over time. It clearly shows that the volume of resources available to the local governments in Europe is very different. After all, in the three sub-periods analysed, 1978-1983, 1984-1989 and 1990-1995, there are serious indications of multimodality.



1978-1983 *1984-1989* *1990-1995*

Graph 1: Per capita expenditures. Probability density functions.

The results displayed in graph 1 show that the disparity does not seem to diminish with time. In fact, instead of diminishing, the multimodality tends to expand as we approach the end of the period. The individuals seem to shift from the mean towards the distribution tails.

Table 2: Per capita expenditures. Transition matrices.

Annual

Stationary states	1 0.51	2 0.62	3 0.74	4 1.46	5 ∞
1: 42	**0.93**	0.07	0.00	0.00	0.00
2: 43	0.07	**0.77**	0.14	0.02	0.00
3: 43	0.00	0.16	**0.74**	0.09	0.00
4: 43	0.00	0.00	0.07	**0.88**	0.05
5: 43	0.00	0.00	0.00	0.02	**0.98**
Ergodic distribution	**0.12**	**0.13**	**0.13**	**0.21**	**0.42**

Quinquennial

Stationary states	1 0.51	2 0.61	3 0.70	4 1.55	5 ∞
1: 31	**0.81**	0.06	0.06	0.06	0.00
2: 32	0.16	**0.41**	0.25	0.19	0.00
3: 31	0.16	0.16	**0.48**	0.19	0.00
4: 32	0.03	0.06	0.13	**0.63**	0.16
5: 32	0.00	0.00	0.00	0.13	**0.88**
Ergodic distribution	**0.22**	**0.09**	**0.13**	**0.25**	**0.32**

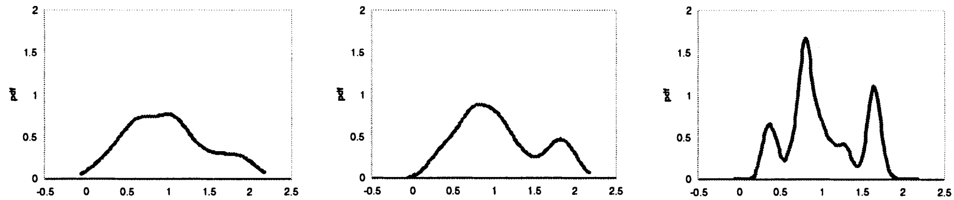
The intra-distribution analysis confirms these results. The quinquennial transition matrix, shown in table 2, does manifest the divergent tendency detected when analysing the evolution of the density functions over time. The ergodic distributions indicate that, long term, the probability tends to shift towards the distribution tails, which would accumulate, more than 50% of the probability.

In short, our results reveal that, throughout the period considered, the local governments' expenditure has not exactly tended to converge. Quite the contrary, our results suggest that there may exist a divergent process.

5.2 The Degree Of Autonomy

The second indicator analysed refers to the degree of autonomy of the local governments. For the reasons described above, the smaller the weight of the grants and greater, therefore, the autonomy of local governments, the more they will strive for efficiency and effectiveness.

Graph 2 shows the density functions of the 'transfers / revenue' indicator for the periods 1978-1983, 1984-1989 and 1990-1995 respectively. The figures show that the density function of the indicator is essentially multimodal. This circumstance reveals that in Europe there exist different models of funding local governments, which, in light of graph 3, have not tended to come closer over these last twenty years. Quite the contrary, the indicator seems to accentuate its multimodality even more in recent years.



1978-1983 *1984-1989* *1990-1995*

Graph 2: The degree of autonomy. Probability density functions.

The conclusions deriving from the estimation of the density functions at different points in time are confirmed with the analysis of the intra-distribution movements. The annual transitions, displayed in table 3, show that the countries change quintiles relatively little from one year to another. In fact, the ergodic distribution suggests neither convergence nor divergence in the long term.

Table 3: The degree of autonomy. Transition matrices.

Annual

Stationary states	1 0.65	2 0.82	3 1.05	4 1.45	5 ∞
1: 42	**0.95**	0.05	0.00	0.00	0.00
2: 43	0.02	**0.79**	0.19	0.00	0.00
3: 43	0.00	0.16	**0.70**	0.14	0.00
4: 43	0.00	0.00	0.16	**0.79**	0.05
5: 43	0.00	0.00	0.00	0.02	**0.98**
Ergodic distribution	**0.09**	**0.18**	**0.21**	**0.18**	**0.35**

Quinquennial

Stationary states	1 0.60	2 0.81	3 1.05	4 1.40	5 ∞
1: 31	**0.87**	0.06	0.06	0.00	0.00
2: 32	0.03	**0.69**	0.28	0.00	0.00
3: 31	0.00	0.29	**0.48**	0.16	0.06
4: 32	0.00	0.00	0.34	**0.50**	0.16
5: 32	0.00	0.00	0.00	0.16	**0.84**
Ergodic distribution	**0.06**	**0.25**	**0.25**	**0.17**	**0.27**

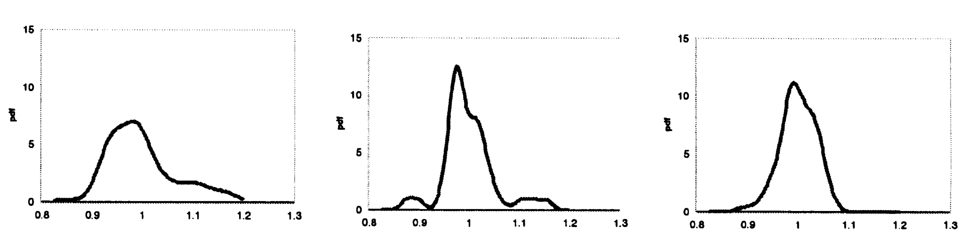
Nevertheless, as we increase the period of analysis, it is possible to see deeper intra-distribution movements. The dynamics implied in the quinquennial transition matrix leads autonomy ratio towards divergence and bipolarisation. The ergodic distribution estimated through quinquennial transition matrix reveals that, in the long term, 31% of the nations would end up in the first and second stationary state and 27% in the fifth.

In short, the analysis of financial autonomy reveals that the models of funding European local governments have not tended to converge in recent years either. Therefore, this variable has not stimulated harmonisation of the public accounting systems.

5.3 Public Deficit

The greater the need to reduce public deficit, the greater are the incentives for reforms that allow a more effective and efficient use of the resources. The implementation of these reforms entails redesigning the accounting objectives, which must provide the managers with the data necessary to execute the proper strategies. Logically, if all the countries are aware of the need to reduce the public deficit, it is easier for accounting reforms to advance in the same direction. In short, it is easier for the harmonisation process to take place.

Graph 3 presents the density functions of the expenditure / revenue indicator for the sub-periods 1978-1983, 1984-1989 and 1990-1995. The preliminary analysis of the density functions reveals, as we approach the decade of the 90s, a slight shift of the probabilistic mass from the distribution tails towards the central values, evincing the existence of a convergence process. This same result appears with greater clarity when we incorporate intra-distribution movements into the analysis.



1978-1983 *1984-1989* *1990-1995*

Graph 3: Public deficit. Probability density functions.

Certainly, the annual transition matrix - table 4 - does not show a convergence process in deficit. Once again, a single year is an excessively short period to observe convergent or divergent tendencies in the indicators considered. Nevertheless, as we increase the period of analysis, convergence appears with greater clarity. The analysis of the quinquennial transitions reveals that the individuals tend to shift towards the central values of the distribution. In fact, the estimation of the ergodic or long term distribution, shows that 28% of the countries would end up in the fourth stationary state, which is precisely where the mean value of the distribution is located.

Table 4: Public deficit. Transition matrices.

Annual

Stationary states	1 0.97	2 0.98	3 1.00	4 1.03	5 ∞
1: 42	**0.55**	0.24	0.12	0.07	0.02
2: 43	0.16	**0.44**	0.16	0.14	0.09
3: 43	0.12	0.21	**0.35**	0.21	0.12
4: 43	0.07	0.12	0.26	**0.35**	0.21
5: 43	0.05	0.02	0.09	0.23	**0.60**
Ergodic distribution	**0.18**	**0.20**	**0.19**	**0.20**	**0.22**

Quinquennial

Stationary states	1 0.96	2 0.98	3 1.00	4 1.03	5 ∞
1: 31	**0.16**	0.32	0.26	0.19	0.06
2: 32	0.13	**0.25**	0.25	0.16	0.22
3: 31	0.19	0.23	**0.16**	0.26	0.16
4: 32	0.00	0.13	0.22	**0.38**	0.28
5: 32	0.09	0.16	0.13	0.31	**0.31**
Ergodic distribution	**0.10**	**0.20**	**0.20**	**0.28**	**0.23**

Therefore, independently of the resources managed and of the way of financing them, the reduction of the deficit has constituted one of the priority objectives of the local governments. They have been compelled to improve efficiency and effectiveness in local management to continue providing the society with the same services using less resources. Since the search for efficiency in management has constituted a shared objective for the European LG, it is not surprising that the accounting reforms have followed a common direction.

Neither is it strange, however, that, after the reforms of the 90s, there are still important differences in Europe with respect to the accounting of the local governments. Very different models of local administration still exist. They are bound to require different information systems. Far from converging, both the per capita expenditures as well as the degree of autonomy have tended to diverge.

6. EUROPEAN CONVERGENCE OR REGIONAL CONVERGENCE?

Instead of converging towards common economic characteristics, each country's models of local administration may be converging towards the specific characteristics of the regions they belong to. In this section, we aim to verify this possibility, analysing the convergence of the conditioned indicators, which are obtained by dividing the indicators of the countries by the annual average of their respective regions.

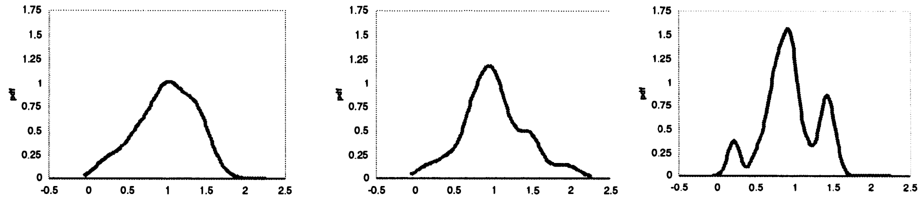
To carry out the proposed analysis, we decided to classify the countries in four large regions, following criteria of geographical, cultural and economic proximity. The result of the classification is displayed in table 5.

Table 5. Regions designed for the analysis of conditioned convergence.

Region 1	Region 2	Region 3	Region 4
Ireland, Netherlands United Kingdom	Denmark, Sweden Finland	Germany, Austria, Luxembourg	Belgium, Spain, France, Italy, Portugal

6.1 Per Capita Expenditure

Graph 4 displays the density functions of the per capita expenditure conditioned by the regional mean. Although, the density function gradually becomes multimodal, as we approach the decade of the 90s, an increasing number of nations cluster in the central values of the distribution. Therefore, everything seems to indicate that the countries tend to converge towards the mean of their own regions.



1978-1983 *1984-1989* *1990-1995*

Graph 4: Per capita expenditures. Conditioned probability density functions.

The results of this analysis are confirmed when we analyse the transition matrices of the conditioned indicator - table 6; particularly those that refer to the quinquennial and decennial transitions. Indeed, although the annual transition matrix reveals that, over the period of a year, hardly any changes occur in the relative positions of the countries, the quinquennial transitions confirm that the individuals tend to shift from the tails towards the central values of distribution. In fact, if we extrapolate the implied dynamics in the quinquennial transitions, more than 60% of the European countries will find themselves in two of the three central stationary states in the long term.

In short, in spite of the fact that the per capita expenditure of the LG is not tending to converge in absolute terms, there does seem to exist a convergence process at the regional level. Insofar as the per capita expenditure constitutes an indicator of the complexity of municipal management, our results indicate that the information needs of the local governments tend to be homogenous within the regions defined in this study, but heterogeneous in the broader scope of the European Union.

Table 6: Per capita expenditures. Conditioned transition matrices.

Annual

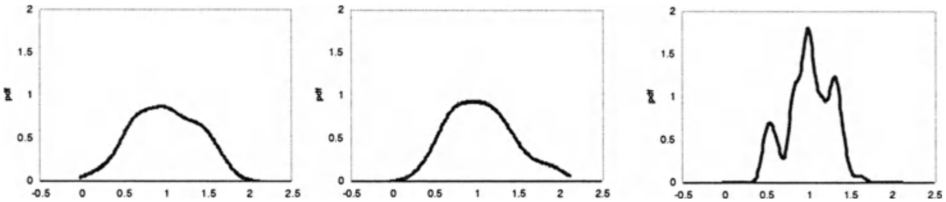
Stationary states	1 0.71	2 0.92	3 1.04	4 1.34	5 ∞
1: 42	**0.83**	0.17	0.00	0.00	0.00
2: 43	0.12	**0.74**	0.14	0.00	0.00
3: 43	0.00	0.16	**0.74**	0.09	0.00
4: 43	0.00	0.00	0.12	**0.81**	0.07
5: 43	0.00	0.00	0.00	0.07	**0.93**
Ergodic distribution	**0.18**	**0.25**	**0.22**	**0.17**	**0.17**

Quinquennial

Stationary states	1 0.70	2 0.93	3 1.06	4 1.31	5 ∞
1: 31	**0.65**	0.35	0.00	0.00	0.00
2: 32	0.16	**0.50**	0.28	0.06	0.00
3: 31	0.00	0.42	**0.39**	0.19	0.00
4: 32	0.00	0.16	0.31	**0.38**	0.16
5: 32	0.00	0.00	0.00	0.22	**0.78**
Ergodic distribution	**0.16**	**0.36**	**0.24**	**0.15**	**0.10**

6.2. Degree of autonomy

Graph 5 presents the density functions of the conditioned indicator corresponding to the degree of autonomy. It is easy to see that the PDF again tends to concentrate in the central values of the distribution although, as occurred with the per capita expenditure, it tends to accentuate the multimodality of the variable as we approach the decade of the 90s.



1978-1983 *1984-1989* *1990-1995*

Graph 5: Degree of autonomy. Conditioned probability density functions.

The convergence process of the degree of autonomy is confirmed when analysing how the countries shift within the probability distribution with time. The transition matrices included in table 7 show that the countries tend to group in the central stationary states in the long term. If we extrapolate the dynamics implied in the transitions, approximately 50% of the countries would end up, in the long term, on a bracket of ±0.1 around the mean. Contrarily to what has been happening throughout the study, the three transition matrices lead to similar results. In this case, convergence is observed even when analysing the annual transitions.

Table 7: Degree of autonomy. Conditioned transition matrices.

Annual

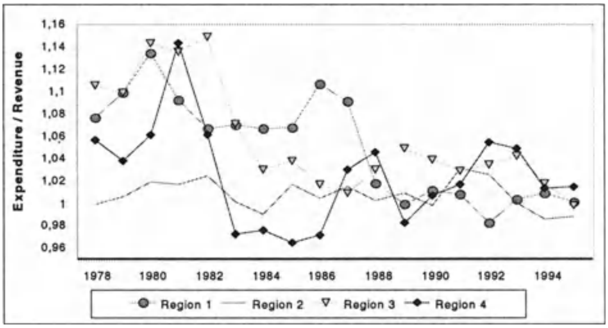
Stationary states	1 0.69	2 0.94	3 1.08	4 1.32	5 ∞
1: 42	**0.88**	0.12	0.00	0.00	0.00
2: 43	0.12	**0.77**	0.09	0.02	0.00
3: 43	0.00	0.07	**0.74**	0.19	0.00
4: 43	0.00	0.00	0.21	**0.72**	0.07
5: 43	0.00	0.00	0.00	0.09	**0.91**
Ergodic distribution	**0.15**	**0.16**	**0.26**	**0.25**	**0.19**

Quinquennial

Stationary states	1 0.68	2 0.88	3 1.08	4 1.32	5 ∞
1: 31	**0.65**	0.32	0.03	0.00	0.00
2: 32	0.19	**0.53**	0.25	0.03	0.00
3: 31	0.00	0.10	**0.52**	0.39	0.00
4: 32	0.00	0.09	0.34	**0.44**	0.13
5: 32	0.00	0.00	0.00	0.38	**0.63**
Ergodic distribution	**0.10**	**0.19**	**0.31**	**0.29**	**0.10**

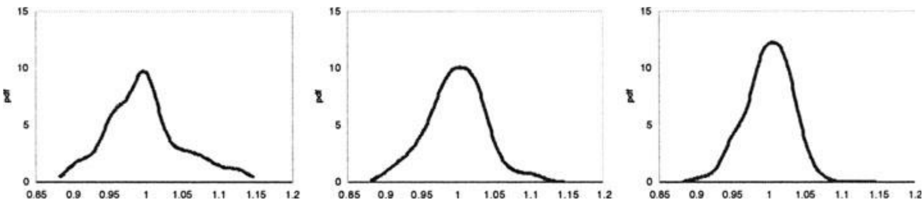
6.3. Deficit

Lastly, this third subsection presents the results corresponding to the deficit-conditioned indicator. This section clearly shows that the deficit of the LG tended to diminish and that a convergence process accompanied that decrease. This process is observed in graph 6, which illustrates how the deficit of the four zones tended to diminish and, of course, to converge. Our objective now consists in contrasting whether, besides convergence among the different zones, there has also been a convergence process in deficit within them.



Graph 6. Deficit of the European local governments. Evolution by regions.

Graph 7 includes the evolution of the deficit density functions over time, conditioned to the average values of the different regions. The different figures show how the density function is increasingly pointed, confirming that the deficit of LG gradually tends to converge towards the average of the regions in which they are located. This circumstance is even more evident when the intra-distribution movements are analysed, particularly when the analysis window covers a period of five years. Table 8 includes the annual and quinquennial transition matrices and the corresponding ergodic distributions. The results deriving from the quinquennial transitions predict that the deficit of 60% of the countries will end up, in the long term, in an interval of five percentage points around the mean of their respective regions.



1978-1983 *1984-1989* *1990-1995*

Graph 7: Public deficit. Conditioned probability density functions.

Table 8: Degree of autonomy. Conditioned transition matrices.

Annual

Stationary states	1 0.96	2 0.99	3 1.01	4 1.03	5 ∞
1: 42	**0.50**	0.21	0.17	0.05	0.07
2: 43	0.33	**0.33**	0.16	0.12	0.07
3: 45	0.09	0.18	**0.36**	0.22	0.16
4: 41	0.07	0.15	0.20	**0.41**	0.17
5: 43	0.00	0.14	0.09	0.16	**0.60**
Ergodic distribution	**0.19**	**0.20**	**0.19**	**0.19**	**0.23**

Quinquennial

Stationary states	1 0.96	2 0.99	3 1.01	4 1.03	5 ∞
1: 31	**0.35**	0.00	0.23	0.23	0.19
2: 32	0.16	**0.25**	0.16	0.28	0.16
3: 31	0.06	0.32	**0.13**	0.39	0.10
4: 32	0.09	0.19	0.19	**0.28**	0.25
5: 32	0.13	0.25	0.16	0.22	**0.25**
Ergodic distribution	**0.15**	**0.21**	**0.17**	**0.28**	**0.20**

7. CONCLUSIONS

The purpose of this paper has been to identify the pattern of convergence of the economic environments that characterise the different European local governments. In this regard, our results indicate that the economic aspects of the environment are still very heterogeneous. In fact, the single environmental factor that has tended to converge is the deficit. For different reasons, the local governments are aware of the need to reduce the deficit and call for management mechanisms that allow them to continue providing the society with the services that it demands. From this perspective, it is not surprising that accounting reforms have advanced all over Europe along the same path: that of providing local governments with useful tools for management decision-making.

Neither is it strange, that, after the reforms, there still remain important differences among the accounting systems. After all, the local management models are still very different. In fact, our results confirm that the per capita expenditure has not tended to converge in Europe, in spite of the fact that the per capita income of the European countries did converge during the years studied. The competencies of local governments are still heterogeneous across Europe. In turn, neither has the degree of autonomy followed a convergent tendency. Not only have the differences persisted, they have tended to become more noticeable.

Environments have actually converged, but the scope has been restricted to groups of countries, similar in economic terms and geographically close to each other. As we pointed out above, we have found evidence of regional convergence, not only in terms of deficit, but also in terms of resources available and degree of autonomy. These results have important implications for the future of the harmonisation process. In fact, since national environments do not tend to converge towards a common European environment, it does not seem reasonable to try to harmonise the accounting of the local governments in the short term. In our opinion, less rejection will be generated by advancing, as up until now, along the path of regional harmonisation, especially taking into account that, within the regions, the economic conditions in which the local governments operate are actually tending to converge.

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Mª. J. DA SILVA
J. B. DA COSTA

GOVERNMENTAL ACCOUNTING REFORM: THE CASES OF PORTUGAL AND SPAIN

1. INTRODUCTION

Portugal and Spain, two countries of the old continental Europe, reached their political and economic peak in the 16th century, with the discovery of America and the conquest of Africa.

As a consequence, their activities turned towards business, colonisation and the increase of wealth. However, following the movement for independence in the colonies, the empire was lost, and internal conflicts ensued.

In 1910, Portugal became a republic, while to date, Spain has remained a monarchy. Both countries have lived under a dictatorship, led by Salazar in Portugal and by Franco in Spain.

During that period, it was accepted that the only purpose of Public Sector Accounting was to serve the Government, its concern being the control and administration of the budget. In this way, the State was the only user of accounting information. Private sector accounting was basically of a fiscal nature, for which the rules were laid down by the State. With the emergence of democracy in 1974 in Portugal, following the Revolution of the Carnations, and in 1976 in Spain on the death of Franco, and the incorporation of both countries into the European Community, in January 1986, the necessary conditions were created for the genuine accounting reform along the lines of the models of the more developed countries. Against this background, the first Official Chart of Accounts for the private sector was adopted in Portugal in 1977, and reviewed in 1989 in accordance with the 4th Directive of the European Community. In Spain, the first Official Chart of Accounts for the private sector (it was, in fact, a Chart for both public and private businesses) appeared in 1973, and was likewise subjected to review by order of the European Community in 1990. These Charts, in particular the Portuguese one, were heavily influenced by the French model. An example of this influence is the Accounting Standards Commission which was created in Portugal, on similar lines to the French one.

On the other hand, Public Sector Accounting reform has been a slower process, due to the following factors:

- The traditional configuration of Public Sector Accounting, in which the main objective is accountability, based on legal control, and whose main basis is budget related information. Thus, it bears little resemblance to private sector

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 115-129.

accounting rules which are oriented towards a completely different set of objectives.

- The political dimension aising from acounting standards, within the framework of the public sector, namely the conflicts of interest between those who prepare financial reporting statements and their respective users.
- Conflicts between some accounting principles and the financial and budgetary legal structures in use, in that legal aspects usually prevail.
- Finally, the limited interest in governmental accounting related issues, both to users of the information and within the accounting profession. (Vela Bargues, 1994 pp 311).

Two additional factors we also consider to be of importance are the absence of researchers in this field and the fact that the public administration technical staff were only qualified for cash accounting.

Despite these constraints, government accounting reform was inevitable as, according to Montesinos and Gimeno (1998), it formed an integral part of the new conception of public management (New Public Management), which is based on three essential principles:

- Stable financial equilibrium
- Quality (on) in public services
- Transparency of information and management

In short, the ongoing reform of governmental accounting is a reality, in spite of the above-mentioned constraints, and its evolution is due to political changes, to the integration into the European Community, to the growing interest in this field of knowledge and to the proliferation of international bodies influencing, either directly or indirectly, this reform.

2. THE RECENT EVOLUTION OF PUBLIC SECTOR ACCOUNTING REFORM IN PORTUGAL AND SPAIN

2.1. The Accounting Standards

The main objectives of public sector accounting reform in Portugal and Spain are set out below:

- To define accounting principles, concepts, specific rules and financial reporting
- To bring governmental accounting closer to private accounting, without compromising its specific nature
- The shift from a situation in which there was only one user of accounting information (the State) to one of a multiplicity of users (citizens, state, providers, etc.).
- The inclusion of the accrual basis as a complement to the cash basis.
- The introduction of financial accounting as a complement to budgetary accounting.
- The shift from a single to a double entry register method.
- The increase of information on the utilisation of public services, thus meeting both the convergence criteria imposed by the European Community, and new public needs, namely the quality of public services.

- The adoption of a Government Chart of Account which lays down the same principles, rules and financial reporting for the Public Administration as a whole.

The drawing up of Charts of Accounts is characteristic of the so-called continental countries, where the standards are produced by State bodies. Thus, in countries such as Portugal and Spain, charts of accounts that guarantee reliable information, terminological homogeneity and uniform standards for codification, registration and valuation are assumed to exist.

In these countries, the drafting and publication of Official Charts of Accounts represents the standards setting process, which according to Fernandes Ferreira (1983, pp 26), constitutes the consolidated instrument for the selected accounts for accounting relevance, by which they are described, classified and codified, and through which the rules for their manipulation, valuation, timing and presentation in appropriate models and registers are indicated.

2.2. *Public Sector Accounting Reform in Portugal*

The first Official Chart of Accounts was issued in 1977 and was aimed only at the private sector and public sector firms. It was subsequently reviewed in 1989.

The governmental accounting reform was initiated in 1990, with the publication of Law 8/90, the Governemental Accounting Law. This law distinguishes two accounting models within central administration entities: a cash basis accounting for entities without financial autonomy, and accrual basis accounting for financially autonomous entities (universities, hospitals, etc.). This requirement for the double entry method led some autonomous institutions to introduce specific charts of accounts, such as the Social Security chart of accounts in 1989 and that of Health in 1991. Due to the absence of specific accounting rules, other institutions adopted the private sector Chart of Accounts.

The need for increasing accounting harmonisation led to the issue of a Chart of Accounts for Governmental Accounting-CAPA (Plano Oficial de Contabilidade Pública) in September 1997 through the Law-decree 232/97, of 3rd September, which provided the framework for any chart of Accounts to be subsequently issue. The POCP was aimed at all the public institutions within central and local administration, and revoked all previous sectorial charts together with all the adaptations made to private sector chart of accounts.

Due to the specific nature of the public sector, and because of the need for an entity to reflect on the problems of public sector accounting, an Accounting Standards Commission for Public Administration was set up in the Ministry of Finance, through the Law decree 68/98 of March 20th, which had the following brief:

- To coordinate and follow the application and improvement of the POCP and its sectorial application
- To promote studies to encourage the adoption of accounting principles, concepts and procedures, in both general and sectorial applications
- To implement projects which involve changes, further developments and interpretations of the POCP standards
- To pronounce on the issue and adaptation of, and amendment to sectorial charts.

Against this background, the following Charts of Accounts were approved for Central Administration entities:

- POC – education sector, compulsory for all entities under Ministry of Education control.
- POC – health sector, for all entities under Ministry of Health control.
- An Official Chart of Accounts for Social Security and Social Institutions is expected to be approved during the current year.

With regard to Local Administration, the publication of the 1st Law on Local Finances in 1977, Law 1/77, ratified an increase in local autonomy both in terms of revenue collection and expenditure. However, only cash basis accounting is required, and the only accounting obligations refer to budgetary control and execution. This situation remained unchanged with the publication of the Local Finances Law of 1987, Law 1/87, and was only modified in 1998 with the publication of Law 42/98, which introduced the accrual basis system into the entire Local Administration system. The POCAL was issued in February 1999, which represented the first sectorial chart based on the POCP.

The present accounting harmonization process in the Portuguese public sector is summarised in the following table:

Table 1: Accounting standards related to the public sector structure

<table>
<tr><th colspan="4">PUBLIC SECTOR STRUCTURE</th><th colspan="2">CHART OF ACCOUNTS FOR PUBLIC SECTOR ACCOUNTING</th></tr>
<tr><td rowspan="9">PUBLIC SECTOR</td><td rowspan="7">State</td><td rowspan="4">Central Administration</td><td>Education</td><td rowspan="7">POCP</td><td>POC-Education</td></tr>
<tr><td>Health</td><td>POC-Health</td></tr>
<tr><td>Economy</td><td rowspan="2">POCP</td></tr>
<tr><td></td></tr>
<tr><td colspan="2">Social Security</td><td>POC-SS</td></tr>
<tr><td colspan="2">Regional Administration</td><td>POCP</td></tr>
<tr><td colspan="2">Local Administration</td><td>POCAL</td></tr>
<tr><td rowspan="2">Public Enterprises</td><td colspan="2">State enterprises</td><td colspan="2" rowspan="2">POC-Enterprises</td></tr>
<tr><td colspan="2">Municipal enterprises</td></tr>
</table>

Table 2: Legislation within the context of Public Sector Accounting Reform in Portugal

2000	Decree 794/2000	- POC-Education
		- POC- Ministry of Health
	Decree 671/2000	- CIBE- Assessment and Inventory of Public Property
1999	Law decree 54-A/99	- POCAL
	Law decree 562/99	- New Economic Classification
1998	Law decree 166/98	- Internal control systems for Public Financial Administration
	Law 42/98	- Law of Local Finances
	Law decree 68/98	- Municipal Enterprises Law - Creation of the Accounting Standards Commission
1997	Law 98/97	- Court of Auditors Statute
	Law decree 232/97	- POCP
1996	Law decree 190/96	- Social Balance (for the services and bodies of Central Administration and Local and Regional Administration)
1992	Law decree 159/92	- Regulation of the Public Sector Accounting Law (introduces the double entry method for bodies with Administrative and Financial Autonomy)
1990	Law 8/90	- Public Sector Accounting Law (introduces the double entry method in Public Administration. Administrative and Financial Autonomy is an exception

Source: Carvalho, João Baptista (2000)

2.3 Public Sector Accounting Reform in Spain

The first Official Chart of Accounts was issued in 1973 and pertained solely to the private sector and to public enterprises. A revision of the Chart took place in 1990.

The publication of the General Budgetary Law (*Ley General Presupuestaria de 1977 - LGP*) can be considered as the beginning of the process of modernisation or reform of the Spanish Public Sector Accounting. This Law is regarded as the basis of Governmental Accounting reform, in that it recognised the importance of public sector accounting, not only for budgetary purposes, but also as an instrument to support decision making, and financial and management control. Article 125 of the Law designates the State Public Sector Accounts Department (Intervencion General de la Administration del Estado) as a management centre for governmental accounting, with powers to produce and submit the General Governmental Accounting Chart to the Ministry of Finance.

As stated by (Montesinos Julve and Vela Vargues, 1996, pp. 221) the most important aspect of this law is that it recognises the need to develop accounting standards, and grants the State Public Sector Accounts Department (SPSAD) with the power to issue accounting regulations.

To this effect, the State Public Sector Accounts Department approved the first Chart of Accounts for Public Sector in 1983, taking the 1973 General Governmental Chart of Accounts *(Plan General de Contabilidad)* as its model.

According to Gimeno Ruiz (1997, pp 45) the ongoing reforms in the public sector during the 90s led to the use of enterprise criteria and had major effects within the sphere of public sector accounting.

Following the publication of this chart, certain adaptations were made to the various Public Administration sectors:

1985: Adaptation of Governmental General Chart of Accounts to the Social Security System

1986: Accounting Instructions for Autonomous Entities

1990: Accounting Instructions for Local Administration

This Chart was revoked in 1994, with the publication of the new PGCP, which was drafted along the lines of the new 1990 private sector PGC. However, it should be noted that this Chart took into consideration the governmental accounting principles published in 1990 by the SPSAD, which, according to Vela Bargues (1992b) were essential in that they laid down the rules to guide the process for the drafting and presentation of economic and financial information in the field of Governmental Accounting.

However, modifications to the Plan for the Social Security system, Autonomous Bodies and Local Administration are still pending approval.

It should be noted that no reule exists which requires Autonomous Communities to adopt the PGCP, as the SPSAD has no regulatory power over the Autonomous Communities.

The present accounting harmonisation in the Spanish public sector is summarised in the following table:

Table 3: Accounting standards related to the public sector structure

<table>
<tr><th colspan="3">PUBLIC SECTOR STRUCTURE</th><th colspan="2">GENERAL GOVERNMENTAL CHART OF ACCOUNTS</th></tr>
<tr><td rowspan="6">PUBLIC SECTOR</td><td rowspan="5">State</td><td>Government Administration</td><td rowspan="5">PGCP</td><td>PGCP</td></tr>
<tr><td>Autonomous Communities</td><td>Autonomous accounting standards</td></tr>
<tr><td>Local Corporations</td><td>Instructions for Local Administration Accounting</td></tr>
<tr><td>Social Security Management Bodies</td><td>Adaptation of PGC to the Social Security</td></tr>
<tr><td>Autonomous Bodies</td><td>Accounting Instructions for Autonomous Bodies</td></tr>
<tr><td colspan="2">Public companies and other public enterprises</td><td colspan="2">PGC-Enterprises</td></tr>
</table>

Table 4: Legislation within the context of Spanish Public Sector Accounting Reform

2000	Account consolidation
1996	Accounting Instructions for General Government Administration
	Accounting Instructions for Government Institutional Administration
1994	General Governmental Chart of Accounts
1990	Accounting Instructions for Local Government
1988	Regulatory Law for Local Finance Offices
	Accounting Instructions for Government Accounting
1986	Accounting Instructions for Local Finance Delegations
	Accounting Instructions for the Treasury and Finance Policy Department
	Accounting Instructions for Autonomous Bodies
1985	Local Regime Principles
	Adaptation of PGCP to Social Security system
1983	General Governmental Chart of Accounts
1981	General Governmental Chart of Accounts (provisional version)
1977	General Budgetary Law

Source: Pina and Torres (1996)

2.4 National Regulatory Bodies

In Portugal, as well as in Spain, the regulatory body is the Ministry of Finance:

- In Spain, the SPSAD (State Public Sector Accounts Department), which produces documents concerning public accounting principles and accountancy instructions. Following the publication of the 1983 Plan, a conceptual structure for the public sector was considered to be necessary. This structure began to be put into place with the publication of the first document on Accounting Principles by the SPSAD. A further document was subsequently published with the objective of clarifying and presenting guidance on the presentation of economic and financial information of public entities.
- In Portugal, the Public Administration Accounting Standards Commission (CNCAP), which elaborates sub-sectorial charts and produces accounting guidelines. This commission includes members from several ministries and one member of the Private Accounting Standards Commission. At the same time, support groups for the implementation of the sub-sectorial charts were created to produce interpretative standards, namely:
- SATAPOCAL- "Subgrupo de Apoio Técnico a Aplicação do Plano Oficial de Contabilidade das Autarquias Locais" implementation which is answerable to the Local Administration Ministry.
- GATEDU- a technical support group for the implementation of POC-Education, which is answerable to the Ministry of Education.

Regulatory bodies

SPAIN	PORTUGAL
IGAE (SPSAD) – *Intervención General da Administración del Estado* (State Public Sector Accounts Department) Documents on public accounting principles: 1. Governmetnal Accounting Principles 2. Rights to collect and revenues 3. Obligations and expenses 4. Transfers and subsidies 5. Debt 6. Fixed assets 7. Public Financial information 8. Expenditures with pre-allocated revenues	CNCAP- *Comissão de Normalização Contabilística paa a Administrção Pública* (Public Administration Accounting Normalisation Commission) Guidelines produced: 1. POCP implementation phase 2. Standards for the application of CIBE

The activities carried out by these two bodies have, both in the Spanish and the Portuguese case, justified the need to introduce changes to the initially approved charts. Thus, in Spain, the PGCP was reviewed and a new version published in 1994 as a consequence of intervention by the SPAD, (the PGCP was reviewed and published again in 1994). In Portugal, as mentioned above, new guidelines were published to support the implementation of the POCP. However, a thorough revision of the Plan was not deemed necessary given the short time it has been in force.

3. SIMILARITIES AND DIFFERENCES BETWEEN THE PORTUGUESE AND SPANISH ACCOUNTING SYSTEMS

The main similarities between the Portuguese and the Spanish Accounting System are set out below:

a) According to the basis of recognition

At an international level, three accounting bases are identified:
- Cash basis: This type of accounting is essentially based on the cash principle, i.e., expenses and revenues are registered at the moment when the respective payment or receiving takes place.
- Expenditure basis: This type of accounting is characterised by registration at the moment of the commitment or of the right to the revenue settlement.
- Accrual basis: This type of accounting is based on the accrual principle, and allows the economic result to be disclosed.

In Portugal and in Spain, as mentioned above, one of the objectives of Public Sector Accounting Reform was the introduction of the Accrual Basis. Thus:
- The Cash basis and Expenditure basis is used in the Budgetary Accounting system.
- The Accrual basis is used in Financial Accounting and Cost or Management Accounting systems.

b) According to the Object of Registration

In both Portugal and Spain, there are three autonomous accounting systems, but they are integrated in unique Chart of Accounts:
- Budgetary Accounting: Characterised by being based on the cash principle, in which all the phases of the Cash Flow Budget are registered.
- Financial or Net-worth Accounting: Characterised by the principle of specialisation of the period, in order to allow the economic result and the financial and net-worth situation of each institution to be recorded.
- Cost or Management Accounting: Characterised by the principle of specialisation of the period, in order to allow the cost of each activity, product or service institution to be recorded.

c) According to the Registration Method

Reference has previously been made to a further objective of Public Sector Accounting Reform: the introduction of the double entry method as a substitute for the single entry method. With the exception of Cost Accounting, governmental Accounting now follows the double entry registration method.

SPAIN	PORTUGAL
Budgetary Accounting	
Double entry	Double entry
Financial Accounting	
Double entry	Double entry
Cost or Management Accounting	
Not obligatory	Obligatory, but (of) using either single or double entry

In spite of taking the Spanish model as a reference, and of having legislation, that as a rule, is based on legislation already passed in Spain, Portugal has its own specificity and, in several aspects, is more advanced than Spain. This can be seen for example, in areas concerning Cost Accounting in Public Administration, in the issue of an accounting system for Local Municipalities already adapted to the POCP, in the assets valuation criteria recently adopted (CIBE). The most significant differences can thus be highlighted as follows:

a) According to the phases of the Public Sector Accounting Reform

As seen above, Public Sector Accounting Reform in Spain started in 1977, while in Portugal it began in 1990. Thus, Spain is notably one of the main sources for the drawing up of Public Sector Accounting legislation.

However, there is evidence to show that increasing accounting harmonisation is taking place in Portugal, i.e., all the public bodies have their own accounting system, based on one single Chart of Accounting: the POCP (1997).

In Spain, the sub-sectorial Charts and Instructions which were modified from the first Chart (1983) have not yet been adapted to the new General Governmental Chart of Accounts (PGCP-1994).

Year	Spain	Portugal
???	Adaptation of the Chart of Accounts to Local organisms	
2001		Official Charts of Accounts to bodies of the Ministry of Social Security Official Chart of Accounts for collection agencies
2000	Approves instructions for account consolidation in public bodies	Official Chart of Accounts for Ministry of Education bodies, which includes account consolidation Official Chart of Accounts for Ministry of Health CIBE – Assessment and Inventory of Public Property
1999		Official Chart of Accounts for Local Municipalities
1997		Official Governmental Accounting Chart Utilisation of accrual accounting in public bodies Revocation of previous charts Creation of Public Administration Accounting Standards Commission
1994	General Governmental Chart of Accounts Utilisation of acrual accounting in public bodies	
1993		Official Governmental Chart of Accounts for Municipal Services
1990	Accounting Instructions for Local Administration	Start of the present Governmental Accounting reform Utilisation of "accrual accounting" in bodies with financial and administrative autonomy
1985	Local Regime Principles	
1983	General Governmental Chart of Accounts Utilisation of accrual accounting in public bodies	

b) According to the rules for sub-sectorial adaptation

In Portugal, it can also be observed that the principles, standards, accounts and final maps can be found in the respective Official Chart of Accounts. In Spain, there are specific standards for the Cost Accounting system, as well as specificic standards for different information systems (SICAL, SICOP, SICAI, etc.).

It is also important to mention that in Portugal there is a Chart of Accounts and specific standards for the whole Education sector, which includes an Analytical Accounting system and consolidation standards.

SPAIN	PORTUGAL
Central Administration	
PGCP (1994) based on the 1990 General Chart of Accounts (PGC) for business enterprises	POCP (1997) based on the 1989 Chart for the Private Sector and on the Spanish PGCP
Local Administration	
• 1985 Instructions a) Based on the previously revoked 1973 Chart of Accounts for the Private Sector b) To be adapted to the 1994 PGCP • CANOA- Analytical Accounting for Autonomous Organisms	• POCAL (1999), a) Based on the 1997 Governmental Chart of Accounts b) Includes budgetary and cost Accounting Standards
Education	
• PGCP (1995) and • SCAU-System of Analytical Accounting for Universities	• POC-Education (2000) a) Based on the 1997 Governmental Chart of Accounts b) Includes Budgetary and Cost Accounting Standards c) Obligatory use in all the bodies in the public education sector
Social Security	
• 1992 Instructions a) Based on the 1983 General Governmental Charts of Accounts (reviewed in 1994) b) To be adapted to the 1994 PGCP • SICOSS- Information Accounting System for Social Security Bodies	• POC-Social Security (2001) a) Based on the 1997 Public Accounting Plan b) Includes norms Financial, Budgetary and Cost Accounting Standards
Health	
• 1992 Instructions (of 1992) a) Based on the 1983 General Chart of Accounts (reviewed in 1994) b) To be adapted to the 1995 PGCP • SICOSS- Accounting Information System for Social Security Organisms	• POC- Health (2000) a) Based on the 1997 Governmental Chart of Accounts b) Includes Financial, Budgetary and Cost Accounting Standards

c) According to the registration of the public domain assets

The problem of public domain assets has been dealt with differently in the two countries. In Spain, the option taken was to consider the inclusion of public domain goods in the Balance(-)Sheet only when they are in the construction phase.

On conclusion, the good is removed from the Balance Sheet. This methodology was not followed by Portugal and is currently one of the most controversial features of the present Public Sector Accounting Reform in Portugal: the fact that all the Public Domain Goods are considered in public entity Assets. In the Balance Sheet of a Spanish entity the economic and financial perspective is predominant, while in Portugal, the net-worth perspective predominates and the Balance Sheet is seen as the set Origin and Funds Application, though up dated. To conclude, in Spain the legal aspect takes precedence over the economic value.

The Official Governmental Chart of Accounts created a specific account for these goods, in which public domain goods defined by law are included.
To clarify these issues, a regulation on the inventory of State-owned goods was recently adopted (CIBE). The evaluation criteria, together with the annual amortisation taxes to be used, are defined in this legislation.

However improved clarification between public domain goods and public usage goods is needed. In our opinion, account 45, Public Domain Goods shows more specific characteristics than Public Usage Goods.

d) According to the registration of pluri-annual expenses

According to the Principle of Annuity, in both Portugal and Spain, Budgets are annual and coincide with the calendar year. However, in Portugal, commitments already taken on with reference to future periods are subject to registration in the Budgetary Accounting, which gives not only more information to the user, but also provides useful information for the preparation of future Budgets.

e) According to the simplified regime

The complexity of the new accounting system, together with the Principle of Relative Importance, has led some small bodies to devise a more simplified regime.
In Portuguese Local Government, the simplified method is to be followed by Town Councils with an annual volume of receipts of below € 2.000.000 In Spain, whether a Town Council follows the general or the simplified regime depends on the number of inhabitants (5.000 inhabitants). On the other hand, in Portugal, Town Councils following the simplified regime use single entry accounting of a Cash Accounting type. In Spain, only certain financial maps are left out of the simplified regime.

It should be also mentioned that in the Portuguese Education sector, small schools integrated into a Public Group whose mother-entity can guarantee their financial position form part of the simplified regime.

f) Subsidy for Investment

The accounting of subsidies and transfers of capital follow different criteria in the two countries.

Portugal uses the principle of the accrual basis which defers investment subsidies, while investments are depreciated. When the goods are not subject to depreciation (land, historical, artistic and cultural heritage, investment subsidies are directly recorded as a net worth increase.

In Spain, subsidies and transfers of capital are totally integrated in the Account of Results, which means that they are considered as profits within the period they are paid.

g) According to the consolidation of accounts in public groups

In Portugal, the consolidation of accounts will be obligatory in Education and Health sectors, from 2002 on. In the Education sector, all mother-entities should present the financial consolidated reports of the Public Group. Publication of financial consolidated reports and of the consolidation management report is compulsory for all mother-entities dependent on the Ministry of Education (which are not included in the legally defined exceptions) and when any of the control conditions can be presumed. This obligation comes into effect for universities and polytechnics in financial year 2002 and other Public Groups will follow the time schedule to be established by the Ministry of Education.

Consolidated financial reporting of the Public Group must, as previously mentioned, give a true and fair view of the financial position and of the results of the set of entities making up the consolidation. The reporting should present:

- Consolidated balance sheet;
- Consolidated result report;
- Annex to the consolidated balance sheet and to the consolidation results report;
- The inclusion of the consolidated cash-flow report is also recommended.

The previewed techniques and consolidation procedures are based on the application of simple aggregation and integral consolidation methods. The method of net-worth equivalence is obligatory for associated entities in which the mother-entity holds a participation of over 20% and below 50%.

The accounting principles to be observed in the preparation of the financial consolidated report, the valuation criteria of applicable assets and liabilities and the structure of the models to be followed are defined in the POC-Education.

In Spain, the Court of Accounts recommends that the State Accounts be consolidated, and suggests the need for a consolidated State balance sheet, a consolidated results account and the consolidated budgetary accounts (Pina and Torres, 2000)

4. CONCLUSIONS

The first fruits of the governmental accounting reform initiated in Spain in the 70s and Portugal in the 90s can already be observed. The publication of the POCP in Portugal and the PGCP in Spain clearly underlined the changes necessary to bring into effect the so-called "New Public Management". They have created conditions for the integration of different accounting system: budgetary, patrimonial and analytical, into modern public sector accounting, thereby providing a support tool for public managers.

In this study, we have shown the evolution of Public Sector Accounting in both countries although the Spanish case was without doubt the source of inspiration for governmental accounting reform in Portugal. However, peculiarities are evident in each model. In conclusion, we put forward some points we believe worthy of further consideration:

a) Despite discontinuity in the reform process, it is irreversible and the balance is positive, as far as the increase of information to internal and external users and the increased efficiency, effectiveness and economy in the management of public resources are concerned;
b) Although the Spanish reform has had a strong influence, in some aspects (for instance consolidation of accounts in POC-Education) Portugal is closer to countries with a more advanced Governmental Accounting System, such as Australia and New Zealand.
c) The change witnessed in the teaching of Accounting in higher education is unquestionable. Governmental accounting must not be seen the "poor relation" or taken as an optional subject. Colleges have modified their accounting teaching programmes to take into account current tendencies and needs; the research in this field is real, and CIGAR Conference bears witness to this fact.

Within the conception of POCP (Portugal) and of PGCP (Spain), there was a clear concern to bring the chart of accounts as close as possible to that of the private sector. This approximation is mainly due to the concern to gather data that could be analysed comparatively with information from the private sector, and satisfies the demands of European Community bodies and the preparation of the National Accounts.

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JUNE PALLOT
KIYOSHI YAMAMOTO

GOVERNMENT OR GOVERNANCE?

Japan's New Balance Sheet In International Perspective

INTRODUCTION

The latter half of the 20th century saw governments face mounting financial pressures, administrative overload, and declining public confidence in the institutions of democracy. While these factors have stimulated innovations in public management and accounting in many countries, the environmental conditions for governmental innovation in Japan were, for a long time, unfavourable (Lüder, 1994). As recently as 1998 Kokubu et al. described Japan as a "runner a lap behind" in New Public Financial Management. Since then, however, the fiscal position of the Japanese central government has become the worst in the developed world while political scandal has heightened citizen demands for accountability and transparency. In response, two major initiatives have been undertaken: the formation of semi-autonomous public organizations called Independent Administrative Institutions (Yamamoto, 2000) and the development of a balance sheet for the whole of government.

This paper examines the second of these initiatives – the efforts made in 2000 to produce a "whole-of-government" balance sheet. We briefly compare the accounting policies adopted with those of countries which have been particularly active in public sector accounting reform and which are seen as potentially useful benchmarks for Japan: the UK, the USA, Canada, and Australia/New Zealand[1]. Some common problems and shortcomings are identified and we suggest that these are difficult to address within an individualistic New Public Management paradigm which views government as an entity separate from society. We argue that public management is a question of *governance* and that management reforms, including accounting system transformation, have to be understood as a response to governance changes which include, but are not confined to, NPM. We then make some preliminary suggestions as to how a governance (as opposed to *government*) paradigm might enhance CIGAR research.

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 131-144.

THE JAPANESE BALANCE SHEET

For a long time academics, accounting professionals and the Public Accounts Committee and Budget Committee of parliament had been asking that the central government prepare a balance sheet on private sector lines. In 1999, international developments, mounting fiscal pressure and initiatives taken in the more innovative Japanese local governments, finally overcame MOF's resistance to accrual accounting and a Study Group, with members including professors of accounting and public finance, accountants and financial practitioners, was established.

Table 1. Accounting for Assets by Country Reviewed

Country	*Infrastructure Assets*		*Defence Assets*		*Heritage Assets*	
	Recording	*Valuation*	*Recording*	*Valuation*	*Recording*	*Valuation*
AUS	O	Depreciated replacement cost	O	Depreciated replacement cost	O	Net present value or current market value
CA	O*	Depreciated acquisition cost	O*	Depreciated acquisition cost*	X*	-*
JP	O	Depreciated historical cost	O	50 per cent of historical cost	X	Numbers of items held
NZ	O	Depreciated replacement cost	O	Depreciated replacement cost	O	Best estimate of net current value
UK	O	Depreciated replacement cost	O*	Depreciated replacement cost*	O	Lower of replacement cost and recoverable amount in operational use
USA	O	Depreciated historical cost	X	Number of system, items	X	Non-financial units

Notes

1: When alternative methods are allowed, most representative methods are shown.

2: The items attached asterisk are based on the planned treatments.

3: The circle and cross signs indicate the recording as on-balance and off-balance respectively.

Based on the discussions of the Study Group, MOF published in October 2000 *Provisional Concepts and Standards for the Japanese Balance Sheet*, which stated that the main objective of government balance sheet preparation is to strengthen accountability to the public through the provision of a complete picture of financial position, and *The Japanese Government Balance Sheet (Primary Trial).* The accounting policies developed are summarized in Tables 1 and 2.

Table 2. Accounting for Liabilities by Country Reviewed

Country	*Government Employee Pensions*		*Public Pensions*	
	Recording	*Valuation*	*Recording*	*Valuation*
AUS	O	Accrued pension liability	X	Disclosed in the notes actuarial valuations of obligations
CA	O	Accrued surpluses or deficits	X	Disclosed in the notes (government's authority to spend is limited to the Plan's net assets)
JP*	X	Government subsidies to the pension (d)	X	Reserves only are recognised as the deposits received of public pensions (c)
	O	(reserve is set aside in non-government body)	O	Reserves and government subsidies to the plan (c) + (d)
	O	Half of the future insurance premium payment ½(a)	O	Total amount of the present value of benefits corresponding to the past period (a) + (c) + (d) (accrued pension liability)
NZ	O	Actuarial pension liability	X	Disclosed in the notes
UK	O	n.a.**	X	n.a.**
USA	O	Actuarial accrued pension liability	X	Disclosed in the notes

* See Figure 1

** The UK will produce central government accounts for 2002/2003

Of particular interest, given their importance to countries around the world, is how to recognise and measure pension liabilities specific to the public sector: pensions for government employees and the public pension for the public at large. In Japan, public pension benefits are financed from insurance premium income in the case of employees (paid equally by employees and employers in both the public and private sectors), tax income in the case of the Basic Pension for other people, and interest on reserves. A premium management system gradually increases premiums over time to align with the aging population and maintain benefit equity across generations.

The present value of benefits corresponding to the past period, although probably not the present value of benefits corresponding to future periods, could meet IFAC's definition of liabilities. The present value of benefits corresponding to the past period means the total amount of benefits provided for those who have already been receiving a pension and the amount of benefits corresponding to the premium-paid period before the end of the current financial year. However, MOF could not decide which part of the present values corresponding to the past period should be recognized as liabilities, and three different methods were displayed (see Figure 1).

In the first method, the future public pension benefits are not recognized as liabilities, but reserves (b) are recognized as deposits. In the second method, which judges each finance source separately in deciding whether it should be recognised as a liability, only reserves and government subsidies are to be recognized as liabilities. The third method recognises the total amount of the present value of benefits corresponding to the past period as liabilities.

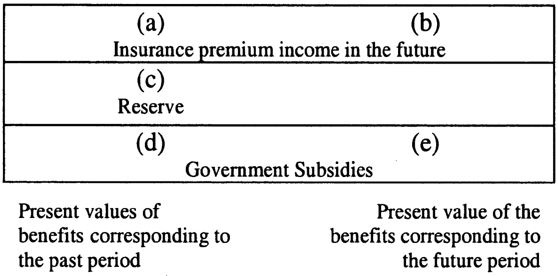

Figure 1. Recognition of Liabilities for Pensions in the Government Balance Sheet

Similarly, three methods were indicated to account for the government employees' pension system. In the first method, as the reserves are recognized as deposits in the balance sheet of the mutual association that is a separate body from the government, neither the reserves or the future pension benefits are recognized as liabilities in the government balance sheet. In the second method, only government subsidies are to be recognized as liabilities and the part of the pension burden entrusted to the Government as employer (half of the amount covered by future increases of insurance premium rates) is excluded from the liabilities. The third method includes the part of the pension burden attributable to the government as employer.

Given that other countries do not appear to recognise liabilities to public pension systems on the government balance sheet, MOF is innovative in suggesting that some part of future pension benefits could be recognized as liabilities. Theoretically the same accounting treatment could also be adopted for recording the future pension benefits corresponding to the past period in the balance sheet of the public employees' pension scheme. Not only is the reliability of calculation identical but also the government has the same obligations as an insurer as it does as an employer.

In contrast to the balance sheet, there is no intention on the part of MOF to produce accruals-based operating statements other than for the Independent Administrative Institutions (IAIs). Japan does not have a double-entry bookkeeping system within government which would provide the necessary information, other than in some Special Accounts. The MOF report considers that the matching of expenses and revenues, as in the private sector, is not meaningful. This approach might seems odd and can be partly understood by the fact that MOF's main concern is disclosure of fiscal position. However, considering that IAIs are required to prepare a cost of services statement, it seems strange that the same should not apply to the government as a whole. Costs should be matched to services provided, and the government does have to balance costs with revenues in the longer term.

ACCOUNTING ISSUES AND PROBLEMS

Contrary to stated objectives, the trial government balance sheet does not show central government in entirety since subsidies for capital expenditures to local governments and public corporations are not recorded in the balance sheet. This incompleteness raised considerable criticism of the disclosure and transparency: every national newspaper doubted the entirety and understandability of the fiscal condition.

The first problem relates to local government. Two-thirds of public services in Japan are delivered by local governments. However, the central government subsidises local government activities and half of the expenditures for capital investment in the local government are financed largely through national bonds issued by central government. This leads to a biased figure in the central government balance sheet. While the bonds are fully recognized as a long-term liability, the capital expenditure undertaken by local government with this finance does not appear in the balance sheet as fixed assets. This is because MOF has modified the third criterion in IFAC's definition of assets to be "the service potential or future economic benefit *must be possessed by the reporting entity* (modification italicised). Accordingly, the more the central government expenses capital investments, the more the gap between assets and liabilities increases.

A second issue (not unique to Japan) is that the reporting entity differs between government accounting and the System of National Accounts (SNA). "General Government" in the SNA consists of central government, local governments and social security funds but does not include government activities which are "Public Enterprises". Unlike the MOF's government balance sheet, SNA does record capital expenditures for local government as the fixed assets of "General Government". However, privatization results in an incomplete figure of "General Government" in the SNA as fifteen of the government's 38 Special Accounts are classified under "Public Enterprises" rather than under "General Government".

Furthermore, public services are increasingly being delivered through networks. Following the UK, the Japanese government has enacted the fundamental law for public private partnerships (PPPs) where the public sector contracts to purchase quality services on a long-term basis from the private sector. Government activities are unable to be identified in terms of traditional notions of ownership and control which have been the basis for defining the accounting entity in commercial accounting.

The fiscal position of the Japanese central government has become the worst among developed counties and Japanese citizens are increasingly demanding more information about infrastructure and the sustainability of public finance (Nihon-Keizai Newspaper, 12^{th} October 2000). However, the true nature of the deficits goes unrecognised because a large part of monetary assets is invested in the public corporations, Special Accounts and local governments whose finances are in deficit.

Even consolidated financial reporting would not present the right information about whether central government finances are sustainable or not; by contrast with the private sector net assets are not a measure of sustainability because some assets (e.g many infrastructure assets and heritage assets) are unable to be sold. Some commentators suggest that since the "huge" public bonds are offset through the savings of citizens (about ¥1000 trillion net monetary assets), the large deficits in public finance will never result in a fiscal crisis in the public sector. Again, there is an issue of how we define the accounting entity.

Public expectations with respect to financial performance also need to be considered. The general public expects that financial reporting in the public sector prepared in accordance with GAAP would provide useful information on performance as it does in the private sector. It is hard to see how the absence of an operating statement would contribute to improving performance.

We believe that these challenges to accounting – fuzzy boundaries, networks, control of resources shared by the government and society, intergenerational equity and increased public participation – cannot be fully conceptualised within a conventional view of government as a separate identifiable entity (a sort of corporation or super-individual). Much of the accounting innovation has taken place under a "New Public Management' paradigm (Lapsley, 1999) and much recent CIGAR research has examined accounting in terms of this paradigm. But as Kettl (2000) points out, NPM was originally an effort to reinvent the distinction between policymaking and policy execution as agencification; it requires clarified boundaries between policy and administration and between government and society. We suggest that NPM is one form of evolution of the public sector but there are others at least equally important. These are better understood in terms of *governance,* not just *government.* As Kickert (1997, p.732) suggests:

> Public management should be broadened into "public governance" in which the external orientation at the socio-political environment plays an important part, as well as the complexity of administrative relations and the specific character of "governance" in complex networks.

Governance includes, but is not confined to, government. In the next section we examine briefly the concept of governance and identify the various directions in which governance is evolving. We then use these dimensions to identify the new challenges they pose for accounting and CIGAR research.

RECONCEPTUALISING THE ISSUES: FROM GOVERNMENT TO GOVERNANCE

"Governance", albeit a term with many different meanings and concepts, has rapidly become a popular concept in the social sciences in light of the decreasing capacity of government to manage the economy and society or to solve social problems and its erosion by other actors such as international or sub-national institutions and companies. It is possible to identify five different directions in which governance is shifting in order to cope with the limitations of government (see Figure 2): shifting the political power of the state upward, downward, outward or inward, and "reinventing" the state[2].

The upward shift is a response to the impact of *globalisation* on governments. Private capital moves globally to seek a profits, decreasing the efficiency and efficacy of traditional domestic control mechanisms, sometimes causing an economic or finance crisis in susceptible nations, and requiring a new model of governance whose modes are not governed by the state (Gamble, 2000). It is widely recognized that certain important problems (e.g. environmental problems, regulation of world trade and international financial markets, developing common accounting standards and checking the international drug trade) cannot be controlled or contained at the level of national states alone (Hirst, 2000, p.15). This has led to extensive discussion of the role of international agencies (e.g. IMF, WTO, ASEAN), inter-state agreements and common commercial governmental practices (like arbitration) as methods of governance. The question is how these supra-national agencies and private governance practices at the international level are monitored and controlled by domestic publics. In other words, public management has to coordinate partly conflicting interests beyond the state border.

The downward shift involves the *devolution* or decentralisation of state authority to regional and local institutions. In part it is a move away from the standardised central state towards stronger expression of local, ethnic and cultural sentiments. It is also a matter of "load-shedding" or displacing problems in times of fiscal constraint, a recognition of limited information capacity of state governments and a result of the growing capacity and skills of local governments grown larger through urbanization and agglomeration. Communities have been given greater financial responsibilities while at the same time allowing more citizen participation on political issues.

Reassertion adopts a strategy of "reinventing" government itself, with governance limited more or less to corporate governance. It aims at enhancing the management potential to resolve problems. The focus is on the micro rather than macro level of public management – management within organizations rather than problems of inter-organizational management (Metcalfe, 1993).

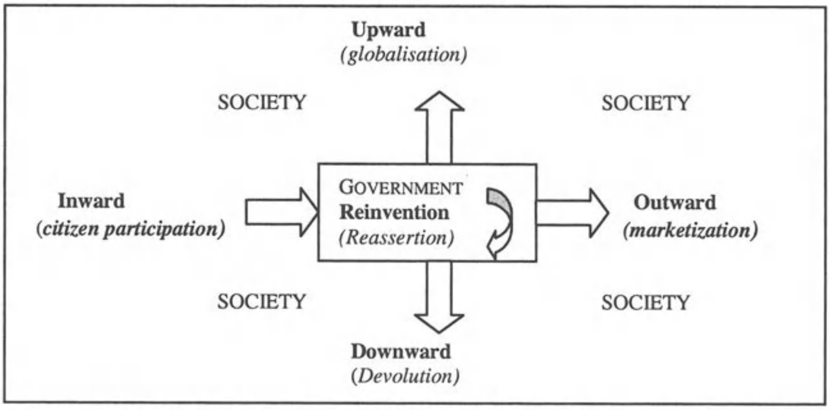

Figure 2. Strategies for New Governance

New Public Management embraces not only reinvention but also an outwards *marketisation* shift in which functions and resources are transferred into institutions operating at arm's length from the state. Under mounting fiscal stress in the 1980s and 1990s, this was seen by many governments as a way of maintaining public service levels with the same or less money. Whilst this governance type combines control by the state through performance contracts with managerial discretion given to the organisations, overall there is a shift from politics to market - from collective interests to individual decision making. It may be more useful in dealing with micro-level problems rather than broader environmental, ecological and social problems which transcend organizational boundaries.

Lastly, the inward shift focuses on direct citizen *participation* – at central, regional or local levels - as the principal source of governance (Kooiman, 1993). As well as a way of dealing with collective action problems, the inward shift can be seen as a response to the apparent decline in confidence or trust in government across developed countries (Norris, 1999; Pharr and Putnam, 2000) and the consequent demand from citizens for greater accountability and a new governance style for governing. It is in this area that major challenges lie. Democratic governance demands practical tools for mutual agreements to manage by participation, apparently not easy despite the development of participatory policy analysis (Durning, 1993).

It is likely that the particular combinations of governance shifts adopted in each country depend on the circumstances of each, including its national culture and political ideology. Thus governance forms a possible framework for comparative research on a dynamic basis.

IMPLICATIONS FOR ACCOUNTING RESEARCH

The governance shifts identified above can be used to classify CIGAR research and identify agendas for future research. Accounting practices can also be evaluated in terms of how well they respond to the various demands posed by these different governance shifts.

The upwards shift should lead us to examine such issues as accounting for national governments (CIGAR 5, Chan, Jones and Lüder 1996); the desirability or otherwise of harmonising accounting standards; the role and expectations of trans-national oversight bodies (e.g. World Bank, IFAC), the role of epistemic communities in transmitting accounting knowledge and ideas across nations (Laughlin and Pallot 1998), accounting by supra-national entities (e.g. the EU) and the relationship between national accounting and government accounting (Jones and Lüder, 1996; *Financial Accountability and Management* special issue May 2000). To date there has been a significant amount of CIGAR research of this type. However, as the boundaries of the state become less clear, we need also to explore other accounting challenges in a comparative fashion.

The downward shift would lead us to compare countries in terms of their local governments (CIGAR 6; Caperchione and Mussari, 1999) and central-local government relations (CIGAR 7; Bac, 2001). Countries differ in the extent of autonomy that local government has from central government. There are implications for whether we view accounting as a mechanism of hierarchical control by central government or as a horizontal accountability to citizens; the interests of the two may differ. In countries such as the UK and Japan (and unlike New Zealand), where a considerable proportion of local government expenditure is financed by central government, there are accounting issues such as whether local government should be consolidated with central government in whole of government financial statements. Furthermore, a comparison of accounting innovation across countries requires an analysis across different levels of government and an understanding of the changing relationship between the levels of government. Olson et al. (1998), for example, found that the speed of New Public Financial Management could not be fully understood by merely focussing on the national level. A possible question for research is whether it is innovation at the local level or movements at the international level which has more impact on national government accounting innovation.

Research focussing on reinvention might look in particular at costing, outputs budgeting and performance measures for managerial decision making and accountability and other aspects of the New Public Management. CIGAR research might attempt to compare aspects of management accounting by organizational type across countries (for example, hospitals) and examine the impact of organizational culture on accounting. NPM has typically emphasised clear specification of outputs (it has not been thought feasible to hold managers accountable for outcomes) and the separation out – preferably into separate departments or agencies – of different functions such as policy and operations, commercial and non-commercial activities, regulation and operations, purchase and provision of services. Yet this emphasis on transparency can create fragmentation and denies the interdependence needed to resolve many public management issues. As the Audit Office in New Zealand points out:

> Government organisations often establish both formal and informal working groups ("virtual departments") to deal with specific issues or to pursue collective objectives. It may be that no one agency is primarily accountable and that no external reports acknowledge the existence of the objectives, the resources applied collectively to pursuing them or the group's performance in doing so. In summary, the structures of government organizations are becoming more diverse and complex. The information exchanges between these organizations and with their stakeholders are increasing in frequency, scope and complexity. (Audit Office, 1999, p.20)

The outward movement has been the subject of research in a number of countries but there is clearly much work to be done and further accounting development to be undertaken. As noted earlier, the Japanese government reporting entity does not include public corporations with the result that the net assets on the balance sheet do not provide the people with the information to assess fiscal sustainability. In New Zealand the Audit Office has expressed concern about the accountability for appropriations to parties other than government departments given that these represent a large and increasing proportion of parliament's appropriations (Audit Office, 1994, 1998). In Australia, it is interesting to note that private sector standards have had their scope extended to the public sector and three standards are dedicated to the public sector. However two accounting standards (on reporting by segments and on related party disclosures) which might have enabled more accountability of non-departmental entities have been excluded from application in the public sector with no explanation provided (Karan, 2001). On the positive side, the UK has established an accounting standard for Public Finance Initiatives, FRS 5, and recently CIPFA (2000) published the code of practice on Partnership and Joint Working Arrangements for Best Value Accounting. In the US, accounting for partnerships was developed and invisible assets such as brands in the privatized organisations were also measured in monetary terms in Italy (Mongiello and Moretti, 2001). There is considerable scope for sharing knowledge of developments across countries in this area.

It is perhaps the inward movement, adopting the "modern government" reform strategy identified by Pollitt and Bouckert (2000) that has been least explored in CIGAR research and which poses some of the most interesting challenges for public sector accounting. Unlike the individualistic, or market-exchange based approach to which commercial accounting is particularly well suited, this approach is more communitarian and has greater potential for dealing with collective action problems which cross organizational boundaries and the public-private divide.

The "Third Way", "Modernising Government" "Joined-Up Government" of New Labour in the UK are responses to the shortcomings of NPM. It seems that the Westminster or Commonwealth countries have been approaching the American style where cross-cutting, cross-government work has traditionally formed a significant part of governance[3]. By contrast, it looks as though Japan is adopting the opposite trajectory. Cross-working or teamwork has been a feature of Japanese society with social capital at a higher level than in other developed countries (Putnam, 1996;

Fukuyama 1999). This has been seen as a source of the competitive power and it might be supposed that Japan would transform into the new governance of the 21st Century rather faster than the western countries. However, this does not seem to be the case. Instead, Japan seems to have been moving in a more individualistic direction, asserting the independence of individual citizens and establishing IAIs in which chief executives are held accountable for defined outputs and services.

According to the cohort survey (EPA, 1995), younger generations much prefer individualistic life styles to the socially-oriented style of elder generations. Because of changing demographics, the younger generation feel an inequality between themselves and their parents' generation in terms of benefits and burdens under the present public pension scheme. It has been suggested that the Employees' Pension be privatised while ensuring the Basic Pension through more subsidies from the government. Such reforms would require people to look attend to their own interests first, rather than collaborate among generations, and could result in more differences in income level among elder people; consequently, social capital might deteriorate. To become a first runner for the transforming into the new governance, Japan needs to restore social capital, not merely introduce NPM principles. It can be expected that rebuilding of social capital would allow the community to solve the macro-level social and inter-generational problems by themselves, though partly supported by the government. Generational accounting (Kotlikoff, 1999) may provide useful information to this end.

In any country which seeks to build (or rebuild) social capital, the role of accounting should be considered. The new governance may be too new for accounting to have any definitive responses as yet but some preliminary suggestions can be made. First, in contrast to the micro-level individualism of NPM (which retains an important accountability and cost-management role at that level), 'socialising accountability' (Roberts, 1991) requires reporting on outcomes. Indeed, given the nature of policy networks, the appropriate accounting entity is more likely to be policies/programmes than organizational entities.

As well as information on outcomes, information on assets and liabilities having inter-generational significance or consequences – notably infrastructure assets, heritage assets and pension liabilities (McCrae and Aiken, 2000) – is needed to enhance public debate. Pallot (1992) suggests a notion of "community assets", based on a notion of common property rather than private property (MacPherson, 1978) to describe infrastructure and heritage assets in order to recognise the beneficial use by, and decision making by, the community. To treat them as "government" assets is to treat them as the private property of the government. Conventional commercial accounting tend to treat assets as either fully under the control of the reporting entity or not under control with no intermediate stage between the two (Ijiri, 1975, p51); perhaps we develop accounting which recognises *degrees* of control. Recognition of assets based on common property alongside private property lends greater visibility to the communitarian perspective with its emphasis on shared values and a common life and to social, as well as technical, concerns. This is particularly so if a term such as "community assets" is adopted rather than a more technical term such as "infrastructure assets" or "facilities".

The idea of common property contributing to social cohesion has a respectable ancestry. Even John Bodin, making a strong case at the end of the sixteenth century for modern private property, argued that "in any state there must also be some common property without which there can be no sense of community and hence no viable state (MacPherson, 1978, p.10) – an early recognition of social capital. An appreciation of common property may also encourage consideration of intergenerational issues such as the depletion of heritage assets and natural resources and has affinity with concepts such as "the common heritage of mankind" which has emerged in the literature of international law and politics. A notion of private property, which gives the present owner the right to destroy the assets, cannot adequately handle such matters.

Japan has made a reasonable start on the pension liabilities issue but more remains to be done. Information on who receives the benefits, the cost, and how the cost is funded, is necessary to stimulate collaboration prevent free-rider behavior. At first glance, such information might enhance the tension between taxpayers because of the imbalance of benefits and burdens in the public services. However, in order to reach a democratic consent on resource allocation, deliberative processes based on full and clear information is needed. Perhaps we need to think of accounting as a *communication* discipline and not just a *measurement* discipline – what may be important is that the accounting information is a basis for ongoing dialogue between stakeholders (including governments). To this end, continuous reporting, rather than periodic backward-looking reports may be important.

SUMMARY AND CONCLUSIONS

Japan, which has so far been slow to reform its government, has experienced both fiscal stress and political scandal in recent times and is beginning to make some changes. There has been emphasis on disclosure in the new whole of government balance sheet but this has not been accompanied by a comprehensive overhaul of internal accounting systems so as to produce information on the full costs of outputs. Consequently, Japan does not produce statements of revenues and expenses or costs of services (other than in IAIs) which would facilitate public accountability and decision making.

In terms of issues which have collective and intergenerational consequences – notably infrastructure assets, defence assets, heritage assets and pension liabilities – the disclosures in the Japanese government's balance sheet compare favourably with those of other nations. However, it is apparent that there are a number of accountability and disclosure problems in all countries arising from shared responsibilities with local government, private sector commercial ventures and citizens at large. We suggest that these problems cannot be adequately addressed within an individualistic paradigm, such as is promoted by NPM, in which government is viewed as a separate organizational entity. We propose instead that these, and the agenda for CIGAR research, be addressed within a wider concept of governance. As Metcalfe (1993, p. 292) points out:

> If the basis of public management reform until now has been the imitation of business management, the challenge is to move on to innovation; the development of new methods of management appropriate to the distinctive needs of government.

What Metcalfe says about public management applies equally to accounting. The main challenge is not the adoption of accrual accounting from the commercial sector into governments. This deals with managerialism-driven reform at the micro-level within an NPM paradigm but not with macro-level problems in which governments are invariably implicated. The real challenge for accounting innovation lies in finding better ways of accounting for collective decision making under new governance approaches.

NOTES

[1]. At the time of research these countries (together with the IASB) were the member countries of the "G4+1" group which was influential in international accounting policy making.

[2]. This is a modification of the three directions of governance shift proposed by Pierre and Peters (2000): moving up, moving down and moving out.

[3]. Putnam (2000), however suggests that citizens' participation in non-profit and community activities has decreased since the 1970s.

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SIR ANDREW LIKIERMAN

THE NEW UK GOVERNMENT FINANCIAL FRAMEWORK

The new UK government financial framework, known as resource accounting and budgeting (RAB), is almost complete. This article sets out the basis of the new framework and a brief history of the project. It describes some of the issues involved in implementing the new framework, including development of the required skills, and the benefits of doing so. Finally the article considers whether the project has been successful and indicates the directions of future work.

For those unfamiliar with the term "resource accounting" and "resource budgeting", these are terms of art devised for the UK project. Resource accounting is a set of accruals-based techniques for reporting on the expenditure of UK central government departments and the relationships between expenditure and departmental objectives. Resource budgeting is the use of resource accounting information and principles as the basis for planning and controlling public expenditure by departments. In addition to the move from cash to accruals, RAB incorporates a charge for the cost of capital. The new framework covers not only procedures within government, but also to the way the government requests resources from Parliament and reports to them on what it has spent.

In addition to the planning, control and reporting on government expenditure, the new information is being used to improve information for national accounting purposes, and a future development is to provide accounts covering the whole of public sector. This will start with statistically based accounts and, after a series of pilots ("dry runs") will provide accounts based on UK generally accepted accounting practice (UK GAAP) for 2006-7.

1. THE PROJECT

RAB can be seen as the final stage in applying accruals-based principles to the public sector. Other parts, starting with public corporations, then successively local government, health and the agencies of central government have already made the move. It can also be seen as an extension of many of the principles laid down over the previous 10 years in increasing the sophistication of financial management in the public sector as well as a part of the overall reform programme for the public sector (see for example Balls and O'Donnell, 2001).

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 145-156.

Why, then, had these principles not been applied before? One reason was concern that the strength of the existing cash-based discipline should not be undermined. Another may well have been that many saw the accruals basis as essentially a private sector discipline. But increasing dissatisfaction with the limitations of cash (especially for capital) in decision-making and difficulties in reconciling the government's financial framework with traditional Parliamentary control methods dating back to 1866 provided good reasons to consider a change.

There were also pressures for greater accountability and transparency, especially in demonstrating value for money. The fact that these techniques were already being applied elsewhere in the public sector and that other countries were either considering (and in the case if New Zealand had already completed) the change, combined with the falling cost of technology, provided additional reasons for doing so. One reason which is of interest because it is absent was noted by Wright (1995). Commenting on the planning and monitoring proposals he wrote "Not since the ...1960s...has a change of such magnitude been introduced unprovoked by either a financial or an economic crisis".

Following the announcement to explore the possibilities of the change (Clarke, 1993), there were extended periods of planning and preparation. These were seen to be necessary because of the uncertainties about the quality of existing departmental accounting systems, the desire to minimise costs in providing new information technology and the importance attached to ensuring that the new information, especially for planning and control, was robust from the beginning.

The confirmation that there would be a move to resource accounting, and that Parliament would be asked to agree to a change in the form of reporting to them, were announced in 1994 (HM Government, 1994). A year later the move to resource budgeting was announced (HM Government, 1995). In the same document, more details were given about the form of reporting. This was to be based on 5 audited statements for each government department:

1. Summary of resource outturn (providing information for Parliamentary control purposes)
2. Operating cost statement (the central government equivalent of the profit and loss account) with a statement of recognised gains and losses.
3. Balance Sheet
4. Cash flow statement
5. Statement of resources (the cost of each of the department's aims and objectives)

The next three years were marked by intensive activity in departments and the Treasury to implement these decisions. Accounting manuals were prepared which were based on UK GAAP, adapted as necessary. Within departments, new systems were introduced to provide information for the resource accounts and a pilot set was produced for 1998-99.

2000 was the key year in the introduction of the new framework. In July, the biannual public expenditure spending review introduced the first phase of resource budgeting (HM Treasury, 2000a), legislation was passed to allow the change to reporting to Parliament (HM Government, 2000) and Parliament agreed to discontinue the traditional cash-based Appropriation Accounts (PAC, 2000). Later came the publication of the first set of resource accounts, covering 1999-2000.

At the time of writing (2002) implementation is almost complete. The last set of cash accounts was produced for 2000-1, Parliament has voted resources rather than cash for the first time in 2002 and the spending review of that year has implemented the second stage of the transition to resource terms (see further details below).

Although the process has been an extended one, it is not clear, in retrospect, that it should have been undertaken any faster. The need to consider complex issues, such as the valuation of defence, transport infrastructure and heritage assets required careful consideration. So too did the conversion of departmental systems. Of course, again in retrospect, certain elements could have been accelerated, but in terms of planning, the team responsible felt that they had made an appropriate judgement about the balance of risk and result in proceeding at the planned pace.

2. RESOURCE BUDGETING

The budgeting aspects of the new framework will have the most far-reaching managerial implications. Since many governments appear more cautious about moving from budgeting in cash terms to an accruals basis than moving reporting, it may be worth setting out how the introduction was approached.

The UK has a cycle of three year rolling public expenditure budgets (spending reviews), updated every 2 years, when the third year of one spending review becomes the first year of the next. In 1998, two years before the first spending review using accruals-based figures, a pilot was conducted with a number of departments to see how the process might work and what problems might be encountered. The following year all departments were asked to participate in an extended pilot exercise. This was intended to ensure that they were aware of the implications of the changes, and to see what problems might arise for each.

As a result of the pilot studies, it was decided to make the transition in two stages. For Stage 1 (the 2000 spending review) the large non-cash items (including depreciation of about £8 billion, capital charges of about £13 billion and most provisions) were to be managed on an annual basis, and only a few were to be included in the three-year limits. The 2000 spending review was conducted on a mix of cash and accruals figures, with the some accruals adjustments made at the end of the process. Two years later came the second stage. In the 2002 spending review, the non-cash items were moved onto a 3-year basis and the whole process was conducted in accruals terms from the start (HM Treasury, 2001a).

The reason for this two-stage process was to reflect the fact that some figures at the early stage were not sufficiently robust to meet concerns by departments and the Treasury about the risks in seeking to manage some of the accruals items over a 3-year period. The process of piloting and a staged introduction has proved successful in ironing out problems and allaying fears about what for many was an unfamiliar set of principles.

3. THE BENEFITS

There are four ways in which the changes are already providing, or will provide, benefits. Some examples (taken from HM Treasury, 2001b) are given in Annex A.

1. *For each department.* Information is now available first the first time on the assets and liabilities of each department, to enable those responsible to take decisions, make comparisons with other bodies in the public and private sectors and to focus on the outputs and outcomes, rather than inputs. To further assist this process, the introduction of capital charging is intended to make better use of the resources used by central government.
2. Indeed for the first time departments have the information to enable them to manage their fixed assets and their working capital. This has required training for these managers and an additional benefit for central government as a whole has therefore been an improvement in their financial knowledge and awareness.
3. *For Parliament,* the new framework provides them with far better information than they have ever had before to enable them to monitor departments. There is not only a greater depth and breadth of financial information, but with additional information made available through Performance Service Agreements (PSAs) (HM Treasury, 2000b) and Service Delivery Agreements (SDAs) (HM Treasury, 2000c), links can be made to outcomes and performance.
4. *For the management of central government as a whole,* the improved information provided by RAB allows for a better basis for the allocation of resources through the planning mechanism of the spending reviews and a more strategic approach to the planning process. In doing so, it underpins the modernising government agenda by allowing for better quantification of output and outcome information. In giving a balance sheet perspective, it also mitigates any potentially perverse effects of the annuality principle by which expenditure control is exercised.
5. Finally, *for the management of the economy,* the improved information plays an important role for the "Golden Rule" that borrowing will not be used to finance current expenditure. It is also essential to construction of an improved National Balance Sheet and other macroeconomic measures (HM Treasury, 1997a). It has also been incorporated in the government's Code for Fiscal Stability (HM Treasury, 1998).

It is worth illustrating how these benefits come in stages, since it may not always be clear to those unfamiliar with the process that the initial impact is only the start of the process of deriving benefit from the changes.

To take one example, there is a great deal of work for departments involved in completing fixed asset registers. The process of ensuring that fixed assets are first identified and then valued on the new principles may be costly and time-consuming. The immediate benefit is to be able to ensure that fixed assets are properly catalogued for good housekeeping purposes. As a result of this work it became possible to publish a National Asset Register, first without values (HM Treasury, 1997b) and then with values (HM Treasury, 2001c) – see Annex B. However this is only the start of the potential benefit from better accounting for fixed assets, which will come mainly from managing the asset base to ensure that the fixed assets are deployed by departments in the right way to achieve the required outputs and outcomes. This is difficult to achieve unless the fixed assets are properly identified in the first place.

Another example is in the management of working capital. As already noted, under cash accounting, working capital was not identified separately. The requirement for a balance sheet has meant that proper accounting is required for stocks, debtors, creditors and cash. As with fixed capital, this can prove a difficult process, particularly if there is extensive use of suspense accounts with cash accounting. But while the rationalisation of these accounts can itself prove very valuable in "cleaning up" the accounts, once again, it is the management of working capital that provides the full benefit of providing the new information. Many departments have been found to have surprising amounts of working capital. Making this visible will enable better control to be exercised.

Only some of the benefits come directly from the changes. Others reinforce reforms already being implemented. Thus the better identification of costs, improvements to control of stock and cash, enhanced performance measurement systems, and a good deal of financial training had already been taking place before the start of the RAB changes. But RAB has been an important influence in reinforcing these changes. For example, in the case of many stock control systems, it forced an acceleration of the change programme and in the case of financial training, it provided a clearer focus for the training taking place.

Of course not all financial management processes changed as a result of the introduction of RAB. The investment appraisal process, for example, was robust enough not to require changes.

It is also worth noting that not all commentators agreed that the benefits outlined above would be reaped. Included among the concerns were whether the changes would be worthwhile for management and whether they would deliver the full potential. These and other issues are discussed elsewhere by the author (Likierman, 2000).

4. SOME REPORTING ISSUES

The development of the reporting aspects of the new framework has revealed a number of important issues of principle and facets of practice in implementation. Two issues of principle – the monitoring of the standard-setting process and the perceived danger of creative accounting are set out below, followed by two facets of practice - the implementation process and the analysis of the information for the future.

As already noted, the accounting framework is based on UK GAAP, adapted as necessary. One major issue, which arose at an early stage of the planning process, was whether it was right that the Treasury should act as sole arbiter of what was a necessary adaptation of UK GAAP. While Parliament welcomed the use of UK GAAP (TSC, 1996; PAC, 1997), it urged the Treasury to stick to it as closely as possible.

Concern was expressed, not only by Parliament, but also by the accountancy profession that there should be external scrutiny of the proposed accounting framework. As a result, the Financial Reporting Advisory Board (FRAB) was set up to provide an independent element in the standard setting process. The Board was constituted in 1996 with an independent Chairman (the former Senior Partner of Ernst and Young in the UK) and an equal number of members from inside and outside government. It has since scrutinised the Treasury's proposals and published public reports on its findings (HM Treasury 1997c, 1999, 2000d, 2001d). The value of this work has been acknowledged by both government and Parliament, indicating that it appears to have worked well.

A second, related, issue of principle was concern that the problems of "creative accountancy" which had bedevilled the private sector, should not affect the integrity of the figures for central government. Such concern was understandable, bearing in mind that the previous years had seen a number of commercial scandals that had involved creative accounting, notably Maxwell Communications Corporation and the Bank of Commerce and Credit International.

Concern died down, however, when it was seen that the safeguards in place were far more substantial than those in the private sector and that there were a number of constraints not present in the private sector. These start with the reduction in the scope for judgement built into the accounting framework of the Resource Accounting Manual (HM Treasury, 1997d), accompanied by rigorous monitoring of departmental practice by the Treasury. The activities of the FRAB, as already noted, provide further safeguards. Then there is the work of the National Audit Office, who not only act as auditors but in doing so apply a single set of standards across central government, thus reducing the opportunity which has caused problems in the private sector of playing off one auditor against another. Finally there is the scrutiny function of Parliament and, more indirectly, the press. It is also important to note that several of the most prominent areas of creative accounting, including mergers and acquisitions, foreign currency transactions and the definition of revenue, are not present in central government.

Turning to the first aspect of implementation, producing the new accounts turned out to be more difficult than expected for many departments. It was known from the beginning that those departments with significant asset holdings but without a great deal of sophistication in some key existing systems (notably the Ministry of Defence) would find the transition a problem. In the event, many of the problems were in departments without a major task in making the transition, but where action was not taken early enough to provide the systems and acquire the necessary skills. The decision, therefore, to go for a "dry run" set of accounts and then allow for parallel running with the existing cash accounts for a period of two years turned out to be wise in retrospect. 30 out of 50 of the first set of dry run accounts, covering 1998-99 were qualified by the National Audit Office. Two years later the number had dropped to 8 and, even more important, the qualifications were far less severe.

For the future, the development of the new framework provides the opportunity to analyse departmental information in a similar way to the scrutiny commonly used for commercial organisations. Yet the conventional ratio analysis for commercial organisations, with its use of measures which require a stock market price (such as the price-earnings ratio) or assume commercial borrowings (such as the gearing ratio) did not provide an easy read-across for central government.

A new set of ratios was therefore devised so that the figures could be analysed. The ratios included those related to staff, departmental costs as a whole, elements of the costs (such as staff) measures for working capital, for fixed assets and for cash flow. Intended as the basis for further work in this area as experience develops, two booklets describe the ratios, one as a summary for users (HM Treasury, 2001e) the other providing a full analysis of a set of resource accounts (HM Treasury, 2001f). This form of analysis will become more valuable as a sequence of resource accounts is produced, allowing trends to be analysed. But it is already of use, especially in conjunction with other information publicly available about departmental activities and expenditure.

5. DEVELOPING THE SKILLS

In order to get the full benefits from the introduction of RAB, a programme has been devised which started almost as soon as the change was announced. This has meant a strategic view of the needs of central government, while recognising that it is departments themselves that will have to deliver the training, adapted to suit their own requirements.

It was assumed from the start that departments should not acquire the new skills only by hiring additional finance specialists. While new hiring of this kind might form part of the required skill set, much would have to be through other methods. These included training existing staff to be finance specialists, bringing in temporary help and providing some training in use of the information by a large number of non-specialists.

The needs were identified through establishing a competence framework to enable departments to understand what was required. The framework specified the skill levels for certain tasks and it was regarded as most important that skill levels should be appropriate, with a hierarchy of skills to correspond to the very different tasks required. Thus many lower-level tasks would only need a lower-level technician qualification, while existing finance staff would need some specific retraining. Senior policy analysts and those using the information for high level decision-making, on the other hand, would require highly focussed awareness training to meet their very different needs.

It was also made clear that training required very careful timing, so that it was delivered just ahead of when it was required. Too early and the person might have moved job or forgotten what had been taught because it had not been used for a long time. Too late and the training would be wasted.

The process of helping departments was started by creating a network of departmental contacts to exchange information and ensure that they did not "reinvent the wheel" because they were not aware of developments elsewhere in central government. This network later became a more formal interdepartmental Finance Training Committee to discuss comments needs as the date for implementation drew nearer. To help them, a booklet was produced which set out the training framework in full, including guidance on the knowledge required by different functions within departments (HM Treasury, 2001g).

6. WAS THE PROJECT A SUCCESS?

There are two aspects to answering this question. First, whether the project was delivered successfully. Second, whether the benefits have been realised.

Looking back at the original plan, finalised in 1995 (HM Government, 1995) it would be reasonable to conclude that the overall objectives have been achieved. Accounts, budgets and Parliamentary Estimates have all been produced on the new basis and to the timescale envisaged. The changes have achieved cross-party support and in particular have been welcomed by Parliament. This does not mean, with the benefit of hindsight, that there might not have been some actions that might have smoothed the path of the transition. But the reasons most commonly responsible for project failure appear to have been avoided.

As for whether the anticipated benefits have been achieved, it is too early to make a definite judgement. But there is already some strong evidence of what has already changed. The new framework is now "the system", not an aspiration and the evidence of change at departmental level is growing all the time. The fall in the number of qualified departmental accounts (with further falls anticipated) is also encouraging. A solid basis has been provided for the development of Whole of Government Accounts. A final piece of circumstantial evidence is that the UK experience has been sought by many other countries considering similar moves.

7. THE FUTURE

There are still some elements of the new framework to be improved, including the quality of the accruals-based financial information from some departments. But the challenge for the future is to ensure that full use is made of the enormously improved information now available in central government. Concern has been expressed about whether the cultural change required of departments is not too great, bearing in mind that there is no history of using such information and that it is complex for non-specialists to understand.

There is no doubt that the process of understanding and using the new information will take time, and this is one reason why such an emphasis has been placed on training. This training will need to be sustained over many years, since only when the information has been available for an extended period will a whole new generation be familiar with it. The series of "Managing Resources" booklets, starting with an overall introduction (HM Treasury, 2001h), many of which are given in the list of references, is intended to act as a useful source of continuing material for dissemination of information and for training purposes.

Meanwhile there are some powerful incentives to learn about the new framework The fact that budgets are now denominated in resource terms through the spending reviews will mean that the new figures are relevant to a far wider range of civil servants than those dealing with financial matters alone. And the range of those involved will increase further in 2003 once the control mechanism is denominated in resource terms following the 2002 spending review. There will also be pressure on those at the very top of departments to understand the details of resource-based information from late 2002, when accountability to Parliament will be through scrutiny of the new resource accounts.

Meanwhile the potential for using the information is increasingly clear. The examples from practice so far (a few of which are set out in Annex A) indicate that improved financial management will enable departments to achieve improvements in efficiency and effectiveness and thereby to do more with the resources they have. At a time of constrained resources this will be a valuable additional element in making the most of what is available. Accountants in government have much to contribute to doing so and this process in turn will mean that accountants need to be integrated into the mainstream of government business. Accountants in government, too, will need to rise to this challenge.

ANNEX A - SOME EXAMPLES OF THE BENEFITS OF RAB

Asset management

The move to RAB resulted in the Foreign and Commonwealth Office improving its asset management. The department used the proceeds from property sold over a two year period to refurbish other buildings and invest in information technology, new posts abroad and staffing in key areas of work.

Working capital management

A significant benefit to the Serious Fraud office from adopting RAB has been the explicit recognition of cost awards made against convicted fraudsters and in the Office's favour as debtors. This has raised the profile of the issue of how much money is due to government but is not being collected by the Courts.

Costs

The RAB treatment of student loans has enabled decisions on loan expenditure by the Department for Education and Skills to be made on the basis of the full long-term cost of making the loan, rather than the transactions in the early years. The cash treatment of subsidised loans involves the full cash cost of making the loan being recognised up front, with the result that the loan is treated no differently in the accounts from a grant. In later years loan repayments count As negative expenditure, but the cost of the subsidy is not recognised. Under RAB treatment, only the cost of the government subsidy plus the likely amount of bad debt is treated as a cost (through making a provision in the current budget). This provides a clearer measure of the real cost of making loans and brings out the benefit s to the taxpayer of support through loans rather than grants.

Budget planning

By focussing on fixed asset management, capital planning and working capital management, resource-based information has enabled the Department of Culture, Media and Sport with a better basis for allocating administrative resources to divisional objectives and outputs.

Performance management

The Royal Navy has used resource-based information as part of a balanced scorecard to enable the Navy Board to monitor performance. The four dimensions of the scorecard are outputs, resources, process and deployment. These are derived from the high level Naval Strategic Plan and linked to a risk analysis which identifies critical areas for attention.

Delegation

The Scotland Office's management information systems, which was installed to meet the requirements of RAB. Has allowed the department to devolve financial control to individual budget units

Training

The Ministry of Defence introduced a "finance licence" scheme whereby staffs in finance posts undertake a computer-based assessment package to determine levels of skill and knowledge set against set competences. Areas of weakness are underpinned by training sessions to aid staff in completing the assessments. On completion they are awarded a "finance licence" which confirms their suitability for their current job.

ANNEX B – THE NATIONAL ASSET REGISTER

In 2001, the government published a National Asset Register (HM Treasury, 2001c). 920 pages long, it gives details of the assets owned by central government departments, using information used in compiling departmental asset registers in order to produce resource accounts.

A National Asset Register had already been produced four years earlier (HM Treasury, 1997b), but because the departmental asset registers were not yet ready and valuations were not yet available, it could only signal the main areas of asset ownership.

The 2001 register provides a huge amount of detail about the assets. The largest values were attached to nuclear submarines, but inevitably a great deal of press attention was devoted to more exotic items, such as the ownership by the Department of Trade and Industry of Newton's Apple Tree (entered at no monetary value), the cost of Trident nuclear submarines (nearly £800 million each) and the valuation placed on the Prime Minister's residence at 10, Downing Street.

Of long-term significance was the fact that details were given of acquisitions and disposals of assets since the 1997 National Asset Register. There was also a commitment to regular registers of this kind every 3 years in which acquisitions and disposals would be disclosed.

As far as is known, the 2001 National Asset Register was the first of its kind in the world to be published.

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KRISTINA LUNDQVIST

CURRENT STATE AND LATEST DEVELOPMENTS OF GOVERNMENTAL ACCOUNTING IN SWEDEN

1. INTRODUCTION

My intention during this session is to give an overview of central government accounting in Sweden. I will focus on the current situation and latest developments. I will also try to describe some experience we have gained in Sweden and highlight some issues that I find interesting in a government accounting perspective. I shall especially highlight the need to consider special government characteristics when moving towards private sector accounting principles.

I dare say that Sweden is one of the front-runners in the field of government management reforms. However, many of the initiatives we have taken are not very well known abroad. One reason for that, I believe, is that we do not have much information in English. I have personally tried to take steps in order to spread information. Giving this presentation today is a small step. I have also recently finished a position paper entitled Accrual Accounting in Swedish Central Government (ESV 2001:8). It is available on our web-site.

2. ORGANISATIONAL STRUCTURE OF THE SWEDISH PUBLIC SECTOR

By way of introduction I would like to give you an overview of the Swedish public sector.

The public sector consists of a central government sector and a local government sector. The local government sector consists of counties and municipalities.

The municipalities are responsible for local issues in the immediate environment of the citizens, for example primary and secondary education, childcare, care of the elderly etc. The main responsibility of the county councils is health and medical care.

The central government sector consists of Parliament and Government, and under the government there are ministries and agencies. The central government is also represented at the local level as some of the agencies have large regional organisations.

This presentation will focus on central government accounting.

The ministries are relatively small and their task is to act as policymakers and prepare decisions of the government. The agencies are responsible for carrying out government activities.

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 157-165.

In my way of counting there are approximately 300 agencies, or authorities. Their size, structure and types of operations vary considerably. Each agency is responsible for its own accounting and reports. The accounting methods are designed as if the agencies are completely independent units, even though they are part of central government and therefore not independent legal entities.

The central government has approximately 235.000 employees.

The National Financial Management Authority is the agency I work for. In Sweden this agency is known as ESV, which is the name I will use in this presentation. The ESV is the government agency for financial management in Sweden and is, among other things, responsible for development of generally accepted accounting practice and for consolidation of accounting information. I am head of a unit responsible for accounting principles and regulations.

3. FINANCIAL MANAGEMENT REFORMS

I would also like to give you an overview of important financial management reforms in Sweden. Some of these reforms were started in the late 1980s and they were all fully implemented in the 1990s. Key words for these reforms are flexibility and performance.

Considerable flexibility in the use of resources was introduced in the late 1980s. This means that a government agency can decide itself how much it will spend on salaries, consultants, travelling etc. Flexibility in spending over fiscal years was also introduced in the late 1980s. This means that the agencies can carry over unused appropriations to the following year. It also makes it possible to spend a part of the following year's budget in advance.

As regards performance, we have seen a shift in focus from resources used to performance. Thus, the outcome of the agencies' activities – the result –is more important than the resources put into the activities. The result can be both in terms of output, such as products and services, and in terms of effects for individuals and society.

Flexibility and the focus on performance are linked to an increase in accountability for financial and operating results. The annual report is a very important tool in this respect. From 1993 all government agencies have had to submit annual financial and performance statements on an accrual basis. The new accounting model makes it possible to monitor performance such as total costs of government programmes and activities. With complete cost accounting it is possible to distribute cost to various products or activities. The implementation of a new accounting model was therefore essential for implementing management by results.

Other financial management reforms in the early 1990's are related to cash management and the allocation of interest expense. The use of interest-bearing accounts with credit facilities for both appropriations and other government funds promotes good cash management. The launching of a system of internal loans to finance investments in fixed assets has had the effect that interest expense is allocated to the agencies. This way a more correct cost allocation is achieved – a sort of capital charge.

The most recent financial management reform is the new budget process from 1996. It includes the setting of a ceiling on total centrally-financed expenditure for each one of the following three years. The ceiling for the following year is broken down into ceilings for 27 expenditure areas.

4. APPLICATION OF ACCRUALS

In a way, the Swedish central government has introduced accrual accounting by taking one step at a time.

The first step was taken at the agency level. This was because the main reason for implementing accrual accounting in Sweden was to facilitate management by results. From July 1993 all agencies have had to use accrual accounting as the general accounting principle. Once a year they have to submit an annual report including financial statements and a performance report. The financial statements are:

- the statement of financial position
- the statement of financial performance
- the cash flow statement and
- the appropriation report

The second step was taken when consolidated accounts were presented on an accrual basis. A consolidated annual report for all of central government has been produced from the financial year 1993/94. Up till now this report has mainly included financial information. However, it is being discussed that the report also should include information on performance.

I should also mention that the submission of a consolidated annual report was not the aim of the reform, but rather a possibility provided by the reform. The consolidated financial statements have, however, gained in importance. It is now stipulated in our budget law that Government shall submit an annual report to Parliament each year.

The third step has still to be taken. We are on our way but we have not yet taken the whole step. What we are struggling with is the implementation of an accrual-based budget decided by Parliament. Up till now the state budget has not been presented on an accrual basis. This is now on the top of our agenda and the plans are that the budget for 2004 will be on an accrual basis. The issue is being dealt with by our Performance Budgeting Project and I will present this project in more detail later on.

5. STATE BUDGET AND ACCOUNTING – DIFFERENT SCOPE AND BASES OF ACCOUNTING

As I already mentioned the state budget and the general accounting currently have different accounting bases. They also have different scope.

The general accounting is on a full accrual basis and comprises total operations irrespective of financing. Besides appropriations from the state budget many agencies also have other sources of finance, such as fees, user charges, grants and donations as well as internal loans and leasing. All these types of income, as well as related expenditure, are recognised in the agencies' accounts as well as in the consolidated annual report.

However, the central government budget differs from the general accounting in both these two respects.

First, the central government budget – and the related accounting- only includes those transactions that affect the central government borrowing requirement. The consequence is, somewhat simplified, that the state budget only includes appropriations and state budget revenue. This means that the budget does not include activities financed by donations, fees, charges etc. and therefor the scope of the budget is narrower than the general accounting.

Secondly, the budget is presented partly on a cash basis and partly on a modified accrual basis, instead of on a full accrual basis. Actually transfers and taxes are presented on cash basis and other types of expenditure are presented on a modified accrual basis. The accounting is organised in a way that deals with this discrepancy. For example, special accounts are used for cut-off items, such as accrued or prepaid expenses. These accounts are either included or excluded, depending on the report produced or the type of analysis one wants to make.

6. PERFORMANCE BUDGETING PROJECT – REFORM PROPOSALS

One important aim of the so-called Performance Management Project is to use the same scope, principles and presentation format in budgeting and in the financial accounts. At the end of last year the project therefor proposed changes of this type, including the move to an accrual-based budget. The proposal was presented in a White Book by the Swedish Ministry of Finance.

The project is very large and performance management is an important issue. Besides focusing on the principles and the structure of the budget the project also focuses on the budget's role as a management and control tool.

The white book proposes a structure for performance management and control that is two-dimensional: an activity dimension and an institutional dimension consisting of the agencies. This means that both the budgeting and the follow-up will be done in both dimensions. The activity dimension is made up of a three-tier hierarchy. The highest level in the hierarchy is the policy area, for example regional development, health or defence. The second level is made up of programmes, for example research in a certain area. The programmes may span several agencies. The third level, called sub-programmes, is contained entirely within one agency.

The overall aim of the project is to make possible a clearer linkage between objectives, outcomes and costs. Thereby the co-ordination between management by results and general financial management is supposed to increase.

At the moment the Ministry of Finance and the ESV are working together on the implementation issues of the proposal.

7. ACCOUNTING REGULATIONS

The Government and the ESV issue the main accounting regulations. The Government issues ordinances and the ESV issues supplementary regulations that include more detailed rules and clarifications. All regulations concerning central government accounting and financial management are gathered in a book, which comes out in a new edition every year. The whole book is also available on our web-site (in Swedish).

The accounting regulations in the central government sector follow very closely the laws and standards in the private sector. This means that our regulations are quite similar to the IASC standards. We continuously monitor the development of new principles and standards in order to identify needs to change our regulations. Of course, we always have to consider special characteristics of the public sector.

In our work on regulations we also have to consider the requirements of the international standard System of National Accounts and the IMF's Government Finance Statistics (GFS).

I should also mention that during the last couple of years we have put more focus on the standards issued by IFAC-PSC. My opinion is that they have gained in importance.

8. FRAMEWORK FOR GOVERNMENT ACCOUNTING

In 1998 we decided to develop a framework for government accounting in Sweden and a preliminary version was finished in 2000. The framework describes underlying assumptions and principles for accounting, such as the elements of various reports and qualitative characteristics.

There are several reasons why we decided to draw up a framework. One purpose was to provide guidance in the development of new accounting regulations. We believe that having a framework will promote uniform and consistent accounting rules.

The starting point for the development of our framework has been the IASC framework. We have also studied the framework developed by FASAB and other relevant material, such as research on the subject. The main reason why we used the IASC framework was to save time and resources.

However, there are many issues specific to government that need to be taken into consideration. As you know the IASC framework is adapted to business accounting and has primarily the investors in mind and their needs of information. The activities of non-profit organisations have a different goal and output and outcomes are normally more relevant than profit. Other specific characteristics we have had to consider are

- the sovereignty of the government,
- the governance situation
- the demand for openness and transparency,
- the scope of the accounting entity,

- special types of assets, as well as
- special types of revenue and expenses

At the moment we have just started a work on revising our framework, and to solve those issues we did not have the time to solve in the preliminary version. A new edition will be finished in the beginning of 2002.

9. SPECIAL ACCOUNTING ISSUES: ASSETS

Now I would like to give further information on how we treat some special types of assets as well as revenue and expenses. I will start with assets.
Assets are normally valued at acquisition value less depreciation. We regard the acquisition value as the resources sacrificed for the acquisition of the asset, which should be distributed over the economic life of the asset. Private companies in Sweden also use acquisition value.

9.1. Infrastructure

We do recognise investment in infrastructure as an asset. For example, roads are depreciated over 40 years. In our opinion, infrastructure makes it possible for government to provide service potential in terms of roads, railways etc., and therefor should be regarded as assets. There are also other aspects, such as the comparability aspect implying the need to make financial comparisons between different financing alternatives. In Sweden, for example, we have Public Private Partnership arrangements as one alternative. This seems to be increasing in frequency.

I should also mention that maintenance expenditure to retain service potential is treated as expense.

9.2. Military assets

Defence materiel such as vehicles, weapons and other equipment, are also recognised as assets. This principle has been in effect since 1998. Before that a distinction was made between materiel used for training on the one hand and materiel kept in reserve, on the other. There are two reasons why all military equipment should now be treated similarly to other assets. One is practical: it has been difficult to distinguish the equipment used for training purposes from that kept in stock. The other reason is more theoretical: keeping military equipment in stock can be regarded as an insurance providing a service potential for each generation of citizens. Therefore the expense should be recognised in the years when people enjoy this benefit.

9.3. Intangible assets

From 2002 expenditure on development activities is to be recognised as an intangible asset if the asset is expected to be of considerable value to operations. The principle follows IAS 38. Up till now the regulations have been somewhat unclear as it has been stated that research and development may be recognised as intangible assets under certain circumstances. Expenditure on research shall always be treated as an expense from 2002.

9.4. Heritage assets

Heritage assets are the only exemptions from the rule that all assets shall be accounted for. Heritage assets were excluded from the accounts when the agencies constructed their statements of financial position in 1993. The reason was that, in many cases, information on acquisition cost did not exist. Also, these assets were judged to be of no interest in respect of the aim of the reform, i.e. to contribute to better financial management. Even heritage assets acquired after 1993 *may* be excluded from recognition. We are currently investigating how the accounting principles for heritage assets can be improved and made more uniform.

10. SPECIAL ACCOUNTING ISSUES: REVENUE AND EXPENSES

10.1. Taxes

Collection of taxes is normally recognised as income when a tax liability is issued to the taxpayer. Earlier recognition than this is, in most cases, difficult due to the criteria of probability and measurability.

10.2. Transfers

Government transfers are normally recognised as expense when the payment is made. The reason is that the payments are regarded as discretionary until payment is made. However, this is a very difficult area and it has been identified as an area that we need to study in more detail. For example, up till now, we have not made any clear distinction between different types of transfers, such as entitlements, transfers under shared cost agreements and grants.

Collections of taxes and transfers are to be accounted for in specific sections in the agencies' statements of financial performance and should be regarded as revenue and expenses. It was concluded that this would be the best way to collect and consolidate information on taxes and transfers.

10.3. Reversed Matching

As regards the matching principle we often use "reversed matching" in the sense that revenue for the period is matched against cost instead of vice versa. The statement of financial performance starts with revenue from operations. However, there was a great deal of discussion when the accounting model was developed whether it would not be more appropriate, in the government sector, to start with expenses.

11. EXPERIENCE

The implementation of accrual accounting went smoothly and the direct goal of facilitating result management was achieved. We have also achieved greater transparency, better financial control and better financial awareness in general.

However, we have experienced that the accrual-based information is sometimes of secondary importance. As mentioned earlier the budget approved by Parliament is presented partly on a cash basis and partly a modified accrual basis. Because of this the accrual based financial statements do not always receive the attention that they should receive. In the follow-up process the focus is often on the budget and its appropriations. Parliament has decided on appropriations in the budget and, when monitoring operations, the appropriations (on a cash or modified accrual basis) are, naturally, the most important follow-up items.

The focus on appropriations can also be explained by the new budget process. The appropriations constitute the expenditure ceilings and are therefor monitored very closely. The new budget process also focuses on macro restrictions. As these restrictions often are on a cash basis, the accrual basis has, maybe, lost somewhat in importance. In any case, it has not facilitated the implementation, the acceptance and the use of accrual accounting in the ministries. In a way, we can see a conflict between economics and financial management.

We have also learned that it is very difficult to abandon old routines and replace them by new ones. Both agencies and ministries often tend to add the new routines to the old ones and this often makes the accounting more complicated than it should be.

On the other hand the annual report has become more important. In the first place the submission of an annual report for whole of central government has been stipulated in law since 1996. In the second place there have been high demands to bring forward the time of submission and to make sure that the different agencies apply the accounting regulations in the same way. In addition Parliament has also requested improved methods for result management.

12. PRIVATE SECTOR ACCOUNTING VS. PUBLIC SECTOR CHARACTERISTICS

Starting from a sort of traditional government accounting, which I would call appropriation accounting, there has been a general trend for government accounting principles to move towards the principles used in the private sector. We have seen this trend in Sweden. To a large degree this development has been an advantage to us, but the Swedish experience is that some accounting policies are not relevant for government accounting. Therefor we are currently seeing a need to focus on special public sector characteristics.

As regards private sector accounting policies, there has been an orientation towards market values and a focus of this type is not as relevant, in the public sector. For example, IAS 36 Impairment of assets points out future cash flows as an important basis for estimating the need to write down the recorded value of an asset.

However, in the government sector the ability of certain assets, for example property, plant and equipment, to generate future cash flows or service potential to a certain entity is not affected in that way. Therefore, in our opinion, property, plant and equipment should primarily be considered impaired if the asset has been destroyed or if it is used for some other purpose than originally intended.

We support the development of standards by IFAC-PSC. However, we would like to emphasise the need to place a special focus on government-specific issues. It is not possible merely to take over private sector accounting standards since the underlying basic accounting theories are not the same. Actually we see a need to have more theories developed with regard to non-profit organisations.

In my introduction I stressed the need to consider special government characteristics when moving towards private sector accounting principles. I hope it has been clear to you why there is this need and what special problems we have to face, those of us who work daily with government accounting.

Tomorrow there is a session focusing on the setting of governmental accounting standards. I look forward to that session, as it is very much in line with what I have been talking about and what I am interested in. For example, I am very eager to know which direction IFAC is taking. How far can harmonisation go?

VICTOR NICOLÁS BRAVO

THE REFORM OF GOVERNMENTAL ACCOUNTING IN SPAIN: MAIN TENDENCIES

Over the last twenty years, a comprehensive process of reform and modernisation of the governmental accounting system has taken place in Spain. The main tendencies of this process are outlined below.

The legal bases required to initiate the reform of governmental accounting were established with the publication in 1977 of the General Budgetary Law. This law represented an important advance in the concept of governmental accounting since it not only recognised the usual objectives of control, but also the more current objectives regarding the provision of information for the various end users who may find it of interest.

Since then, the following objectives, with which governmental accounting must comply, have become increasingly prominent in the regulations brought into force in Spain:

- Management objectives: Governmental accounting must provide useful information to public managers for the support and improvement of decision-making.
- Control objectives: Providing support for the inspection and control activities to which public sector entities are subject continues to be an essential objective of governmental accounting. This must provide for the accountability of all types of accounts and enable all types of control to which the public entity is subject to be effected.
- Analysis and disclosure objectives: Governmental accounting must satisfy the demands for information, which are increasingly being made by other users who have an interest in the activities of public entities.

In addition, the beginning of the 1980s saw the initiation of an accounting regularisation process in the Spanish public sector that has continued up to the present. Prior to this, a tendency towards harmonisation in the field of company accounting had been started, which in turn encouraged the view that it was vital to continue and extend this trend within governmental accounting, and led to the approval of a General Governmental Chart of Accounts.

Amongst the most notable aspects of Spanish governmental accounting reform over recent years, the following can be highlighted:

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 167-176.

1. THE 1983's GENERAL GOVERNMENTAL CHART OF ACCOUNTS (GGCA)

Of the aspects of governmental accounting reform considered to be in need of urgent modification was firstly, accounting techniques. This led to the introduction of the double entry bookkeeping method, with the application of the General Governmental Chart of Accounts (GGCA).

As mentioned above, the GGCA was also aimed at securing the regularisation of accounting in public sector entities. The 1973 General Chart of Accounts for business corporations was taken as a model for the drafting of the GGCA, with the aim of achieving harmonisation with accounting in the private sector.

Due to the fact that the introduction of a Chart of Accounts into the public sector was considered a major innovation at that time, and given the difficulties its introduction would imply, the Order which approved the GGCA established an initial experimental period in which the GGCA would be brought in provisionally and exclusively in the General State Administration.

It was proposed that the introduction of the GGCA to other public sector entities would be extended at a later date, once the introduction had been duly consolidated in the General State Administration.

The effective introduction of the GGCA took place from 1986 onwards when a computerised system was brought in which enabled operations to be registered from an asset-based as well as a budgetary perspective. This is further explained in the following section.

The GGCA did not develop the areas of accounting principles or evaluation criteria in any great depth, since the initial aim in the area of governmental accounting was to effect the introduction of the double entry bookkeeping system. Thus, the study of governmental accounting principles, or the conceptual framework of governmental accounting, was postponed until the system of asset-based accounting had been duly established.

2. DESIGN, DEVELOPMENT AND INTRODUCTION OF THE CENTRAL GOVERNMENT ACCOUNTING SYSTEM (CGAS)

Throughout 1983, the necessary steps were taken for the design of this system, which was developed during 1984 and 1985, and it was finally introduced at the beginning of 1986.

The CGAS was designed as a set of perfectly integrated sub-systems or accounting areas, in such a way that economic- asset based accounting became one of the registers making up the system.

The most notable basic characteristics of the CGAS are as follows:

It aims to register all operations of an asset related, budgetary and financial nature which occur within the area of responsibilities of the Central Government.

- It is an integrated system in which the interrelationships between the registered data of each accounting area are regulated.
- It is based on the decentralisation of the functions of accounting management in the accounts offices of the Central Government.

- Operations can be registered in accordance with the double entry bookkeeping method through the application of the GGCA.
- It is computer based and automatic in such a way that operation data are registered only once, with effects being produced in all relevant accounting subsystems or areas.
- The introduction of the CGAS announced the end of the physical movement of documents on paper between accounts offices, replacing this system with computerised information transfer methods.

In 1996, a new version of the CGAS), with the same features as the CGAS and based on the same principles, was introduced. It brought improvements to the existing subsystems in the previous version together with new computerised subsystems. This CGAS new version is the accounting system currently used in General State Administration.

3. APPLICATION OF THE GENERAL GOVERNMENTAL CHART OF ACCOUNTS TO OTHER SPANISH PUBLIC SECTOR ENTITIES

As mentioned above, and in contrast to the experiences of other countries, in Spain governmental accounting reforms were initiated at central level and subsequently extended to other public sector areas.
a) Within the state public sector, once the GGCA had been introduced into the General State Administration, the scope of the reform was amplified to include other entities, which then introduced the GGCA. These entities were State Autonomous Organisations and the Social Security System.
b) At local public sector level, 1990 saw the approval of the Local Authority Accounting Regulations through Ministry of Finance regulations. These regulations were of two types, one simplified type for local entities with a population of less than 5,000 and another general type for the rest. For the first time, these regulations included an adaptation of the GGCA for Local Public Administrations. It began to be put into effect in 1992.
c) At the regional level, the regulation of governmental accounting matters comes under the responsibilities of the Regional Governments. Over the last decade, they thus gradually introduced the GGCA through their own regulating systems.

4. CREATION OF A CONCEPTUAL FRAMEWORK FOR GOVERNMENTAL ACCOUNTING

In 1989 a new course of action was initiated in the field of governmental accounting, prompted by the State Public Accounts Department. This consisted of studying the accounting principles, which should govern the register of operations and the presentation of accounting information in the entities subject to the GGCA.

In the Spanish governmental accounting reform process, the first aspects to be tackled were those which required the most urgent modernisation. These aspects consisted of the way operations were registered, with the incorporation of the double entry bookkeeping system and the GGCA, and the accounting procedures used, with manual methods being replaced by computerised systems. Once these aspects had been remodelled and the new procedures were running smoothly, it was essential to pursue the study of governmental accounting theory, which had been in need of development since the approval of the first GGCA.

As a result of the work of a group of experts in governmental accounting, set up in 1989, an initial document was formulated which stated the major principles that should lead accounting information to reflect a true picture of the assets and financial positions and of the financial-assets and budgetary results of the accounting entity. Amongst the accounting principles included in this document, the following are worth highlighting:

- Accrual basis.
- "Recording".
- Prudence.
- Consistency.
- Cost basis.
- Going-concern.
- "No offsetting".
- Materiality.
- Matching of revenues and expenses.

The Commission on Governmental accounting Principles and Standards was established in the Resolution of 28 December 1990 with the aim of continuing and extending the activity begun by the previous working party. This Commission was made up of professionals from the various Administrations (State, Autonomous and Local), from universities and other professional corporations and institutions from both the public and private sectors. The Commission was assigned the task of devising governmental accounting standards which, as a development of governmental accounting principles, would determine the accounting approach to specific aspects of governmental accounting. This task was carried out not so much through the promulgation and publication of judicial rules, but rather by the drafting of documents containing the generally accepted principles and rules governing public entities subject to the GGCA, and which were to prompt the accountancy standards that were subsequently approved by the bodies responsible.

The documents and accounting principles, which have so far been developed by the Commission on Governmental Accounting Principles and Standards, are as follows:

- Rights to be paid amounts due and revenues.
- Revenues and Expenses.
- Transfers and subsidies.
- Public debt.
- Non-financial fixed assets.
- Public economic-financial information.
- Earmarked revenues.

5. THE 1994's NEW GENERAL GOVERNMENTAL CHART OF ACCOUNTS (NGGCA)

As a consequence of the work carried out on formulating a conceptual framework for governmental accounting by the Commission on Governmental accounting Principles and Standards, it was now essential to represent all the accounting criteria defined within this conceptual framework in a new GGCA. The incorporation of the new theoretical elements into the new Chart affected not only the headings concerning accounting principles and evaluation criteria, but also the other areas of the old Chart, such as the accounts table, accounting definitions and records and the annual financial statements.

Furthermore, in order to adapt the Spanish mercantile regulations to the European Union Accounting Directives, following Spain's incorporation into the European Community, a new General Chart of Accounts for Spanish business corporations was approved in 1990. Bearing in mind that the reform of Spanish governmental accounting sought to normalise accounting systems not only in the area of public sector accounting, but also in that of the private sector, it was considered necessary to include the changes introduced with the 1990 Chart of Accounts for business enterprises in the NGGCA.

Of all the accounting principles covered by the NGGCA, perhaps the accrual basis principle is most worthy of further attention. This principle establishes the criterion of temporal allocation of revenue and expense in the moment when real flow of goods and services represented by this revenue and expense occurs, with the express exclusion of the cash receipts basis of accounting.

Amongst the currents in the evolution of governmental accounting, the present line of thought is that annual financial statements covered by the NGGCA should provide information according to national accounting criteria (ESA'95), since these criteria are used in international comparisons of Public Administration financial data.

6. NEW REGULATION OF THE GENERAL STATE ACCOUNT.

Under Law 50/1998, Heading VI on governmental accounting, of the Amended Text of the General Budgetary Law was redrafted. Amongst other matters, the General State Account was modified. On the one hand, the subjective sphere of the General State Account was extended to include all entities which make up the state public sector (under previous regulations, only certain of these entities were included). On the other hand, a reference was included for the first time stating that General State Account information must be obtained by means of account consolidation techniques, although it can temporarily be effected through the aggregation of accounts.

According to the 1998 normative modification, the General State Account comprises the following documents:

- General Account of State Public Administrations, formed by the aggregation or consolidation of the accounts of the entities which produce their accounts in accordance with the accounting principles and standards covered by the GPAP.
- General Account of state-owned business corporations, formed by the aggregation or consolidation of the accounts of the entities which produce their accounts in accordance with the accounting principles and standards covered by the General Chart of Accounts for Spanish business corporations.
- General Account of state foundations, formed by the aggregation or consolidation of the accounts of the entities which produce their accounts in accordance with the accounting principles and standards covered by the General Chart of Accounts adapted for non-profit making entities.

It also establishes that the content, structure, the drafting standards and the criteria for aggregation or consolidation of the General State Account will be determined by the Ministry of Finance, and must provide information on the following:

- The economic, financial and asset position of the state public sector.
- Financial year financial-asset balance.
- The execution and liquidation of the budgets.

The Ministry of Finance employed the provisions of this Law to approve an Order on 12 December 2000, in which the drafting of the General State Account was regulated.

If the final objective sought through the General State Account is to offer consolidated information on the activities developed in the state public sector as a whole, certain arguments point to the advisability of this consolidation process being carried out gradually.

Firstly, account consolidation in the Spanish public sector sphere is an innovative issue. Although there is a tendency towards normalisation in the field of accounting, it is not possible to extrapolate private sector consolidation standards to the public sector, due to both the peculiarities of state public sector entities and the variety of relationships of dependency which exist between them.

The second argument for the gradual execution of this process is that two accounting systems coexist in the state public sector, one public and the other private. Whether public sector entities are subject to one system or another depends on the activities they carry out, which therefore makes the presentation of consolidated statements difficult.

As a consequence of this, the above-mentioned Ministry of Finance Order opted to begin the consolidation process with the General Account of State Public Administrations, while postponing the consolidation of the General Account of State Business corporations and State Foundations.

7. PROJECTS DESIGNED TO FOSTER THE USE OF INFORMATION TECHNOLOGY IN GOVERNMENTAL ACCOUNTING PROCEDURES:

7.1. Centralisation of the General State Administration Accounting Information System Local Databases in the State Public Accounts Department.

From the outset, this system was designed as a totally decentralised structure with independent databases in each of the General State Administration accounts offices (one in each Ministry, one in the Directorate-General for the Treasury and one in each local Tax Office). The previous system meant that daily information transfer processes had to be made from the accounts offices to the Central Accounts Office in order for centralised and aggregated information on the General State Administration as a whole to be available.

The centralisation of the System's databases led to an improved availability of information with these transfers now being made in real time. This also brought about a significant reduction in the costs of maintaining the system itself.

The centralisation of the local databases was brought in during the year 2000.

7.2. Computerised preparation and rendering of annual accounts.

The preparation and rendering of the annual accounts by Public Organisations had always been carried out by employing the traditional methods of sending statements, reports and documents, all on paper, which make up the accounts to be rendered to the Court of Auditors.

Now that technological developments have make the use of electronic information exchange systems commonplace in even household economies, it seemed inappropriate for Public Organisations to still be using traditional procedures for the rendering of accounts by sending vast amounts of information on paper. This is all the more pertinent when the accounting information systems employed allow other procedures to be used with total reliability, which are more in line with the technology supporting these systems.

Thus, on 28 June, 2000 using the authorisation provided for in the General Budgetary Law, the Ministry of Finance introduced a new procedure for Public Organisations subject to the GPAP, to computerise the obtaining and rendering of accounts.

In accordance with this norm, the first annual accounts prepared and rendered to the Court of Auditors under the new procedure were those corresponding to the financial year 2000.

Activities designed to bring about the diffusion of accounting information. One of the most important aims of governmental accounting reform, this measure attempted to ensure that accounting information was brought to its end-users, the general public.

In an attempt to achieve this objective, in the year 2000, the Ministry of Finance ruled that Public Organisations subject to the GPAP must publish the information contained in the Summary of their respective annual accounts in the Official Gazette of the Spanish State within a period of one month after their approval, so that all potential users of this accounting information might have access to data on the activities carried out by these Public Organisations.

The Summary of the annual accounts, of which it forms a part, is comprised of the following statements:

- Balance sheet

- Account of financial-assets results
- Budget liquidation Statement
- Budget liquidation of Expenses by Programme
- Budget liquidation of Expenses by Chapters
- Budget liquidation of Revenue by Chapters
- Trading operations performance
- Budgetary performance
- Report on the organisation

The Order of the Ministry of Finance dated 28 June 2000, made compulsory the publication of Summary of the Annual Accounts of Public Organisations subject to the General Governmental Chart of Accounts. The first Summary to be published was that corresponding to the Accounts of financial year 2000.

8. ACTIVITIES DESIGNED TO BRING ABOUT THE DIFFUSION OF ACCOUNTING INFORMATION

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    - Budgetary performance
- Report on the organisation

The Order of the Ministry of Finance dated 28 June 2000, made compulsory the publication of Summary of the Annual Accounts of Public Organisations subject to the General Chart for Governmental accounting. The first Summary to be published was that corresponding to the Accounts of financial year 2000.

9. INTRODUCTION OF COST ACCOUNTING IN PUBLIC ADMINISTRATIONS

Within the scope of the Ministry of Finance, the State Public Accounts Department has drawn up a theoretical model of cost accounting regulated for Public Administrations. The aim of this model is to introduce cost accounting systems into those Administrations which, together with other information systems, will make their management easier by revealing how efficiently this management is carried out and providing public managers with the information necessary to take decisions.

The introduction of cost accounting systems in Public Administration sets out to achieve the following objectives:

- Facilitate the preparation and evaluation of budgets.
- Determine the value of charges and prices to the public.
- Clarify the use of public resources thereby making management control possible.
- Provide support for the adoption of decisions on the production of goods or the provision of services.
- Supplement the information provided by traditional financial statements obtained from asset accounting.

The most important characteristics of the regulated accounting model are as follows:

- An effort was made to keep the model as simple as possible.
- The traditional double entry bookkeeping system was dropped
- Actual or historical costs are allocated
- A complete costs technique is included
- It is a radical dual model, since it can operate autonomously from financial accounting.

With the regulated cost accounting model developed and installed in the Public Organisations which applied for it, the current position of the Project to introduce cost accounting is as follows: in the year 2000 the computerised support for the system was developed, and during 2001, it is going to be tested out and introduced in some of the Organisations making up the Project.

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EVELYNE LANDE

THE ACCOUNTING REFORM OF CENTRAL GOVERNMENT IN FRANCE

1. CRITICISMS OF THE PRESENT SYSTEM

The present accounting and budget information system of the French Government has been much criticised over the last few years due to its lack of transparency and fairness, which does not allow for genuine parliamentary supervision and does not ensure effective budget management.

1.1. Lack of transparency and fairness of the accounts

1.1.1. The origin of the debate: the tax "cagnotte" ('windfall') of 1999

During the summer of 1999, there was a major political debate regarding the use of a "tax windfall" corresponding to a surplus of tax revenues due to an improvement in the French economy[1]. In order to prevent this surplus from resulting in an increase in spending in response to sector-based pressures or the requests of the ministers themselves, the Ministry of Finance and the Economy made use of certain accounting adjustments to limit the size of these surplus revenues. Thus, the final report of the French Audit Court (*Cour des Comptes)* regarding the implementation of the Finance Bill for 1999 highlights the willingness to downplay the economic substance in order to smooth accounting income for the 1999 and 2000 financial years by the use of the following two mechanisms:

1. the addition of expenditure for the 2000 financial year to the 1999 financial year decided during the supplementary period (the period between 31 December 1999 and 28 January 2000) for an amount of EUR 1.68 billion (anticipation of expenditure disbursed in January 2000 relating to the storm in France at the end of 1999),
1. the adjustment in the level of spending of the Treasury's special accounts by EUR 1.53 billion, this item being in fact the traditional adjustment variable for the budget year,
2. revenues carried forward:
- Non-tax revenues for an amount of EUR 2.73 billion. The French Audit Court states that "the revenues carried forward, in some cases decided on at the very end of the supplementary period and at Ministries' request, reached significant levels last year". Thus, the French Audit Court considers that the adjustments carried out with some of the Treasury's main contacts, such as the French

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 177-190.

Consignments and Loans Fund, highlight "the ambiguity of financial relations that the Government has with such bodies",
- VAT revenues for an amount of EUR 910 million and corporate income tax revenues for EUR 240 million.

Table 1 - The actual budgetary deficit situation of the French Government in 1999

In billions	*FRF*	*EUR*
Finance Bill budget deficit	(236.60)	(36.07)
Surplus tax revenues	30.70	4.68
Published Finance Bill implementation deficit	(205.90)	(31.39)
Revenues carried forward		
- non - tax revenues	18.00	2.74
- VAT revenues	6.00	0.91
- Corporate Income Tax revenues	1.60	0.24
Anticipation of expenses		
- Allocation to bad weather fund	11.00	1.68
- Spending adjustment in the Treasury's special accounts	10.00	1.52
Restated implementation deficit	(159.30)	(24.29)

The French Audit Court concluded its analysis by suggesting that the Ministry of Finance and the Economy speed up the process of reform which should make it possible to move from cash accounting to commitment accounting between now and 2003, thus putting a stop to these practices of carrying forward revenues and anticipating expenditure according to the date of receipt or payment.

1.1.2. The economic and political stakes of accounting adjustments

This practice of smoothing out financial results and, in particular, surplus revenues is not new and can frequently be explained by very important political or economic factors.

Thus, the French Audit Court noted that the health insurance accounts, covering expenditure generally linked to spending on health by the French Social Security, have shown much less of a deficit since the changeover to commitment accounting (EUR 1.5 billion reduction in the deficit). However, the presence of a significant deficit in the health insurance accounts has suited French Governments. In fact, in the past, the Governments had committed themselves to a policy of controlling public health spending, requesting, in particular, that the Department of Health actively participate in such control by implementing financial measures to penalise excess spending. However, such penalties and actions are only appropriate if there is a deficit to be reduced since it is the variable, which is the easiest to propose politically. However, explaining the cost of public health spending as being a cost for the general public, which may harm the performance of the French economy due to the pressure it puts on employees and companies, is harder to accept politically. Thus, the recording of account deficits is a simple and effective way for a Minister to implement a tight budgetary control policy.

The case of the 'tax windfall' in 1999 and the smoothing of income in the accounts over 1999 and 2000 as shown above follow the same logic. In fact, France has undertaken to comply with the Maastricht criteria and, in particular, the limitation of government debt to 0.3% of GDP. For this purpose, the French government presented a multiannual public finance programme to the European Commission, based on an intangible level of public expenditure. This programme is based on a limited change in the volume of expenditure, i.e., not including inflation, so that France may eventually comply with the criterion for public debt of less than 0.3% of GDP.

Table 2 - The Government's commitment to reducing the public deficit in France

2000	2001	2002	2003
1.5%	1.2%	0.7%	0.3%

Source: French Government's multiannual public finance programme

If the Ministry of Finance and the Economy records a revenue surplus, the other Ministries will be likely to ask for a share of this tax windfall so that they may increase their spending, which, from a logical standpoint, is impossible due to the government's multiannual commitment. The government is thus faced with the following dilemma:

1. carrying forward a part of the surplus in revenues to limit pressure by Ministries and thus be able to meet commitments to reduce the debt burden,
2. or recording the existence of the revenue surplus to bring forward the programme to reduce the French Government's debt, although in this case it will find it very hard to maintain the level of expenditure (budget appropriations) by the various ministries which will have to meet the demands of civil servants (revaluation of salaries, hiring more staff) or the users of public services who will want more services, or taxpayers who will seek a reduction in their contribution. In this situation, the surplus economic revenues will be transformed into a structural expense and will not permit a reduction in the debt burden.

In spite of all this, the impact of the tax 'windfall' in 1999 obliged the French government in June 2000 to grant additional budget allocations to ministries for the *lettres de cadrage* [letters setting out the main points of the budget] for 2001. For this purpose, it had to use an accounting 'trick' to comply with multiannual commitments for the development of expenditure, by changing the inflation assumptions: instead of the 0.9% initially forecast, the assumption for price increases was fixed at 1.1% so as to justify a nominal increase in ministerial credits higher than the level fixed at the outset, while ostensibly making it possible to comply with the standard for increase in volume.

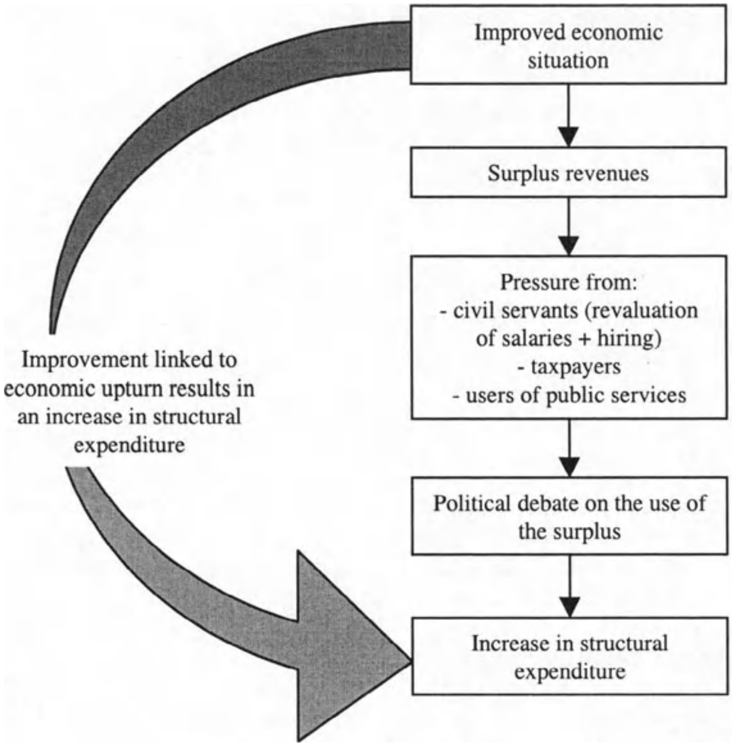

Figure 1. The consequences of clear recording of surplus revenues

2.1. Parliamentary control which does not enable the effectiveness of budgetary management to be evaluated

The various budgetary adjustments set out above do not favour parliamentary control under suitable conditions. Three other factors should also be taken into account:

1. time required for presenting information on the implementation of the budget,
2. the principles governing the budget and the Government's public accounts,
3. the terms and conditions for the adoption of the budget and the evaluation of its implementation.

The first factor recalls the efforts made over the last few years to improve the information provided to Members of the French Parliament; the two other factors show the efforts to be made over the years to come.

1.2.1. Time required for publishing the financial statements

In less than ten years, the time required by the French Government to publish the financial statements and have them validated by the French Audit Court has been reduced by more than six months, as shown by the two timetables set out below:

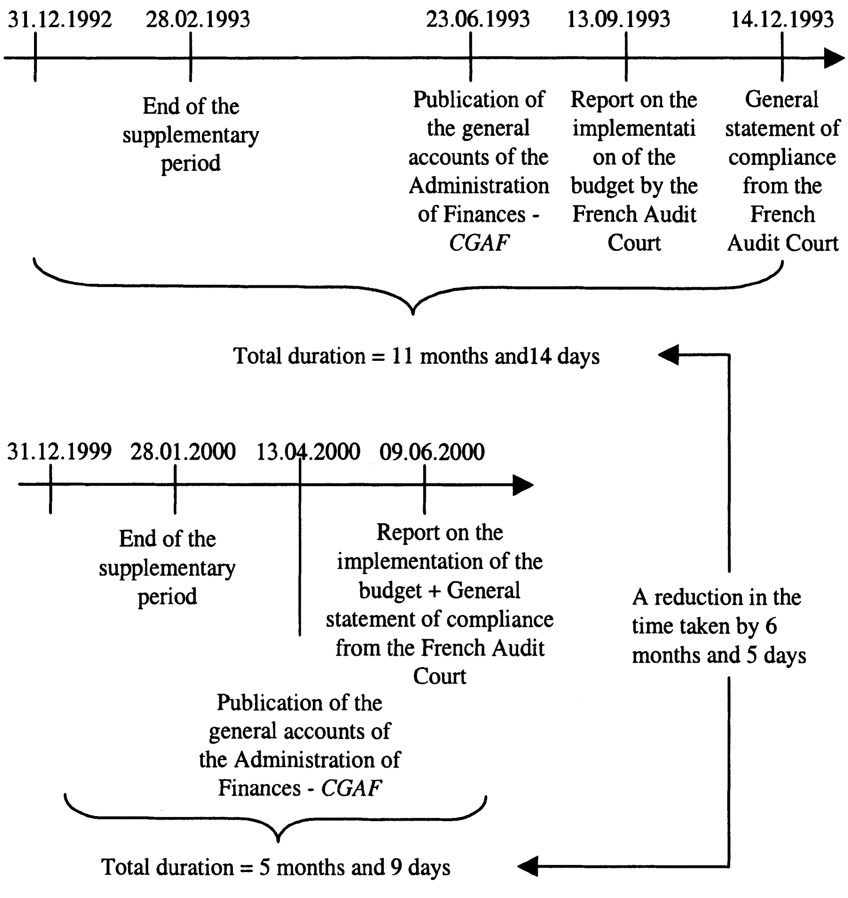

Figure 2 .The reduction of time required for publishing the Government's financial statements

Source: *ZUBER (2001)*

This reduction in the time taken by more than 6 months thus makes it possible for the first time to approve the financial statements for the 1999 financial year before the *lettres de cadrage* for expenditure for the financial year 2001 are drawn up, which took place in mid-July 2000. This factor enables Members of the French

Parliament to be better informed and can only improve the procedure for the adoption of the budget.

1.2.2. The standards for drawing up the budget and the budgetary implementation statement

Nonetheless, speed of approval is not the only factor to be taken into account. Proper control presupposes information being obtained within a reasonable time period, in addition to content which enables Members of the French Parliament to pass judgement on the implementation of the budget.

France elected to:

1. Vote on the cash budget: only the receipts and disbursements recorded during the financial year are included in the budget submitted to Members of the French Parliament, without reference to the commitments undertaken during a financial year which do not immediately create a disbursement.

For example, to tackle youth unemployment, the French Ministry of Employment and Social Affairs established five-year public contracts for young people. At the end of this period, if these young people have not found employment, the Government will have to pay their unemployment benefit since these contracts do not provide for contributions to unemployment insurance funds. Thus, each time a young person enters into a contract, the Government knows that it will probably have to bear an extra cost at the end of five years, but this extra cost is not taken into account in the budget by means of provisions. Another example is that depreciation and amortisation are not taken into account in the budget.

The CGAF (general accounts of the administration of finances) for financial year 1999 indicate that "it did not appear appropriate to transform Parliamentary authorisation into approval of interim financial statements, based on accounting policies which may change depending on justifications or arguments which are difficult to control. Parliament should keep a robust and indisputable indicator which enables it to ensure that its instructions are properly carried out by the administrative bodies."

It thus appears that cash accounting would be a more "robust and indisputable" indicator than commitment accounting. However, the various budgetary adjustments identified above following the 'tax windfall' of 1999 show that, on the contrary, adopting a budget which only incorporates receipts and disbursements makes it possible to adjust the financial results by carrying forward receipts and disbursements by a few days.

2. Present the accounts by means of financial statements (balance sheet, profit and loss account and notes to the financial statements) on the basis of commitment accounting principles: the French Government needed to make this change in order to limit the adjustments of accounting data to draw up the country's financial statements (LANDE, 2000) published by the INSEE (French National Institute of Statistics and Economic Surveys) (financial statements including data from companies, institutional investors, households and public administrations) and adopting commitment accounting in accordance with the European SEC 95 regulation.

Thus, the CGAF of 1999 was the opportunity to introduce 4 major innovations in terms of the recording of assets, liabilities and commitments (ZUBER, 2001):
- presentation of debt on a full accrual basis,
- setting aside provisions for the main tax credits in the assets,
- restructuring and improvement of accounting information relating to State assets which led to a valuation of assets and the taking into account of depreciation and amortisation (LANDE & SCHEID, 2000),
- publication in the presentation report of actual notes to the balance sheet providing information on off-balance sheet commitments.

The financial accounting of the Government must still be improved to enable it to be classified as full commitment accounting according to the IFAC (International Federation of Accountants) benchmark, although the public authorities are keen to publish financial statements which come as close as possible to this benchmark.

This duality between the budget drawn up according to a cash system and the implementation account drawn up in accordance with commitment accounting principles do not facilitate the control of commitments at the time of the vote on the budget, or the control of operations carried out at the time of the approval of the execution account.

However, this duality should be considered as a phase of transition: the Ministry of Finance and the Economy had planned to adopt a commitment accounting system both for the budget and the public accounts. However, confronted with the difficulties of implementation due to the large number of budgetary operations in question, and the institutional difficulties, the Ministry preferred to opt for a reform limited only to public accounts, rather than opting for an ambitious reform whose complexity was likely to "obstruct any immediate change." (DGCP, 2000).

The pretext, used to maintain a cash accounting system for the budget ("a robust and indisputable indicator"), will certainly be called into question, as soon as the difficulties are overcome and there is a strong political will to align the budgetary system principles with those of public service accounting.

1.2.3. The methods for the adoption of the budget

The vote on the budget is currently made by chapter and by article, i.e., at a very specific level of detail which does not enable Members of the French Parliament to view the appropriations committed to large programmes or major political activities. This also leads to a limitation of the room for manoeuvre of managers, who are bound by strict compliance with the budget passed, even if it appears during implementation that it would be better to modify the allocation of resources (changes in budgetary appropriations) to better meet public requirements.

Furthermore, the budget is subject to the principle of annuality: it only records the receipts and disbursements relating to one financial year. Thus, this principle does not make it possible to monitor the programmes multiannually, which might provide a basis for agreements relating to targets, entered into by civil servants.

Under such conditions, the vote on the budget does not enable:

1. Members of the French Parliament to have an overall view of the programmes or activities undertaken (lack of multiannual overview), or the corresponding

commitments (the budget only includes receipts and disbursements), or the efficiency of public action,
2. Managers to have room for manoeuvre, allowing them to arbitrate in the allocation of resources to improve the effectiveness of the budget, since they are not evaluated according to the targets achieved but according to the legality of the expenditure (whether or not the expenditure complies with the budget passed).

2. THE MAIN CURRENT LINES OF REFORM

In order to try to correct previous faults and respond to criticisms, the French government has chosen two main lines of reform:
1. the first involves reform of the accounting system through the implementation of commitment accounting and the inventory of assets and liabilities,
2. the second is more specifically orientated towards the restructuring of the budgetary framework.

The first accounting reform must be considered as a significant advance for identifying the Government's financial situation. Nevertheless, it has had little impact on management methods, since traditionally in France the budgetary system has always prevailed over the accounting system. Consequently, only a reform of the budgetary framework could have an impact at the level of public management.

2.1. Government accounting reform

In 1997, the Ministry of Finance and the Economy carried out a study with the aim of defining concrete proposals for the implementation of an accounting system for the Government's assets. Thus the CGAF of 1999 integrates these various proposals with a view to gaining a clearer picture of the Government's financial situation, using the Government's balance sheet and the profit and loss account.

However, improving appraisal is not the only objective of this reform which aims to publish financial statements which are more in compliance with international standards and to communicate on aggregates such as those defined by the Maastricht Treaty, which enable the benchmarking of the French Government's management in line with that of other OECD countries.

2.1.1. Improved measurement

Improved appraisal has been achieved through the implementation of commitment accounting (recording of expenses and income and not only receipts and disbursements) which has been supported, in concrete terms, by:
- an inventory of liabilities (full accrual recognition)
- the depreciation/amortisation of tax credits
- the inventory and valuation of some of the assets, taking into account depreciation/amortisation in the financial statements

- the evaluation of the Government's financial investments in companies, using valuation methods from the private sector (valuation according to the share of net equity)
- the publication of notes to the financial statements providing off-balance sheet information.

In this respect, the comparison of the financial statements for 1998 and 1999 shows significant changes.

Table 3. The balance sheet of the French Government (a)

ASSETS	31/12/99	31/12/98	LIABILITIES	31/12/99	31/12/98
Fixed assets	*1 199.8*	*731.8*	*Net financial situation*	*(3 082.1)*	*(2 956.2)*
net fixed assets	504.1	13.3	*Financial debt*	*4 061.8*	*3 801.3*
amortisation expenses and investments	561.7	581.4	negotiable	3 932.8	3 789.3
loans and advances	128.4	131.2	non-negotiable	119.4	
miscellaneous fixed assets	5.6	5.9	overdraft with the BF(b)	9.6	12.0
Current assets	*371.4*	*663.1*	*Miscellaneous liabilities*	*589.0*	*528.5*
taxpayers	115.0	353.4	Transactions through SSB(c)	10.3	439.2
Cash and marketable securities	49.6	126.7	Deposits	458.7	
other receivables	206.8	183.0	other payables	119.9	89.3
Miscellaneous assets	*85.7*	*67.9*	*Miscellaneous liabilities*	*88.2*	*89.2*
TOTAL	1 656.9	1 462.8	TOTAL	1 656.9	1 462.8

(a) Source: ZUBER (2001)
(b) Bank of France
(c) Supplementary State budgets

2.2.2. Introduction of new tools and a new reporting system

The purpose of improving the content and accuracy of appraisal is to attain better knowledge of the Government's financial situation. This also assumes that the public accounts serve as a point of reference and a communication tool. However, in France, communication to institutions or Members of the French Parliament has always been directed towards the budget and its implementation, as the public accounts constitute an item of information reserved for experts and not for the general public. It is therefore surprising to note that there are budgetary principles, which provide a framework for, and govern, budgetary data, whereas until the beginning of the 1990's there were no rules at all for financial accounting.

However, with the establishment of the European Central Bank, Eurostat[2] and the adoption of the Maastricht criteria, France is obliged to provide information on the basis of European aggregates which require all European countries to produce financial statements drawn up in accordance with the same generally accepted accounting principles.

Using accounting information as a communication tool is a Governmental requirement, which implies the implementation of a proper reporting system, making it possible to monitor the Maastricht aggregates. This implies the capacity to reconcile all the information relating to public administrations: the Government, national institutions, Social Security accounts, local and regional authorities, etc. At the moment this consolidation is carried out by the INSEE, which is faced, in particular, with major problems due to:

- the use of different accounting principles. In this respect, the Government reform aims to standardise accounting systems with the eventual objective of converting public administrations to commitment accounting,
- the multiplicity of sources of accounting information: in the past, for the Government alone, each Ministry possessed its own system of recording accounting entries, as was the case for supplementary budgets. To solve this problem, the French Government developed a piece of integrated software (ERP - *Enterprise Resource Planning*) known as ACCORD. The French Interior Ministry has used this software on a trial basis since 1 January 2001 and its use will be extended to all Ministries in 2002-2003. It will eventually make it possible to have only one system for recording accounting information to facilitate the consolidation of data.

2.1.3. Conclusion

The reform of the French Government's accounting system is underway. New improvements are expected, in particular:

- at the level of financial reporting: development of consolidated financial statements and reporting on the basis of key aggregates,
- monitoring of State assets: use of accounting information in order to manage assets on a more active basis.

2.2. The reform of the budgetary system: the Migaud bill

The French budgetary system is governed by the French Order of 2 January 1959[3]. This legislation governs the conditions for the drawing up, adoption and monitoring of the budget. The bill submitted by deputy Migaud on 12 July 2000[4] aims to strengthen Parliamentary control and ensure more effective management. It is thus an extremely important reform due to the impact it will have on Members of the French Parliament, managers and control bodies.

2.2.1. A reform of the powers of Members of the French Parliament

The vote on the budget by Members of the French Parliament is governed by two principles:

1. the principle of annuality: the budget should only include disbursements and receipts in respect of the calendar year,

2. the principle of the specific nature of the budget which consists in only authorising the allocation of funds to a particular department for a specific purpose. There are therefore around 1000 chapters, which are then divided into articles and paragraphs. This classification by type does not give a coherent overview of all the appropriations to an activity. In addition, the vote on the budget by chapter and by article does not enable managers to alter the allocation of resources to meet changing needs.

The bill aims to radically alter these two basic principles via the introduction of a series of reforms:

1. The development of multiannual authorisations,
2. The development of Ministerial programmes offering a clearer picture of the use of appropriations along clearly established political lines. This involves, in particular, the budget being presented in two sections: one section for operating expenses and another for investment expenses. However, there are no plans to present these sections side by side as is the case for local and regional authorities,
3. The introduction of fungible appropriations (save for those relating to payroll costs) within these ministerial programmes: managers will be able to alter the appropriations passed, according to requirements as they arise during the financial year, as the objective is not to conform with the use of appropriations but to meet public requirements.

The purpose of this reform is for "the government and its administration to set targets for public action, linked to results indicators, with respect to the Parliament and the public. The management of these budgets will be highly flexible, seeing as, apart from payroll costs, appropriations will be fully fungible so that managers can allocate available public resources more efficiently under the Parliament's control." (French National Assembly, 2000a).

Thus, the role of Members of the French Parliament is based on the political objectives of the programmes and not on material contingencies which then become managers' responsibility. There is thus a transfer of responsibility from Members of the French Parliament to managers.

2.2.2. A reform of the terms and conditions for action by managers

It is not sufficient to grant more freedom to managers, this freedom also has to bring with it more responsibility and managers must therefore account for the use of appropriations allocated to meet objectives defined in the political programmes voted on:

> «Management flexibility (...) offered to the executive should not result in Parliament's control being weakened. In return (...) the manager must be made accountable for its management with respect to the budgetary authority, namely the Parliament." (French National Assembly, 2000a).

This implies:

1. A reform of management methods in line with the co-ordination of activities and the appraisal of performances. As an example, the French Interior Ministry,

which is the Ministry responsible for co-ordinating the implementation of the ACCORD project, has decided to set up a unit responsible for management control made up of around 20 people, even though this Ministry has more than 30,000 employees, the task of this unit being the organisation of Prefectures' reporting systems and training activities, and the raising of awareness with respect to management control. This unit has called on the services of private consulting firms in order to identify the objectives of political programmes and to decide on the appropriate action to be taken, to develop IT tools for the upward flow of management information (reporting) and to conduct training seminars.

2. A radical reform of human resources management. The promotional and wage structure of civil servants is currently managed by competitions and by seniority of administrative grade. There is also very often a discrepancy between the grade, skills and the position held. However, the introduction of public service performance appraisal based on the meeting of targets assumes that civil servants are hired on the basis of their suitability for a position (which implies defining profiles for positions which is not yet the case) and not according to their grade.

Lastly, above and beyond reforms, Ministries must bring about a revolution in the culture of central government, which will be aided by the retirement of 45% of civil servants over the next 12 years.

2.2.3. *A reform of methods of control/evaluation*

The bill (Article 35 - 5) is highly ambitious with respect to the role of the French Audit Court which should certify the regularity, fairness and faithful representation of the published financial statements: "in exchange for the flexibility offered to the government for the implementation of the budget, control would subsequently be reinforced, as the submission of the bill must be accompanied by the presentation of performance reports, the justification of the use of appropriations (....); the scope of intervention of the French Audit Court with a view to the drafting of the bill would also be strengthened, as the statement of compliance alone must eventually become a proper certification." (French National Assembly, 2000a).

The bill provides that the French Audit Court will have 3 years as from the passing of legislation to undertake such reforms as will permit such Court to pass judgement on the accounts (certification) and on the operations carried out (evaluation of public policies).

2.2.4. *Summary*

The alteration of the budget framework will thus have an impact both on the content of the budget and management tools, but will above all alter the role and the balance of power between the entities concerned, with two aims: increasing the clarity and fairness of the accounts and ensuring effective and efficient budget management.

Table 4- Summary of the consequences of budgetary system reform

	Drafting of and vote on the budget	*Implementation of the budget by Government and Ministries*	*Control of the implementation of the budget*
Current system	Vote on annual appropriations (annuality principle) by chapter and by article (principle of specification)	Use of budgetary appropriations by chapter and by article	Control of the legality of expenditure (level of spending and allocation)
Planned system	Vote on the budget by programme or by political activity in accordance with the targets to be reached	Implementation of management tools (management chart) Fungibility of appropriations (more room for manoeuvre in the budget)	Evaluation of programmes by the Parliament: - effectiveness: reaching targets set - efficiency: cost of services - relevance: relating objectives to requirements Certification of the implementation of the budget by the French Audit Court

Table 5- Change in the role and the powers of the entities concerned

Parliament	*Government + Ministries*	*French Audit Court*
Task of defining the "political strategy" in the form of a programme Role as inspector in the evaluation of the public policy carried out by the government	More freedom of management accompanied by more responsibility on the targets to be reached Submission of a management report	French Audit Court's role as inspector of the fairness of the financial statements (faithful representation)

3. CONCLUSION: THE OBSTACLES AND OPPORTUNITIES

In France, reforms are traditionally undertaken with the aid of tools or techniques and then passed on through training activities, which enable public organisations to adapt to the new tools. Political will is a key to the success of a reform, but it appears to be disguised by tools, or it attempts to gain legitimacy in administrative departments through management tools or information systems.

For this to take place, above and beyond a reform of the information system (ACCORD software) or of the law, there must be a change in attitudes and organisation: the retirement of 45% of civil servants over the next 12 years is an opportunity which should not be missed.

NOTES

[1] A similar debate took place for financial year 2000, as the Ministry of Finance and the Economy recorded a surplus in revenues of EUR 4.6 billion in July 2000, to which should be added the EUR 7.6 billion earmarked for a reduction in taxes within the scope of the supplementary estimates, i.e., a total 'tax windfall' of EUR 12.2 billion for the 2000 financial year.

[2] Body responsible for drawing up European statistics and monitoring the European aggregates laid downin the Maastricht Treaty.

[3] This Ordinance has the same value as a Law under French Law

[4] The French National Assembly examined this bill on a first reading on 8th February 2001.

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J.R. CHRISTIAENS
C. VANHEE

INNOVATIONS IN GOVERNMENTAL ACCOUNTING SYSTEMS

The Concept of a "Mega General Ledger" in Belgian Provinces

1. INTRODUCTION

In the last years a number Belgian public sector organisations have been reformed from cameralistic/cash accounting towards business-like accrual accounting. Recently, the Belgian legislator prepared the accounting reform of provincial governments (1999, 2000) starting as of 1st January 2002. Generally, the provincial accounting reform implies a maintaining of the traditional cameralistic accounting system together with the introduction of accrual accounting in order to obtain a patrimonial view of each province. Although provinces are more extensive than local governments, they have mostly a centralised accounting system.

Governmental accounting reform studies show a lot of conflicts and debates when governments are being reformed towards accrual accounting in light of New Public Management intentions. Implementing a system of business-like accounting often creates resistance and a number of technical, managerial and political problems in respect of the traditional cameralistic accounting system. Particularly the technical problems of combining and integrating accrual accounting in governments is hypothesized to be one of the explaining factors regarding the adoption problems.

This paper aims at focusing on the technical questions and problems with respect to the combination of *new* accrual accounting in the context of the *old* cameralistic accounting. Those problems are examined looking at the development of a governmental accounting innovation: the "Mega General Ledger". This innovation reveals a possible technical solution of keeping the strengths of the former cameralistic systems and gaining the accrual accounting advantages. Therefore, an integrated approach for the traditional cameralistic system with the new accrual system together with a new analytical system is elaborated. Apart from an examination of previous research, this innovation is based on preceding fieldwork in preparing detailed decrees regarding the drawing up of the first balance sheet and evaluation rules for provinces, which was a research project last year on behalf of the Ministry of Internal Affairs in Belgium.

The study is not considering the reasons for the reform, nor the usefulness of adopting accrual accounting in governments. The concept of integrating the different

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 191-202.

accounting systems in a "Mega General Ledger" is studied only from a technical point of view.

2. REVIEW FORMER APPRAISING AND CRITICAL STUDIES

Table 1 provides an overview of a number of studies classified from different angles and discussed hereafter.

Table 1. Overview appraising, critical studies accounting reforms

CAMERALISTIC CASH ACCOUNTING	ACCRUAL ACCOUNTING
Conceptual studies favouring Cameralistic / cash accounting	*Conceptual studies favouring accrual accounting*
- Montesinos, Pina & Vela 1995 - Caperchione 1995 - Monsen & Näsi 1997, 1998, 2000	- Likierman 1994 - Jones 1995 - Anthony 1989
CONCEPTUAL STUDIES COMBINING CASH AND ACCRUAL ACCOUNTING	
- Caperchione 1995 - Jaruga & Nowak 1995 - Jones & Lüder 1996 - Christiaens 2000	
ACCOUNTING PRACTICE STUDIES CONCERNING TECHNICAL IMPLEMENTATION OF COMBINED REFORMS	
- Jones & Lüder 1996 - Caperchione 1995 - Montesinos & Vela 1996 - Cotte, Milot & Nante 1995 - Christiaens 2000 - Caperchione 2000	

2.1. Conceptual Studies Favouring Accrual Accounting

Some studies or parts of studies belief in the need for business-like accrual accounting mainly starting from a dissatisfaction regarding the cameralistic/cash accounting. Also shortcomings in the functioning of cash accounting in practice (Jaruga & Nowak 1995 p. 95; Christiaens 2000) are an important reason for the need to reform.

All those favouring studies could be seen as being part of the "protagonists" and they focus on the advantages of accrual accounting and on the related management tools. For example, Jones (1995, p.40-42) agrees with the lasting necessity of being able to obtain budget balances by means of cameralistic accounting, but he criticizes the exclusion of assets and liabilities. Others view governments as close to enterprises if seen from a financial economic point of view and argue that there should be one world of accounting in which enterprises and governments should prepare similar financial statements (Anthony 1989; Mellemvik & Monsen 1995). However, this idea of uniqueness needs not to be shared by everyone.

2.2. Conceptual studies favouring cameralistic accounting

On the other hand some studies are not convinced of the necessary adequacy and presupposed uniqueness of one business-like accounting system and they evidence the advantages of the traditional cameralistic system. They could be called the "antagonists" who stress the particular governmental features such as the absence of stockholders, the overestimated focus on profitability and the need for a system of financial controls in a democratic government. Montesinos, Pina & Vela (1995) motivate the cameralistic accounting system by referring to the role of the legal control, which is the monitoring of the budget execution process and accountability. Caperchione (1995, p. 68) posits that accrual accounting is a step forward, but undergoing an accrual accounting reform does not imply automatically the supply of managerial tools applicable for governments.

Monsen & Näsi (2000, p. 2) are somewhat disappointed that seemingly the experiences of local government accounting are not enough taken into account when adopting a reform. In their study they quote an older source (Johns 1951): "In the public sector it is only possible to prepare a *financial income statement*, in the private sector a *performance income statement*". This tells a lot of the intrinsic differences of governments with respect to enterprises. Finally, they mention the difficulty of summarising the result of government's activities by a single accrual accounting figure. Therefore, they argue that the cameralistic point of view managing the tax money remains an important objective. The current study will show that the two groups of accounting methods need not to be polarised and that a concept of combining them harmoniously can be elaborated.

2.3. Conceptual studies combining cash and accrual accounting

Some of the earlier discussed studies or parts of them or other studies pay also attention to the combination and the transition of the two accounting systems. Caperchione (1995, p. 70) considers the risk that the two opposite schools of thinking (protagonists and antagonists) will create compromises in terms of neither fish nor flesh. This will lead to obstacles and giving up a further interest in management needs. Similar conclusions can also be found in Jaruga & Nowak (1995, p. 95) stating that despite the adoption of accrual accounting, the government's cash approach still prevails due to its major role in providing budgetary information. Also in Belgium this budgetary prevalence is maintained in local governments and even dominates the accrual accounting system (Christiaens 2000).

2.4. Accounting practice studies concerning reform's technical implementation

Referring to some studies included in Table 1 the technical relationships between the former cash accounting and the new accrual accounting appear to be strongly different across different countries and governments. For central governments in Germany the study of Jones & Lüder (1996 p. 64) evidences that the basic accounting system has remained a cash accounting system resulting in an accrual accounting after reclassifications, eliminations, additions and accrual adjustments. This situation is similar for German local authorities (Lüder 1994, p. 71-75).

In the Italian local governments (Caperchione 1995, p. 71; Anessi & Steccolini 2000, p. 23) cash accounting is not abandoned; appropriation processes continue to be executed in terms of cash.

Table 2. Cash accounting and accrual accounting

ACCOUNTING SYSTEM	REPORTING
- Basis = cash accounting - In addition at year end through adjustments without of general ledger	- Budgetary financial statements - Balance sheet and Profit/Loss account

Thus, the Italian local governments have chosen for an additional accrual based reporting maintaining the cameralistic system rather than introducing accrual accounting. The pursued advantages of accrual accounting being introduced just as a kind of an "add-on", could be questioned. In UK agencies (Jones & Lüder 1996, p. 68) accrual accounting has to be adopted, but similarly as in Italy one could expect only an "add-on" to the traditional cash based accounting. In UK local governments new accrual accounting is developed separately from the budgetary system without being just an "add-on" (Glynn 1993).

For local governments in Spain (Montesinos & Vela 1996) and in France (Cotte, Milot & Nante 1995; Perreault 1995) the two accounting systems are included in one accrual-accounting-like general ledger by a division of the numbers of the accounts.

Table 3. Local governments in Spain and France

	GENERAL LEDGER DOUBLE ENTRY	
Country	*Cash accounting*	*Accrual accounting*
Spain	0, 4	1-5 , 6-7
France	9	1-7

The cash accounting numbers are used during the accounting period in order to record authorizations and encumbrances without immediately having in mind the patrimonial consequences. The resulting amounts receivable and amounts due lead to changes in assets and liabilities and are recorded in the accrual accounting system. In France the accrual accounting accounts are used only at year-end and there reasons to believe that this is also the case in Spain in practice.

One could criticize both of these kinds of integration in that *firstly* 0, 4, 9 accounts are not exclusive for cash accounting, they also used in accrual accounting and their use can create confusion. *Secondly*, cash accounting is disguised as accrual accounting by using its techniques and therefore it could create an adoption to the letter but not to the content. *Thirdly*, the different measurement focus and basis of accounting does not appear to be regulated, which might unsuccessfully lead to a full accrual accounting approach disregarding cash accounting or a factual dominance of the former cameralistic system though dressed in a accrual chart of accounts. Finally, this kind of reform is hard to impose since the accounting staff has to switch strongly its basic habits. Keeping the former system in force and enlarging it with additional accounting processing could avoid this problem. On the other hand a first approach of integrating the two systems exists and breaking down the class 9 into the budgetary classification of accounts, brings the two systems together.

In Belgian municipalities (Christiaens 2000) the existing budgetary accounting numbers were enlarged with an according accrual accounting number. An entry in the budgetary system creates on-line a journal entry in the financial accounting system.

Table 4. Belgian municipalities

ACCOUNTING SYSTEM	REPORTING
- Cash accounting + accrual accounting in one general ledger	- Budgetary financial statements - Balance sheet and P/L account

Apart from the automatic link between them, there are a limited number of possible entries in the financial accounting system, which are not recorded, in the budgetary accounting system. These unlinked accounts mainly represent non-cash items like depreciations, writing-off's, revaluations and stock movements. This obligatory technical combining of budgetary and financial accounting, which is in many respects incompatible, creates a conflicting situation implying an unplanned dominance of the former system.

In summary, these studies reveal a lot of different approaches across different countries and organisations apart from the implementation problems mentioned earlier. The reasons for this "chimera" (Jones 1995) are not clear. Some researchers argue that the difference and the numerous problems are due to a lack of conceptual framework in transferring business accounting concepts into the public sector (Christiaens 1999, 2000, Ellwood 1999, Anessi-Pessina & Steccolini 2000) and that this lack could lead to further irrational and expensive mix of systems (Caperchione 1995, p. 73). Another explaining factor is the incorrect assumption that a sudden reform will be adopted and implemented immediately just like that without any condition or consequence. On the contrary, reforms should be regarded and treated as projects in harmony with cultural aspects and with well-studied generally governmental accounting standards and not as facts. A third possible reason is the following: one could hypothesize that the diversity and the implementation problems are caused by a lack of technical accounting knowledge how to combine both systems in a technical way. Adapted accounting techniques being the means to implement the reforms are lagging behind the new public management intentions.

2.5. Remaining technical question

Almost none of the previous studies and even the last ones, which concentrate on practical issues, succeed in examining and explaining the technical questions of relating the two accounting systems. The relationships between the two systems are not thoroughly examined from a theoretical or a practical point of view. Particularly the different accounting principles, the different concept of timing of recording, the different typology of classification of accounts and sub accounts, the IT and behavioural aspects of introducing a second accounting system with its characteristics is neglected or disregarded. The lack of accounting research on this technical subject, the presumed occurrence of a poor adoption and a weak harmony in reforming public sector accounting and the differing function of a central provincial government, invite us to the following question: To what extent can the "Mega General Ledger" being a technical integration of cameralistic accounting, accrual accounting and cost accounting be a solution to prepare and to continue the transition?

3. MEGA GENERAL LEDGER

3.1. Integration

After having undergone the unsuccessful reform in Belgian municipalities, it was the intention of the provincial accounting reformers to firstly maintain the characteristics and advantages of the cameralistic accounting and secondly to achieve simultaneously the advantages of business accounting. It can be argued that many occurring problems of combining those accounting systems are due to the separate and often opposite principles. However, keeping the rules of each system in force and respecting those of the other system, can lead to a consensus. This means that in the approach of the "mega general ledger", it is the intention that the budgetary system respects its own budgetary rules without implications to the accrual system and vice versa. Likewise the analytical system plays the same role.

Instead of introducing accrual accounting without a general ledger (Italy) or making the cash accounting part of the accrual accounting general ledger (Spain, France) or imposing the same accounting rules for the two systems (Belgian municipalities), the mega general ledger attempts to keep three general ledgers simultaneously as shown in Table 5.

Table 5. "Mega general ledger"

BUDGETARY ACCOUNTING	FINANCIAL ACCOUNTING	ANALYTICAL ACCOUNTING
Single entry	Double entry	Double entry (single also possible)
G/L: Ecocodes	G/L: Accounts 0-7	G/L: Accounts 8-9
Budget	Annual accounts	Cost accounting statements
Budgetary account		

3.2. Processing

In the case of Belgian provinces the budgetary accounts to be used are the so-called "economic codes" (ecocodes), which have the first three digits of the more detailed financial accounts in common. In order to process all financial economic transactions correctly, a distinction is made between the accounting activities during the accounting period (e.g. a month or a trimester) and those specifically at the end of each accounting period. During the accounting period all transactions are recorded simultaneously in single entry budgetary accounting by using the ecocodes as well as in financial accounting with their according journal entries and lastly with their journal entries in analytical accounting. Until then the accounting systems are up to date in budgetary terms. In order to get a "true and fair view" a number of accrual adjustments are entered at the end of each period combined with their journal entries in analytical accounting. Most of these end of period recordings take place in the financial and analytical accounting system.

The three general ledgers can be visualised generally in Appendix 1. Particularly for the cycle of purchases Appendix 2 provides a zoom in a spreadsheet with three groups of columns. Each line represents the consequences of a transaction and this in three kinds of accounting systems. For a number of transactions the recording takes place simultaneously in the three systems; other kinds of transactions influence only one or two systems.

3.3. Advantages, strengths and opportunities

Adequate information using the according accounting system becomes possible: information concerning certain appropriations of certain budgets can be consulted as well as information about accounts receivable, etc. These kinds of information differ and a condition to succeed is the fact that one has to get used to think in three accounting systems with different results. Preparing periodically a state of reconciliation between the accounting systems would be an advice. Another advantage of the "mega general ledger" is that unwanted interference among the three accounting systems can be avoided. Each system corresponds with its own rules, not with the rules of the other systems and this is an improvement because empirical research has shown that often problems are due to mixing up different rules.

In terms of "accounting engineering" the "mega general ledger" is set up as a modular system, which means that each of the three accounting systems can stand alone. If desired, one could postpone implementing the cost accounting system without losing the advantages of combining the other two. Furthermore, the technical innovation is not an obstacle against the choice for certain accounting methods such as fund accounting.

Contrary to the situation in countries where accrual accounting could be called just an "add-on" at year end and where the management cannot use the accounting in the middle of the year, accounting information can be used more frequently in the "mega general ledger".

Attention is paid to the contextual aspects in that governmental accounting persons are used to process cameralistic accounting and they can maintain their knowledge and habits. This facilitates the adoption of the additional financial and analytical accounting methods since one starts from an unchanged well-known situation.

Nowadays many enterprises are integrating their financial accounting system and cost accounting (e.g. Activity Based Costing) as well their operational and strategic performance measurement system (Cooper & Kaplan 1999). This integration has in many cases been accomplished with enterprise resource planning systems (ERP) that integrate and coordinate all major business functions such as purchasing, production, marketing, sales, logistics, order fulfilment, plus support services (e.g. human resources, accounting). The facilities of ERP could also be used in governmental accounting. Apart from the financial accounting system, the cost accounting system and the operational and strategic performance measurement system, there will be a need to integrate a fourth system which is the budgetary accounting system. Using the technology of ERP governments could bring together their separate information systems into a single integrated system and the development of a "mega general ledger" is in line with this evolution. Unfortunately, research efforts regarding ERP in governments seem to be limited.

In the public sector reforms convergence (Ellwood 1999, Christiaens 2001) appear to be an important objective. It is noteworthy to mention that the concept and the adoption of a "mega general ledger" across different kinds of public sector organisations and different countries is a means to support/improve the aim for convergence of systems. For the moment one misses a generally accepted technical vehicle or device to carry out the reformed accounting job. IPSAS are being developed, but until now the themes remain general and the technical and automation aspects are not enough taken into consideration.

3.4. Critical issues

A traditional problem which is seldom explored, is the differing typology of accounts comparing cameralistic and financial accounting. In the latter, accounts are classified according to an external way of reporting. In the former the classification of accounts is driven by an internal authorisation point of view. Sometimes both of the classifications consider the same account, but there are also a lot of accounts having another meaning or content. In the approach of the Belgian provinces, one has installed the so-called "ecocodes" whose numbers are the same as the first three digits of the general accounts. This approach is not perfect and could be critisized since it makes compromises necessary. In summary, there is a need for studying a reconciled typology of the budgetary accounts and the financial accounts and one could hypothesize that the differing typologies probable occurring in many countries are an important factor explaining the current adoption problems. One could argue that the introduction of a "mega general ledger" will neither be value neutral nor policy neutral in practice. Therefore, the success of this innovation depends on the climate of receptivity amongst governments (Ryan 1998) and further research is needed.

Caperchione (2000, p. 74) remarks that there is a basic problem shared by many innovation attempts: an accounting system cannot meet widely divergent information needs at the same time. He mentions that the coexistence of cash accounting and accrual accounting creates risks for the quality of information referring to the probable dominance of the traditional cameralistic accounting. One could agree that indeed one accounting system should not be hybrid and that one's rules should not be dominant for the other. In the "mega general ledger" three autonomous accounting systems are harmonised and integrated meeting three different kinds of information needs.

In the current concept little attention is paid to the third central issue, which is the analytical accounting system. Implementing cost accounting systems necessitates the definition of cost centres, functions, products, etc. In the Belgian provinces one has chosen for a continuation of the former predefined functions. Although the provincial committee had the opinion that this classification of functions and thus cost centres and responsibility centres had to be reviewed and ameliorated, these aspects were temporarily set aside.

4. CONCLUSIONS

This paper attempted to show that in governmental reforms many accounting problems and conflicts are due to the lack of a technical means of combining and integrating harmoniously the different accounting systems governments are running into. Based on a review of existing accounting techniques and on the field experience in the standard setting activities in the Belgian provincial accounting reform, an accounting innovation (i.e. "mega general ledger") could be worked out. This innovation integrates three different accounting systems and could be useful also for other kinds of governments. Also in countries in which budgetary accounting of the kind of a cameralistic, authorization type always has prevailed, this innovation could be valorised.

A positive characteristic regarding its implementation is the fact that the former cameralistic accounting system primarily remains keeping its own rules and that the advantages of accrual accounting are achieved simultaneously without interfering. Being interested in governmental accounting reforms, it is not necessary to abandon the existing cameralistic system. Many negative perceptions seem to be due to the processing in practice, not to the concept itself.

There remains certainly need for further testing of the innovative concept in practice taking behavioural and IT aspects into account. A remaining problem is the search for a convergent typology of budgetary accounts and financial accounts. Hopefully, transferring business accounting to governments will have a better vehicle using the proposed integrated accounting approach and then the drifting apart of the governmental accounting systems could be stopped. Examining the conditions and contextual variables of implementing this proposed integration was not discussed; it could also be interesting for further research.

Appendix 1. Registration Process Mega General Ledger

Registration process	*Budgetary accounting*	*Accrual accounting*	*Analytical accounting*
During the accounting period			
Purchases			
1/ Definition of the budget	S	-	-
2/ Appropriation	S	-	-
3/ Delivery	-	-	-
4/ Receipt of the invoice and charging	S	D	D
5/ Payment	-	D	-
Revenues out of taxes			
1/ Definition of the budget	S	-	-
2/ Amounts receivable	S	D	D
3/ Receipt of the payment	-	D	-
Revenues out of services			
1/ Definition of the budget	S	-	-
2/ Delivery of services	-	-	-
3/ Billing	S	D	D
3/ Receipt of the payment	-	D	-
Investments			
1/ Definition of the budget	S	-	-
2/ Appropriation	S	-	-
3/ Delivery	-	-	-
4/ Receipt of the invoice and charging	S	D	D
5/ Payment	-	D	-
Staff			
1/ Definition of the budget	S	-	-
2/ Appropriation	S	-	-
3/ Voucher	S	D	D
4/ Payment	-	D	
Adjustments at the end of the accounting period (e.g. month)			
1/ Stock movements	-	D	D
2/ Invoices, credit notes to receive	-	D	D
3/ Depreciation and revaluation	-	D	D
4/ Written-off amounts	-	D	D
5/ Transitory items	-	D	D
6/...			

S / D / - = Single / Double / No entry

Appendix 2. Detail Mega General Ledger: Purchase Cycle

Purchases during period	BuAcc	Fin.Acc Dt	Fin.Acc Ct	An.Acc Dt	An.Acc Ct
1) Definition of the budget	X	-	-	-	-
2) Appropriation	X	-	-	-	-
3) Delivery	-	-	-	-	-
4) Receipt of the invoice and charging	ecocode 60,61,64	60,61, 64	440, 48	/98, /90 Ind.c.	-
5) Payment		440	55	-	-
Adjustments at end of period	BuAcc	Fin.Acc D	Fin.Acc C	An.Acc D	An.Acc C
Invoices to receive	-	60,61	440	/98, /90 Ind.c.	-
Stock movements start	-	609	3	/98 PI	-
Stock movements end	-	3	609	-	/98 PI
Disposal of material	-	-	-	89, 90	98 PI
Written-of amounts on stocks	-	63	3X9	-	-
Transitory items: deferred charges, deferred income, (analoguous accrued charges, accrued income)	-	490	60,61	-	-

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GWENDA R. JENSEN

REPORTING GOVERNMENT OBLIGATION

1. INTRODUCTION

This paper considers whether present accounting concepts and existing practice support increased recognition of the future costs of social welfare obligations. A review of arguments considered by the Federal Accounting Standards Advisory Board (FASAB) and the New Zealand Treasury indicates that there are major weaknesses in the conceptual arguments for present recognition practice. Governments should expect to experience pressure to increase their recognition of future costs. That pressure will come from the momentum inherent in a change to business (accrual) accounting combined with present political concerns about the future costs of social welfare and social insurance programs. This situation presents research opportunities.

The first section is an overview of present business (accrual) accounting practice for social welfare obligations. The accounting practices of the New Zealand, Australian, United States of America, and the United Kingdom governments will be described. Next, a description of the most likely alternative recognition approach is given. Third, the main technical accounting arguments for and against increased recognition will be described. While the primary focus is on New Zealand accounting practice and principles the relevance of these for future developments in international public sector accounting standards will be shown. Fourth, likely sources of pressure on governments to increase their recognition of social insurance obligations will be discussed. Last, opportunities for research arising from this issue will be considered.

2. PRESENT ACCOUNTING PRACTICE FOR SOCIAL WELFARE OBLIGATIONS

Government obligations can be divided into two broad groups – ordinary business obligations and social welfare obligations. The first group includes all obligations that are similar in purpose and type to obligations that any private sector company would have. For example, public debt, accounts payable (for services or goods received), government employee remuneration obligations (including government employee superannuation scheme obligations), and finance lease obligations. This

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 203-215.

first group includes insurance and superannuation provided to government *employees* - what the FASAB calls "insurance programs".

The second group – the social welfare group - includes such things as governments' obligations to provide welfare payments to the unemployed, to pensioners, and the sick; and obligations to provide free or subsidized education and health care. These obligations have not arisen due to an employment relationship between the recipients and the government. The group is defined here to include both "general assistance" and "social insurance" obligations, as defined by the FASAB. New Zealand Superannuation, and the New Zealand Government's accident insurance scheme are properly included within this group.

Presently, the New Zealand Government recognizes a liability equivalent to the "due and payable" amount for social welfare obligations that involve regular payments to beneficiaries. There is one exception to this policy. In 1999 the New Zealand Government decided to change its accounting policy for its accident insurance social welfare scheme from the due and payable policy to one where the present value of claims incurred is recognized. The Australian, American and United Kingdom governments apply the same recognition practice. The United States Government's reporting is distinguished by its extensive additional disclosures about its "social insurance" programs.

The "due and payable" amount is the amount due to be paid at balance date but not yet paid. For example, if benefits are paid fortnightly in arrears and balance day is three days into a new payment period then the "due and payable" amount is three days worth of benefits. If the balance day and payment day are the same day then the due and payable amount is zero.

Unless something happens to delay payments, the "due and payable" liability will usually be negligible. So long as benefit payments are made frequently and at regular intervals, reported expenses will be approximately the same as expenditure using this recognition policy. While the reported numbers will be the same as cash payments in ordinary circumstances, this accrual adjustment does ensure that a government cannot manipulate its annual reported benefit expenses by either delaying or anticipating benefit payments at the end of the financial year.

The "due and payable" recognition policy implies that a beneficiary must continue to qualify (or "earn") a benefit in order to continue to receive the benefit. An alternative view is that beneficiaries will continue to receive a benefit once they have qualified for the benefit. This conceptualization implies that the government's social welfare support is similar to an insurance policy. The government is obliged by legislation to provide financial benefits if the "insured event" occurs. For example, the existence of unemployment benefit is equivalent to income insurance; the government has insured citizens against becoming unemployed. Once the insured event has occurred, the obligation to provide future financial benefits exists. Recipients have met the necessary payment conditions. The government's future costs are unconditional and a liability for these costs exists. In its discussion of accounting for social insurance, the FASAB described this recognition approach as recognizing "...the unpaid expected present value (PV) cost of insured events that had occurred".

The liability is not a present value of all expected future costs. The liability only reflects the future costs of obligations that exist at balance date. At balance date, a present value of the expected future costs of supplying the benefit to those beneficiaries that have met the qualifying conditions is calculated. For example, to calculate such a liability for the unemployment benefit would involve estimating the expected average time unemployed and the cost of future payments for those presently unemployed as at balance date. Usually an actuarial calculation is done to determine the liability. For most social welfare obligations, future costs arising from "claims incurred" are significant. The liability reported using a "future costs of existing claims" recognition policy would show the present value of these future costs. Therefore, the reported liability using this recognition policy will be significantly larger than the liability reported using a "due and payable" recognition policy.

The amount of the reported liability will be affected by factors such as qualifying population, discount rate, inflation rate, scheme experience, and benefits provided. For example, if the number of unemployment benefit recipients remains constant but experience shows that they are likely to remain on the benefit for longer, then the reported liability using this recognition policy will increase to reflect that new information. Some of the New Zealand Government's benefits are adjusted to maintain parity with salary levels – salary inflation indexing. If a government decides to remove indexing i.e. to freeze benefits, then this would reduce the size of the reported liability and affect the reported expense.

All four governments have adopted essentially the same accounting practice for social welfare obligations. Why then consider an alternative recognition policy when what appears to be emerging is international consensus over the best accounting practice for such obligations? In fact, the situation is not as settled as first appears. There are consistency problems with existing practices. There are also problems in applying accounting principles to existing practice.

While a majority of FASAB members found that the due and payable recognition policy should apply to this group of social welfare obligations (FASAB 1999,paragraph 52), the FASAB was seriously split over its consideration of accounting for social insurance (FASAB 1995 , paragraph 7). For the only social insurance program that it runs – its accident insurance scheme - the New Zealand Government does not use a due and payable recognition policy. Instead, the New Zealand Government has adopted the same policy used by private sector insurance companies and recognized the future costs of claims incurred. Because the boundary between social insurance and other types of social welfare obligations is unclear, this consistency problem is not confined to the social insurance subset of social welfare obligations. FASAB does not provide criteria to distinguish social insurance from other obligations and admits the difficulty of doing so. Instead FASAB identified five relevant characteristics and listed specific programs that would be covered by SFFAS-17: *Accounting for Social Insurance.* Using the FASAB characteristics the New Zealand accident insurance scheme could fit into either the social insurance or general assistance categories.

In New Zealand the advent of a new accounting standard, (FRS-15: *Provisions, Contingent Liabilities and Contingent Assets* (FRS-15)), based on the international standard on accounting for provisions (IAS-37: *Provisions, Contingent Liabilities* *and Contingent Assets* (IAS-37) highlighted the difficulty of aligning the due and payable recognition policy with present accounting principles. IAS-37 and FRS-15 apply the liability definition and recognition principles set out in conceptual frameworks accepted in Australia, New Zealand, the United Kingdom and America. The New Zealand Treasury requested that social welfare obligations be scoped out of FRS-15 because of concerns that the standard could be understood to require increased recognition of social welfare obligations. The IFAC Public Sector Committee plans to apply the same liability definition and recognition criteria in the IPSAS on accounting for provisions and has already discussed the difficulties encountered in New Zealand. So beneath the surface of accepted practice, there are problems arising from practice and principles.

3. ARGUMENTS FOR AND AGAINST INCREASED RECOGNITION

As described above, the alternative recognition policy involves recognizing a far larger proportion of future costs for existing social welfare obligations. This section describes the arguments for and against increased recognition of future costs. These arguments are drawn from two recent considerations of this issue. The FASAB looked at this issue as part of the development of accounting standards for liabilities (SFFAS-5: *Accounting for Liabilities of the Federal Government,* issued in 1995) and social insurance (SFFAS-17: *Accounting for Social Insurance*, issued in 1999). The New Zealand Treasury considered this issue in response to a draft New Zealand financial reporting standard on accounting for provisions and contingencies - ED-86 Accounting for Provisions, Contingent Liabiities and Contingent Assets (the exposure draft leading to the final standard FRS-15).

Social welfare obligations cover a diverse range of different financial arrangements. Each arrangement needs to be evaluated on its own merits. The following discussion summarizes the New Zealand Treasury and FASAB considerations of this issue in the context of their respective governments' present social welfare obligations. While the social welfare obligations are specific to their respective governments, the accounting principles applied by the FASAB and the New Zealand Treasury together capture the range of principles that the IFAC Public Sector Committee could apply in its deliberations on the same issue. The FASAB and New Zealand Treasury applied similar accounting principles. These principles are set out in SFFAS-5 and the New Zealand *Statement of Concepts for General Purpose Financial Reporting* (*Statement of Concepts*).

SFFAS-5 states that a liability is a *probable* future *outflow or other sacrifice* of resources as a result of *past transactions or events* (FASAB 1995, paragraph 19). Financial reports "should recognize *probable* and *measurable* future outflows or other sacrifices…" The general principles appear to be the same as those in the New Zealand *Statement of Concepts.* However, SFFAS-5 then divides liabilities into two broad categories – "exchange transactions" and "non-exchange transactions". Within the non-exchange transactions category different obligations are classified according to the type of event that initiates an obligation.

Social welfare arrangements are generally "non-exchange transactions". SFFAS-5 states that:

> For federal non-exchange transactions a liability should be recognized for any unpaid amounts due as of the reporting date. (Paragraph 24)

The New Zealand *Statement of Concepts* states that a liability exists when there is a *present obligation* (legal or constructive) as a result of a *past event* with the result that a *future outflow of economic benefits* will be required to settle the obligation (ICANZ 1993 paragraph 7.10). If the outflow of economic benefits is *probable* and can be measured *with reliability* then a liability should be recognized (paragraph 7.14).

The New Zealand debate focused on both the *Statement of Concepts* and an exposure draft (*ED-86*) that operationalized the *Statement of Concepts'* liability definition and recognition criteria. ED-86 was a direct copy of an international accounting standard dealing with accounting for provisions - IAS-37. IAS-37 applies the same liability definition and recognition criteria as those in the New Zealand *Statement of Concepts*. (This is no coincidence. The same criteria are shared by those jurisdictions that have statements of accounting principles (the United States of America, Australia, New Zealand, and the United Kingdom). IAS-37 (and therefore ED-86) added two points to the basic definition and recognition criteria. First, IAS-37 states that where it is more likely than not that a present liability exists it should be deemed to exist (IASC 1998, paragraph 15). Second, IAS-37 states that a reliable measurement will be able to be made except in extremely rare circumstances (IASC 1998, paragraph 25).

Both the FASAB and the New Zealand Treasury considerations concluded that only the due and payable amount should be recognized for social welfare obligations (FASAB 1999 paragraph 8, New Zealand Treasury 1999 and New Zealand Treasury 2000). However, their conclusions differ in the extent to which they were viewed as reflecting existing accounting principles. The FASAB was split over whether the principles applied supported increased recognition of social insurance obligations. A majority held that the principles supported the status quo and did not support increased recognition. The New Zealand Treasury found that the principles *as operationalized* in the draft standard ED-86 either required increased recognition or could be viewed as requiring increased recognition.

Both the FASAB and the New Zealand Treasury considerations considered that there was a probable future outflow or future sacrifice of economic benefits due to social welfare obligations. Clearly a future sacrifice exists. The key issue with respect to these two criteria arises from the issue of probability and is driven by whether or not the government can *avoid* the future costs. Therefore, it is dealt with as an *avoidability* issue – i.e. whether or not there is an existing obligation - rather than a probability or future economic sacrifice issue.

The liability definition requires that a transaction or event that creates the liability has happened. In ordinary commercial transactions there can be doubt about the relevant event or transaction. Financial reporting standards will often provide guidance on how to determine the relevant event. For example, IAS-37 stipulates a number of factors (detailed plan, plan made public or in process of being implemented, etc) that must be present before the future costs of an entity's restructuring plans can be recognized as a liability (IASC 1998, paragraph 72). IAS-37, FRS-15, statements of accounting principles, and other accounting standards emphasize a number of key factors that indicate that an "obligating event" has happened. The factors include that an entity's obligation is now unavoidable; there are no further conditions that a recipient must meet in order to qualify for receipt of economic benefits from the entity; the other party has a valid expectation of receiving the benefits, the other party will rely on receiving the benefits; and, the consequences (economic, political or legal) are such that the entity cannot avoid the future cost.

The FASAB consideration distinguished between exchange and non-exchange transactions. SFFAS-5 and SFFAS-17 note that an exchange transaction indicates a strong claim on the government's resources at the point that goods or services have been supplied. Therefore this distinction relates to the avoidability question. Whether or not an exchange transaction has happened, the existence or otherwise of an equitable claim, and the probability of future payments are all identified as significant factors in the liability recognition decision:

> Although a high probability may exist that a grant, a subsidy or an income transfer will be made or will continue to be made in future years, the recipients do not have as high an equitable claim to receive grants, subsidies, or transfers in the future as do those who exchange services for promises of future payments. The latter have a greater probability of being paid than the former. At the same time, many people feel that some social insurance benefits, Social Security in particular, also have similar "exchange" or "equitable" claims. They also believe that social insurance benefits have as great a probability of being paid as any other payments (FASAB 1999, paragraph 62).

The FASAB consideration notes the lack of an exchange event but does not explicitly replace that event with another relevant transaction or event. Its consideration of other possible recognition policies implies other possible past events such as the passing of relevant legislation, recipients meeting necessary conditions for payments, and recipients accumulating a right to payments through payment of targeted taxes.

The New Zealand Treasury considered that the main significant events to consider were: the passing of social welfare legislation that committed the government to a future economic sacrifice; beneficiaries meeting the criteria to receive a particular benefit; and, beneficiaries having a legal right to receive present payments. For some benefits (education services, superannuation benefits) the only further requirement needed to receive the benefits, once the legislation was passed, was the passage of time. For other benefits a further qualifying condition had to be met. For example, a beneficiary had to be out of work in order to qualify for unemployment benefit. Both the FASAB and New Zealand Treasury considerations of past event focused on whether or not an event conferred an unavoidable obligation on the government.

Future governments can change existing entitlements if they so choose. Future governments can change the legislation that confers benefits. Yet the unavoidability of future payments seems to be a fundamental requirement if an obligation is to be recognized. The avoidability of future social welfare payments appeared to both the FASAB and the New Zealand Treasury to be a strong argument in favor of the due and payable recognition policy. However, the New Zealand Treasury's consideration found serious flaws in this argument. The FASAB arguments against increased recognition held that meeting the conditions to receive future benefits did not give the recipients of social insurance and general assistance benefits a legal right to receive future benefits. Recipients could not cash up this right. Recipients could not force the government to pay benefits in the future. The government retained its ability to avoid future costs.

The FASAB arguments against increased recognition rely in part on a government's power to over-turn present arrangements and the inability of present legislation to bind the decisions of future governments. For FASAB members opposed to increased recognition "...the political nature of the commitment is critical, for its terms can be and are changed by the Congress to maintain actuarial balance (FASAB 1999, paragraph 65)."

The contrasting argument was that recipients "earned" a right to future benefits by providing money from taxes ear-marked for those future benefits. This argument identifies the past event for liability recognition as being the payment of taxes. Arguments against this were that no legal right was conferred by payment of taxes, the government can and does change recipients benefits unilaterally, and there is a lack of reciprocity between taxes paid and benefits received (with high payers receiving relatively low benefits and vice versa).

The FASAB's final decision emphasized a recipient's *legal* right to receive future payments rather than the possibility that a *constructive* obligation exists. A constructive obligation exists when an entity will not ordinarily avoid the obligation even though the entity is not legally bound and even though the recipient does not have a legal right to the future payment. If a recipient has a "valid expectation" that he or she will receive future benefits and relies on that expectation then an obligation exists. Examples of such obligations are unvested employee entitlements and the future costs of restructuring.

The concept of construction obligation and a wider view of the existence of an obligation was presented in the opposing members' arguments. In the FASAB consideration those in favor of increased recognition held that the distinguishing characteristics of social insurance programs "...in conjunction with the historical experience and political climate affecting the programs, create obligations and societal expectations that make the outflow of resources highly probable – far more than 50 percent (paragraph 74)." This view was supported by the requirement that individuals must pay taxes in order to establish an "insured status" and be eligible for benefits, and that there is usually a link between taxes paid and benefits received. Some FASAB members also argued that the obligations are constructive liabilities and "users of financial statements are accustomed to seeing commitments as firm as these quantified in financial statements or in notes to the statements (paragraph 76)." Finally, members argued that if the exchange/non-exchange issue were treated as irrelevant then, applying the Financial Accounting Standards Board (FASB) concepts statement asset/liability perspective, "...the only reason for not recognizing a liability for the amount promised by the social insurance program would be the assumption that it may not be paid (paragraph 77)."

This final argument was tested by the New Zealand consideration. The New Zealand *Statement of Concepts* requires the same asset/liability perspective as that required by the FASB concepts approach. As will be seen, the results of that consideration supported this argument and went still further in concluding that even the possibility that future payments will not be made is not necessarily a sufficient basis for non-recognition because recognition is based on legislation that applies at balance date rather than possible future changes.

The New Zealand Treasury found that there were problems with the argument that governments can change legislation and thus avoid making future social welfare payments. First, the actual wording of the proposed standard on provisions – ED-86 - did not make unavoidability a necessary criterion for an obligation to exist. Second, as discussed above, ED-86 did not require that an obligation be legally binding before it could be recognized. Instead ED-86 used the likelihood that an entity would be bound to meet future costs as the determining factor as to the existence or otherwise of an obligation. If it was probable (more likely than not) that an obligation existed then it was deemed to exist.

A more serious weakness was that the avoidability argument conflicts with a fundamental precept under-lying financial reporting. The New Zealand Government's financial statements are prepared on the assumption that the legislation enacted at balance date will continue into the future. The financial reports reflect conditions that apply on balance date. Possible future changes to the legislation are irrelevant. This precept affects a multitude of individual reporting decisions – accounting for conservation land, student loans, government employee superannuation, the Government reporting entity boundary etc. Without this principle, the financial statements become a collection of subjective statements about what might be in the future rather than an objective statement about the situation that exists at balance date. Despite this understanding, the New Zealand Treasury's submissions on ED-86 included the avoidability of future payments as an argument in favor of the present due and payable recognition practice.

The FASAB reliability arguments against increased recognition referred to the *uncertainty* around future payments. Members argued that:

> ...the level of future benefit payments is too uncertain for accrual as a liability. ...Congress is able to change any provision in the Social Security Act, and has made changes frequently in the past. Furthermore, estimates of future benefit payments depend on economic and demographic variables that leave scope for wide variations between low and high cost assumptions and large changes when estimates are adjusted for new information (FASAB 1999, paragraphs 67-69).

Reliability of measurement is understood in two different ways: first whether or not there is a wide range of possible values; and second, whether or not the measurement value can be arrived at objectively. The New Zealand Treasury had previously considered this to be a strong argument against increased recognition. But the Treasury found that neither aspect of reliability represents a reason for non-recognition.

First, ED-86 required that if an objective estimate can be made then a liability should be recognized; only in "rare" circumstances would lack of reliability be an argument for non-recognition. The future costs of the New Zealand Government's social welfare obligations can be measured at least as precisely as other obligations that are already reported. Because of the size of the populations and the clear-cut definition of benefits many of these obligations can be determined with more precision than other obligations that are already reported.

Second, as previously stated, the financial statements show the conditions that prevail at the balance date and apply existing legislation. Possible future policy changes and future legislation changes should not be considered in determining liabilities at this point in time. "Reliable measurement" depends on the ability to make an *objective* estimate rather than an ability to determine the amount with precision. Objective verifiable estimates of future payment amounts can be made, by applying the policy and legislation existing at balance date.

In summary, while the FASAB consideration held that past event, avoidability and reliability issues could support a due and payable recognition policy the New Zealand Treasury consideration found real difficulties with these arguments.

Apart from issues surrounding the liability definition and recognition criteria, both the FASAB and the New Zealand Treasury had concerns about the usefulness of information reported under an increased recognition policy for social welfare obligations. SFFAS-17 describes arguments both for and against increased recognition using ideas of information usefulness. Information usefulness arguments exist on both sides of the recognition question. The likely effect and value of information involves judgments applied to many different factors – including both the relative importance of factors and users' likely reaction to new information.

Arguably, the liability definition and recognition criteria in conceptual frameworks have been developed in order to meet users' information requirements. If this argument is applied then there is no reason to delve behind the definition and recognition criteria and appeal to deeper principles of information usefulness. The concerns below about information usefulness highlight the potential for conflict between concepts statements' very high-level guiding principles and the lower level but more specific definition and recognition criteria.

The following highlight from SFFAS-17's basis for conclusions shows the main arguments *against* increased recognition from an information usefulness perspective:

> ...liability-type measures of the social insurance obligation (e.g., the closed group measure...) are meaningless or even potentially misleading. In particular, they argue that this information would not be useful to assess sustainability. It ignores the pay-as-you-go financing, excludes future earmarked taxes from future participants, and results in such an enormous actuarial present value that it may needlessly scare those unfamiliar with the debate. Such measures do not reflect the way the program is financed under current law and could, if taken out of context, imply that the current participants have a right to benefits superior to future participants (paragraph 71).

In support of increased recognition FASAB members argued that:

> ...the closed group number is a measure of the intergenerational transfer implicit in the program under its current terms and that this number should be reported. They would argue that the failure to disclose this number makes these programs look healthier than they are and thus may lead to poor decisions about consumption and saving by Congress and by citizens. Those who hold this view would argue that a closed group measure that treats social insurance benefits as earned annually would help users to understand the extent to which social insurance programs have committed future-year taxpayers to finance amounts earned by participants as of a given point in time (paragraph 77).

Because most users are familiar with FASB's definition, or at least are accustomed to seeing financial reports based on it, those who favor recognition or disclosure of a liability-type measure argue it is inherently misleading to fail to quantify the size of the promise that is continually being made and on which people are told they can rely. While many who support liability-type disclosure agree the open group data are desirable to aid in assessing the sustainability of social insurance programs, they also believe that an assessment of the financial condition of the program -- and more importantly, of the Federal Government -- is not possible absent liability or closed group data. If a reader seeks to answer the question -- Have we burdened future generations of citizens with the cost of the current and past years? and, if so, to what extent? -- the very large obligations for social insurance must be considered (paragraph 79).

The New Zealand Treasury was concerned that the reported information: would not be understood by users of the financial statements and be too different from information reported by other governments. If only one politically important obligation were recognized (for example New Zealand Superannuation) then it would imply that it mattered more than other obligations even though there were equally good conceptual arguments in favor of their recognition. If all of the government's social welfare obligations were recognized (education, health, etc) then the financial statements would be completely transformed. Would users of the statements understand the new information?

The New Zealand Treasury was also concerned that the reported information would incorrectly convey that the government was insolvent, unless an asset showing the government's ability to collect future taxes could also be recognized. The susceptibility of present value figures to large changes in value when discount rates changed would increase the level of "noise" in the operating result and obscure the effect of more significant changes to expenses and revenues. In addition to these negatives, the New Zealand Treasury was not convinced that the resulting information would help with decisions to fund and manage social welfare costs. Benefits similar to those identified by FASAB were also identified (New Zealand Treasury 2000, Appendix 2).

After the main internal New Zealand Treasury consideration which focused on liability definition and recognition criteria, a further argument was developed in support of the due and payable recognition policy. This argument - that social welfare obligations have characteristics similar to those of executory contracts - appears as an explanation for the scope exclusion included in the final wording of the New Zealand standard for provisions and contingencies, FRS-15. Accounting for social welfare obligations as though they were executory contracts implies two different conceptualizations of these arrangements. One conceptualization is that these benefits are similar to *salary payments*. Beneficiaries are on the government's payroll. They "earn" the benefit by continuing to meet the conditions of the benefit. At the end of the financial year both sides of the contract are mutually unperformed – the beneficiary has not yet continued to meet the necessary conditions into the future, the government has not yet paid future benefits. A second possible conceptualization is that there is an *executory contract* between the government and taxpayers (or citizens). The social contract is that taxpayers pay taxes each year and expect to receive social welfare and other services in exchange. At the end of the year both sides of this contract are mutually unperformed. Taxpayers have not yet paid future taxes. The Government has not yet provided future services.

In summary, while both the FASB and the New Zealand Treasury concluded that the status quo for reporting social welfare obligations should continue, there were serious difficulties in showing that basic accounting concepts and principles supported the status quo. The New Zealand Treasury consideration identified weaknesses in key arguments previously used to support existing recognition practice. Arguments based on social welfare obligations' lack of reliability, and the ability of governments to avoid future payments through changing future entitlements were found to have serious flaws.

4. PRESSURES TO CHANGE AND FUTURE RESEARCH

Governments are likely to experience pressure to change towards increased recognition of social welfare obligations. This pressure comes from a number of factors including: the desire for consistency with private sector reporting and public sector financial reporting practices and principles; public expectations that costs and liabilities be fully reported under an accrual basis for accounting; and needs to improve the information available for managing obligations.

These pressures were all evident in the New Zealand Government's decision in 1999 to change from a due and payable recognition approach to an approach that recognized the future costs of claims incurred for its accident insurance program. The desire to improve available information in order to better manage the accident insurance obligation was a particularly important concern. The simple fact that the scheme was called an *insurance* scheme meant that commentators expected that the same rules as those used to account for private sector insurance obligations should be used for this social welfare program. Arguably, the same factors (concerns about the management of the obligation and a name that suggests a particular private sector accounting approach requiring increased recognition) support the ordinary person's belief that there is a New Zealand Superannuation liability, which is presently unrecognized. In 2000 the New Zealand Minister of Finance told a Parliamentary Select Committee that for New Zealand Superannuation "...it is desirable to recognize[(1)] in some form the long-term liability." The Select Committee heard that recognizing this liability would add an estimated $170 Billion (328%) to the Government's reported liabilities. The associated expenses would transform the Government's present operating surpluses into deficits. Subsequently, the Minister decided that the Government would not change its present recognition policy for New Zealand Superannuation on the basis that a change would not be consistent with generally accepted accounting practice.

Most governments are either considering a change or in process of making a change to accrual accounting. For them these issues would appear far off. But these factors and their implications for reporting obligations are not unique to New Zealand. The move to accrual accounting with its associated promises and rationale has its own momentum. Once government accounting looks sufficiently like business enterprise accounting, business commentators experienced in evaluating private sector accounting practice apply the same approach to look at government accounting practice. Their expectations are that government accounting should apply existing best private sector accounting practice, unless the under-lying economic reality can be distinguished.

These issues raise questions about how governments and public sector financial reporting standard setters determine policies for reporting government obligations. What factors influence a government's reaction to these pressures? What factors determine accounting standard setters' positions on these accounting issues? How important are accounting principles in this debate? If changes to recognition or disclosure are made, are the decisions of key stakeholders affected by such changes? Where a standard setting body has not yet considered this issue but is likely to do so in the foreseeable future, a researcher has an opportunity to interview key decision makers prior to the decision and compare the factors on which they expect to place reliance prior to the decision and the factors that dominated the actual decision. Similarly, there is scope for comparatives between financial statement users' assessments of existing obligations before and after financial reporting changes. If a baseline study of statement users' knowledge of, and beliefs about, particular obligations is done *before* a government changes its reporting policy (either changing to provide additional disclosures or to recognize a liability), then the impact of providing the new information can be evaluated.

Government accounting is still evolving. Further significant accounting changes are foreseeable. This state of evolution provides the researcher with scope to learn more about how reporting entities and standard setters make accounting policy decisions, the relative importance of accounting concepts statements where these apply, and the impact of new reported information on financial statement users.

5.CONCLUSION

This paper describes a current issue with respect to accounting for governments' social welfare obligations and reviewed the technical accounting arguments for and against increased recognition that were considered by the FASAB and the New Zealand Treasury. These two considerations found weaknesses in the conceptual arguments for present social welfare liability recognition practice. The paper suggests that Governments will experience pressure to increase their recognition of future social welfare costs. That pressure will come from the momentum inherent in a change to business (accrual) accounting combined with concerns about the future costs of social welfare programs. Possible research opportunities arising from this situation were described.

NOTES

[1] "Recognition" means reporting a dollar value on the face of the basic financial statements.

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LÓPEZ HERNÁNDEZ, A. M.
CABA PÉREZ, C.
RODRÍGUEZ BOLÍVAR, M. P.

THE PRESENTATION OF GOVERNMENTAL FINANCIAL INFORMATION ON THE INTERNET: AN INTERNATIONAL VIEW

Many developed countries are currently reforming their public accounting systems, mainly in an attempt to bring them into line with accounting principles and practices used in the business sector.

However, we can still find major differences between the regulations on the presentation of public accounting information in a given country and the content of the financial statements through which the information is delivered.

In this context, it could be somewhat premature to consider, as we have done in this article, the degree to which public accounting information is provided over the Internet. However, public organisations, for reasons of image and prestige, are taking an increasing interest in offering the public their economic, financial and budgetary management information, thereby mirroring the situation in the private sector, where more and more firms are using the Internet to convey their financial information to the public (see Ashbaugh et al. 1999), since this is one of the mechanisms with the greatest distribution potential for all parties.

We would expect the digital distribution of public financial information via communication networks to progressively rise and, at the same time, to become more detailed. Currently, numerous governments are beginning to offer financial reports via Internet.

We sincerely believe that, in the foreseeable future, real-time on-line information will replace the way users currently receive such details.

In light of the above, this article presents the results obtained from searching and visiting the web sites of eleven governments and evaluating the content published therein, together with the structure of the sites themselves.

1. WORKING METHODOLOGY

1.1. Field of Study and Countries Selected

Although in recent years, there has been a clear convergence in how certain economic, financial and budgetary information is presented by the various public

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 217-229.

administration areas in each country, there are still differences to be overcome (Vela & Fuertes, 1997).

In order to avoid these disparities, which are highlighted even further depending on whether we are looking at the obligations to inform at a central, regional or local level, this work has concentrated on the area of central administration.

Due to the international heterogeneity in the public accounting practices of the different central administrations, our analysis only includes those countries in which the full or modified accrual basis is used to recognise financial statements, or in which there is a certain similarity between public and private accounting practices (see, among others, Montesinos, et al., 1998; Vela, 1997; Pina & Torres, 1996).

The countries we have chosen, all of which belong to the OECD and which follow the two leading trends in accounting normalisation processes are: USA, UK, Spain, France, Netherlands, New Zealand, Canada, Australia, Finland, Ireland and Greece.

1.2. Research Work Methodology

The methodology used was as follows. An index was elaborated in order to evaluate and compare the web sites of these governments. A scoring sheet was then developed so as to provide the potential Internet user with the relevant data necessary to gain a sound idea of the organisation's financial management by simply moving around the web site.

The research was not limited to the analysis of the type of public accounting information available on the web pages, but also looked at whether certain qualities were present in the accounting information provided and at the effort the governments had made to design a user-friendly web page. Thus, three sections can be differentiated: *a) Type of information supplied; b) Characteristics of the accounting information; c) Navegability, design and access.*

Our major problem was caused by the items chosen to analyse each of these three sections which were discussed and revised various times. As an initial approximation to an analysis of this type, in the selection we have aimed to show the most basic aspects of public accounting information, by comparing their presentation on the web pages of the previously-selected countries' central administrations.

To establish these aspects, we looked at the literature available on the private sector, discarding and including the concepts needed to adapt the scoring sheet to the field of public administration. We thus took into account some of the aspects included in the work of the International Accounting Committee (IASC, 1999), the Institute of Chartered Accountants in England and Wales (ICAEW) (Spaul, 1997), the Financial Accounting Standards Board (FASB), and the Canadian Institute of Chartered Accountants (CICA) (Trites, 1999). Likewise, we reviewed papers on the publication of the public accounting information of the various countries included.

The first section differentiates 13 items, while the second includes only 5 (although the last three items are divided into two subitems each) and for the third section 7 items were selected. Their distribution is shown in Table 1:

Table 1

	Number of items	%
1. *Type of information supplied*	*13*	*52%*
Budgetary information and cash-flow	6	24%
Financial position	5	20%
Non-financial information	2	8%
2. *Characteristics of the accounting information*	*5*	*20%*
Completeness	1	4%
Timeliness	1	4%
Comparability of the information	1	4%
Understandability of the information	1	4%
Relevance	1	4%
3. *Navegability, design and access*	*7*	*28%*
TOTAL	25	100%

1.2.1. Section 1: Type of Information Supplied

The aim of this section was to find out, on the one hand, whether the central administrations of the countries studied publish the accounting information on the Internet that, in terms of the recognition criteria used in this study, would otherwise be published by other means, for example hard copies. We also analysed whether any other additional relevant accounting information was included on the Internet which would enable visitors to the site to form an opinion on the organisation's financial management.

In order to do this, the structure chosen in this section attempted to include items related to the supply of information concerning budget, financial position and, finally, other non-financial information. Nevertheless, we should reiterate that our aim was not to cover all the variables and sections included in the General Account, but, rather, to attempt to identify the relevant informational aspects that would help the user to form an opinion on the management carried out.

For the scoring of these items, in most cases we used a dichotomous procedure in which an item scored one if the information was available on the web page, and zero otherwise. In some cases, as will be seen below, it was felt necessary to use a different scoring system.

Thus, a country's central government that offers all the budgetary and cash-flow information selected would be given a score of 6 points. In the same way, a government that only supplies information on the financial position would score a maximum of 5 points, and if only the non-financial information is provided, the score would be 2 points.

1.2.2. Section 2: The Presence of Certain Accounting Information Characteristics in the Data Published on Web Pages

This second section includes data on the extent to which certain characteristics of public accounting information are present. Thus, a survey was drawn up to check the existence of those qualities that, according to the literature on digital reports, are considered important when publishing accounting information. We therefore concentrated on the completeness of the accounting information (FASB, 2000), opportunity (ICAEW, 1998), understandability or clarity (AICPA, 1994), and comparability and relevance (Spaul, 1997).

The evaluation in this section was conditioned by the presence of the number of items analysed within each characteristic, with all of them being given an identical weighting in each of the characteristics of public accounting information.

At this point, we should establish which criteria were used to decide the inclusion, or otherwise, of some of the items that make up the qualitative characteristics in the information supplied over the Internet. Thus, we shall refer to the criterion followed with regard to the timeliness of the information, its comparability, its understandability and its relevance.

In studying the timeliness of public accounting information published on the Internet we concentrated on the presentation of two clear options: a) those countries that only supply yearly information on the Internet and b) those countries whose web pages offer more frequent information (monthly, quarterly, etc.).

The reason for this was the philosophy itself behind the inclusion of financial economic reports on the Web. According to the on-line reporting philosophy of the CICA (Trites, 1999), the advantages Internet offers as regards distributing accounting information include the possibility of obtaining constant information in real time, or, at least, more frequently than that established by the legal regulations used by countries to produce hard copies of their reports.

In view of this, and establishing the annual benchmark as a standard, any information offered over a shorter time span adds another quality (timeliness) that makes it more relevant to accounting information users. Therefore, in this case, a value of 1 would be given. Likewise, countries that only publish yearly on-line information would be assigned a 0, since they are not considered to be using Internet's potential to improve the timeliness of accounting information.

As for the comparability of accounting information, we believe it to be of paramount importance that the user has access to financial information from various financial years in order to be able to produce comparative reports. A second point of relevance would be that the organisations themselves prepare these comparative reports and upload them onto the Web. Each of these two items was given a value of 0.5 if they were present.

To establish a value of 0.5 or 0 for the first of these comparability items, we felt that this information should include more than two financial years. Information containing only two years or less would not lend itself to an adequate analysis of, for example, the evaluation of trends in the organisation. Thus, those administrations that gave public accounting information on the Internet for more than two financial years were assigned a score of 0.5, otherwise, they were assigned 0 points.

As regards understandability and relevance, both included two items with a score of 0.5 each. In the first case, for a better understanding of the information, a good combination of ratios and graphics is important, together with associated commentaries. As for the second case, we believe that this information is more relevant if the organisation has prepared and uploaded technical reports on this information, and if this information can be consulted separately; in other words, by sectors or activities.

1.2.3. Section 3: Navigability, Design and Access

In this section, we aimed to find out whether the organisation had created a site with a design that aids navigability and access to the information requested. We therefore looked at certain characteristics in the site's structure that, from our point of view, could affect the availability of the accounting information.

Here, with particular reference to the criterion of being able to download the accounting information in different electronic formats, we should mention that, unlike the previous sections where there were only two options (presence or absence), in this case we valued whether the information can be downloaded so that the user can handle, combine or summarise it according to his/her needs *(.xls)*, whether it can be downloaded but not manipulated (*.pdf or .doc*), or whether it is simply *.html* text.

Thus, using the reporting model established by the Special Committee on Financial Reporting at the American Institute of Certified Public Accountants (AICPA, 1994) as a basis, in which the possibility of downloading the information as an adaptable *.xls* file is considered to be important, we decided to give this characteristic a value of 0.5. On the other hand, the *.html*, *.pdf* or *.doc* formats would be given a score of 0.25 each. Therefore, countries that offer the chance of using all of these electronic information-processing formats would be given a maximum score of 1 in this section.

Thus, the total presentation score for the governmental financial information on the Internet (TPI) was obtained by calculating:

$$TPI = \sum_{i=1} p_i \qquad (1)$$

Where pi_i = 1 if the item is presented (in exceptional cases, 0.25, 0.5 or 0.75)
= *0 if the item is not presented*

Once all the items were scored, an index was created to measure the level of presentation of governmental financial information on the Internet (IPI):

$$IPI = \frac{TPI}{n} \times 100 \qquad (2)$$

Where n is the maximum score that can be presented; in our case, 25.

We should, however, point out that there could be partial indices for each of these sections – TPI_t for the type of information supplied; TPI_c for the characteristics of the accounting information; TPI_n for the navigability, design and access.

2. RESULTS ANALYSIS

Now that the framework of our study has been established, our aim is to apply the aforementioned methodology to the different countries selected. In order to do this, the three sections considered will be studied separately.

The scoring sheet was established after consulting the organisation's web page presenting the public financial information corresponding to November-December 2001.

2.1. Section 1: Type of Information Supplied

In the partial results, seen in Appendix 1, and beginning with the information offered on budget and cash-flow, we can see that most countries usually offer good information of this type. In fact, 90.9% of the countries generally obtain more than 4 points out of a total of 6. However, the Netherlands offers no information on the budget executed, and only gives information on the approved budget, an aspect that is generally included on all the web pages.

Likewise, in this section we can observe that little importance is given to publishing information on the Internet on the modifications made to the approved tax-year budget, since only 18.18% offer this information.

Providing information on cash-flows is, however, considered to be important, since this variable is included for 72.72% of the countries studied.

The data on the financial position published on the Internet shows a wider variety of situations than for budgetary information. 45.45% of the countries give deficient financial information, with scores of 2 points or less. For the study period, Spain and the Netherlands, countries that provide a high volume of budgetary information, fail to present any financial position data whatsoever.

It should also be pointed out that more than 72% of the countries considered Internet publication of information on public borrowing and its variation to be important, which was not the case for information on non-financial fixed assets and the operating statement.

The inclusion of non-financial information on the web pages is extremely low, it being provided by only 18.18% of these countries.

After compiling the results (TPI_t) for the analysed period we can see that the country with the highest number of points is Australia, followed by the USA and New Zealand. When establishing differences between the various countries, the Anglo-Saxon block stands out above the continental countries in terms of information supplied, as is apparent from their overall scores.

2.2. Section 2: Characteristics of the Accounting Information

With regard to the level of the qualitative characteristics of the accounting information, the results are relatively varied, although in general, all the countries are more or less on a par with the mean established in our survey (45.45% have a score of above 2.5). Again, the countries from the Anglo-Saxon accounting area achieve higher results than the rest.

It can also be noted that the most frequently observed qualitative characteristics are those which refer to comparability and understandability of the accounting information. These results are, in part, a reflection of the concern shown by central administrations to provide data that is useful to the various users of accounting information, in that one of their main needs is to compare public organisations over time, enabling a database to be created that helps to complete the historical overview of public finance evolution. Thus, comparability has traditionally been considered as an essential qualitative characteristic in the area of public accounting information (see Jones & Pendlebury, 1988, or Hepworth & Vass, 1984 on this subject).

In fact, the possibility for information comparability is only fully absent in the case of Spain.

Since the Internet is a means of communication that has greatly widened the public accounting information user base, it is logically necessary to compile and publish it in a manner that is understandable to all different users. Undoubtedly, one of the main advantages of the Internet is that it allows Public Accounts to be presented in a much more flexible way.

As a consequence, it is evident that the different countries attempt to make their information as understandable as possible (7 out of the 11 countries - 63.63% - fully observe the accounting information understandability characteristic). Most of the countries (81.8%) generally use tools such as ratios and graphs to give a clearer view of the financial information, supported, at the same time, by commentaries (7 of the 9 countries that use graphs or ratios also include this type of information).

On the other hand, it is surprising to see that the remaining characteristics are only observed to a level of around 50% in the countries studied, even more so when we consider, for example, that the Internet is able to provide continuous accounting information to all user types. In fact, the main advantage of this medium is based on the possibility of fully observing the requirement of opportunity??? by noticeably increasing the relevance of the information supplied.

Thus, on-line information, published in real time, adds value to the data supplied to potential users. However, only 45.45% of the public bodies provide this updated information, by giving complementary public data to the historical information already available on the management carried out.

Undoubtedly, if the information that can be taken from the Internet is incomplete, this will be prejudicial to the potential user, since the data published on the web pages should, at the very least, coincide with that supplied using other formats. For this reason, the hyperlinks needed to access the full information (in other words, the General Account), should be provided. However, this access is provided by only 45.45% of the governments studied, including certain administrations from the Anglo-Saxon area – USA, New Zealand, Australia, UK – and also one continental-area government – France –.

Finally, we should also refer to the relevance of the information supplied on the web page, which has been measured in terms of a greater diversity of the information, by taking into account, on the one hand, the publication of segmented information and, on the other, the drawing up of specific technical reports. Both of the items in this section are included in 27.27% of the governmental web pages analysed, indicating that most of the countries in the sample place little importance on supplying these details.

To sum up, once again, two of the Anglo-Saxon countries stand out above the rest in terms of accomplishment of the accounting information characteristics (TPI_c) -USA and Australia-, followed closely by another Anglo-Saxon country -New Zealand- and a continental-style nation –France-.

2.3. Section 3: Navigability, Design and Access

Regarding the availability of a specific hyperlink to the Accounting Board within the Department responsible for drawing up the financial information, less than 40% of the web pages provide one; in the remainder, the Departments themselves provide the information directly.

Likewise, it is significant that only 18.18% do not have a specific section on their web pages for financial and budgetary information.

If we combine the two data above (countries that do not have a specific accounting web page and do not have a specific section to include public accounting information) the percentage remains at 18.18%. The fact that this relatively small percentage of the web pages do not have links to the Accounting Board and, in addition, do not have a specific section for this type of information reflects the great importance now given to publishing public accounting information. However we hope that, in the future, all the central administrations will clearly differentiate this information on their web sites.

Having said this, the lack of a specific accounting section on the web site could, to a certain extent, be overcome by including a web map that gives an indication of the site content. However, none of the countries lacking in the two aforementioned characteristics provide such a tool on their pages. Countries such as the UK, Canada, Australia and the USA, however, do provide both a specific section and a web map, in order to simplify the information search process.

That the Internet is the first two-way mass communication media, allowing a degree of interactiveness between the financial information publisher and the receiver, is clearly highlighted by the fact that, in 90.9% of the cases, an e-mail address other than that of the webmaster is provided, which allows the user to ask questions and request information not included on the web page.

As for the processing language used to present the information, Spain is alone in using only the *html* language, which means that the information can be viewed but not downloaded. 63.63% of the countries usually combine this format with others that permit downloading - *.pdf* or *.doc* -. Lastly, an interesting aspect in this section is that two Anglo-Saxon countries – USA and Ireland – have also introduced a format that not only allows the information to be downloaded, but also provides the user with the possibility of creating his own reports; namely, the *.xls* format, for Excel spreadsheets.

Table 2 shows a summary of the values obtained for the different countries studied.

Table 2. Summary

	Type of information		Characteristics of the information		Navigability, Design and Access		Overall evaluation		
	TPI_t	Pos.	TPI_c	Pos.	TPI_n	Pos.	*TPI*	*IPI*	Pos.
USA	10	2	5	1	5	1	20	80%	1
Australia	12	1	4,5	2	3,5	4	20	80%	1
New Zealand	10	2	4	3	2,5	6	16,5	66%	2
UK	8	4	4	3	3,5	4	15,5	62%	3
France	8	4	4	3	3,5	4	15,5	62%	3
Canada	7	5	2,5	4	4,5	2	14	56%	4
Greece	6	6	2,5	4	4,25	3	12,75	51%	5
Spain	5	7	2	5	3,25	5	10,5	42%	6
Ireland	7	4	1,5	6	0,75	8	9,25	37%	7
Finland	9	3	1,5	6	3,5	4	14	56%	4
The Netherlands	1	8	2,5	4	2,25	7	5,75	23%	8

Another important point concerns the fact that since Internet represents the long-dreamt-of universal access to all types of information, at any time and in any place, this information should, ideally, be available in languages other than that of the country of origin. However, this does not seem to be a governmental priority, since only 66% of the non-English-speaking countries provide the information in English and none of the English-speaking nations consider it necessary to supply data in any other language.

One of the Internet's advantages is that it allows a certain flexibility in the content of the information supplied, which means that public organisations can modify the rigid structure of the General Account. Using a language such as *html*, as well as providing hyperlinks, allows for a more efficient access to the report, since it can easily be browsed. However, none of the cases studied provides this option.

If we place the countries in order according to the highest level of navigability, design and access to public financial information, the USA comes at the top, followed by Canada and Greece.

3. CONCLUSIONS

From the study carried out on the web pages of the organisations responsible for compiling the financial information for the central governments of the countries chosen, we can say that:

- There is a general consensus regarding the inclusion of information on the approved budget.

- Information of a budgetary nature is mainly provided, leaving the data on the financial position somewhat to one side.
- Including non-financial information on the web pages is virtually non-existent, with the exception of Australia.
- Access to the whole content of the General Account is virtually limited to the Anglo-Saxon area.
- Although some of the web pages have included the idea of on-line reporting, offering greater frequency than year-to-year information, data published in real time has still not replaced historical information.
- The idea of providing information that allows a degree of comparability is definitely present on virtually all the web pages.
- Likewise, the understandability of the public financial information is backed up by the inclusion of ratios or graphs, as well as commentaries on this information.
- Access to the information in most of the countries is made easier through hyperlinks or specific sections.
- Although a site map allows users to see what information is included on the pages, which is of utmost importance to the visitor, this idea has only been considered in Anglo-Saxon block countries.
- The use of a language such as *html*, which allows the information to be presented on the web page, but which does not allow downloading, is one of the most widely used formats. The information is also offered in *.pdf* or *.doc* formats, which are both downloadable documents.
- The use of Excel is given little importance in virtually all the countries, except for the USA and Ireland.
- The use of a hyperlink system that facilitates browsing around the accounting report is an idea that has not been taken on board (when the) in designing the web pages of any of the countries studied.
- Translating the accounting information into another language is not considered necessary in the English-speaking countries.
- Understanding that the Internet is a two-way information system, allowing interactiveness between the publisher and the receiver of the financial information, is a reality in most of the central governments, since they include an e-mail address other than that of the webmaster.

The final order following the overall evaluation of each of the web pages studied shows that the countries in the Anglo-Saxon area are in the highest positions. This same situation occurs when evaluating the type of information supplied, together with its characteristics.

APPENDIX 1

Score sheet of the aspects analysed to measure the presentation of governmental financial information on the Internet

	SP	F	NL	UK	GR
SECTION 1: TYPE OF INFORMATION SUPPLIED	5	8	1	8	6
Budgetary information and cash-flow	**4**	**5**	**1**	**6**	**4**
1.1. Information on the fiscal year budget.	1	1	1	1	1
1.2. Expenditure execution	1	1	0	1	1
1.3. Revenue execution	1	1	0	1	1
1.4. Budgetary result	0	1	0	1	1
1.5. Budgetary modifications	1	0	0	1	0
1.6. Cash-flow statement	0	1	0	1	0
Financial position	**0**	**3**	**0**	**2**	**2**
1.7. Information on non-financial fixed assets	0	1	0	0	0
1.8. Information on assets variation	0	1	0	0	0
1.9. Total borrowing amount	0	0	0	1	1
1.10. Variation in the public borrowing	0	0	0	1	1
1.11. Operating statement	0	1	0	0	0
Non-financial information	**1**	**0**	**0**	**0**	**0**
1.12. Indicators on efficiency, effectiveness and economy	0	0	0	0	0
1.13. Information on human resources	1	0	0	0	0
SECTION 2: ACCOUNTING INFORMATION CHARACTERISTICS	2	4	2.5	4	2.5
Completeness	**0**	**1**	**0**	**1**	**0**
2.1. The General Account can be consulted on the web page	0	1	0	1	0
Timeliness	**1**	**1**	**0**	**0**	**0**
2.2. Opportunity of the information supplied	1	1	0	0	0
Comparability of the information	**0**	**1**	**1**	**1**	**1**
2.3. Possibility exists for comparing the information	0	0.5	0.5	0.5	0.5
2.4. Comparative summaries of the accounting information elaborated by the entity itself are divulged	0	0.5	0.5	0.5	0.5
Understandability of the information	**0.5**	**1**	**0.5**	**1**	**1**
2.5. Ratios and graphics or back-up images are included to present the accounting information	0.5	0.5	0	0.5	0.5
2.6. Comments on accounting information are included	0	0.5	0.5	0.5	0.5
Relevance	**0.5**	**0**	**1**	**1**	**0.5**
2.7. Technical reports elaborated by the entity itself are divulged	0	0	0.5	0.5	0.5
2.8. Segregated information offered on the Internet	0.5	0	0.5	0.5	0
SECTION 3: NAVIGABILITY, DESIGN AND ACCESS	3.25	3.5	2.25	3.5	4.25
3.1. The Department responsible for compiling the financial information has a specific hyperlink to Accounting Board or similar	1	1	0	0	1
3.2. A web map showing the contents is available	0	0	0	1	0
3.3. The web page has a specific section that includes information on public accounting	1	1	0	1	1
3.4. A system of hyperlinks for the information offered is provided	0	0	0	0	0
3.5. Electronic formats used to process the accounting information	0.25	0.5	0.25	0.5	0.25
• .html	0.25	0.25	0.25	0.25	0
• .pdf o .doc	0	0.25	0	0.25	0.25
• .xls	0	0	0	0	0
3.6. Information content is available in different languages	0	0	1	0	1
3.7. A different e-mail address from that of the webmaster is provided to request information or explanations	1	1	1	1	1

APPENDIX 1: (continued)

	NZL	CAN	AUS	USA	IRL	FIN
SECTION 1: TYPE OF INFORMATION SUPPLIED	10	7	12	10	7	9
Budgetary information and cash-flow	**5**	**4**	**5**	**5**	**5**	**5**
1.1. Information on the fiscal year budget.	1	0	1	1	1	1
1.2. Expenditure execution	1	1	1	1	1	1
1.3. Revenue execution	1	1	1	1	1	1
1.4. Budgetary result	1	1	1	1	1	1
1.5. Budgetary modifications	0	0	0	0	0	0
1.6. Cash-flow statement	1	1	1	1	1	1
Financial position	**5**	**3**	**5**	**5**	**2**	**4**
1.7. Information on non-financial fixed assets	1	1	1	1	0	1
1.8. Information on assets variation	1	0	1	1	0	0
1.9. Total borrowing amount	1	1	1	1	1	1
1.10. Variation in the public borrowing	1	0	1	1	1	1
1.11. Operating statement	1	1	1	1	0	1
Non-financial information	**0**	**0**	**2**	**0**	**0**	**0**
1.12. Indicators on efficiency, effectiveness and economy	0	0	1	0	0	0
1.13. Information on human resources	0	0	1	0	0	0
SECTION 2: ACCOUNTING INFORMATION CHARACTERISTICS	4	2.5	4.5	5	1.5	1.5
Completeness	**1**	**0**	**1**	**1**	**0**	**0**
2.1. The General Account can be consulted on the web page	1	0	1	1	0	0
Timeliness	**1**	**0**	**1**	**1**	**0**	**0**
2.2. Opportunity of the information supplied	1	0	1	1	0	0
Comparability of the information	**1**	**1**	**1**	**1**	**1**	**0.5**
2.3. Possibility exists for comparing the information	0.5	0.5	0.5	0.5	0.5	0
2.4. Comparative summaries of the accounting information elaborated by the entity itself are divulged	0.5	0.5	0.5	0.5	0.5	0.5
Understandability of the information	**1**	**1**	**1**	**1**	**0.5**	**0.5**
2.5. Ratios and graphics or back-up images are included to present the accounting information	0.5	0.5	0.5	0.5	0	0.5
2.6. Comments on accounting information are included	0.5	0.5	0.5	0.5	0.5	0
Relevance	**0**	**0.5**	**0.5**	**1**	**0**	**0.5**
2.7. Technical reports elaborated by the entity itself are divulged	0	0.5	0	0.5	0	0
2.8. Segregated information offered on the Internet	0	0	0.5	0.5	0	0.5
SECTION 3: NAVIGABILITY, DESIGN AND ACCESS	2.5	4.5	3.5	5	0.75	3.5
3.1. The Department responsible for compiling the financial information has a specific hyperlink to the Accounting Board or similar	0	0	0	1	0	0
3.2. A web map showing the contents is available	0	1	1	1	0	0
3.3. The web page has a specific section that includes information on public accounting	1	1	1	1	0	1
3.4. A system of hyperlinks for the information offered is provided	0	0	0	0	0	0
3.5. Electronic formats used to process the accounting information	0.5	0.5	0.5	1	0.75	0.5
• .html	0.25	0.25	0.25	0.25	0.25	0.25
• .pdf o .doc	0.25	0.25	0.25	0.25	0	0.25
• .xls	0	0	0	0.5	0.5	0
3.6. Information content is available in different languages	0	1	0	0	0	1
3.7. A different e-mail address from that of the webmaster is provided to request information or explanations	1	1	1	1	0	1

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JOSÉ LUIS PABLOS RODRÍGUEZ
ANA CÁRCABA GARCÍA
ANTONIO LÓPEZ DÍAZ

THE DISCLOSURE OF FINANCIAL INFORMATION IN LOCAL GOVERNMENTS: STATE OF THE ART AND FUTURE DIRECTIONS

1. INTRODUCTION

On almost a daily basis, the media report news of the "deficient management" of our municipalities and, as a consequence, their delicate financial situation. The pages of local newspapers comment on the quality and quantity of services provided, the excess indebtedness ratios, the shortage of liquid resources or the heavy dependence on current grants. Some editorials try to justify local government practices while others take up the criticisms of the Opposition. However, despite the political use that is frequently given to this information, the large space devoted by the media to local management and finance reflects the growing interest of the public in the economic and financial health of the level of Administration they find themselves closest to.

Users of public accounting information, especially the citizens, demand access to data that allows the performance and financial condition of local governments to be evaluated, as a means of estimating the capacity of these entities to guarantee the feasibility of their financial and non-financial commitments to provide services. Public entities cannot refuse to cooperate with such demands, as politicians and public management must be accountable to those that have delegated these responsibilities to them.

In this context, the effective disclosure of financial information by local governments is seen as a basic requirement for accountability. The usefulness of the financial information formulated by the local entities depends to a large extent on its availability. Even if accounting statements are correctly formulated, their use would be scant if access to potential users is not granted. Appropriate diffusion of the financial information allows the government to remain publicly accountable, and can be interpreted as a bonding cost incurred to create an image of transparency, a reputation, that helps to justify past decisions and to form a base for future policies.

This paper analyses the role of financial communication in local public entities. The state of the art is presented in the first section, which includes a description of currently used tools of communication. The following section provides a detailed analysis of the annual reports. The analysis of current practices suggests a series of recommendations that Spanish local governments could implement in the drafting

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 231-246.

and diffusion of an annual report, guidelines that are provided in the last section of the paper.

2. STATE OF THE ART. CURRENT EXPERIENCES ON FINANCIAL INFORMATION DISCLOSURE

According to the *Green Paper on Public Sector information in the Information Society*, "Public information in Europe is often fragmented and dispersed and so in many instances it is less clear than intended. This situation is mainly due to differing national legislation on the ways information can be accessed and exploited, and to various practices which hamper the availability of data. The issue at stake is not that Member States should produce more information, but that the information which is already available to the public should be clearer and more accessible to potential users" (European Commission, 1998; par. 2).

In developed countries, the right of different user groups to access to financial information is granted by legal accounting provisions. The purpose of these provisions is to guarantee the availability of information, but, in most cases, local governments are not compelled to undertake a proactive disclosure policy. Practice evidences that access is not equally and completely granted to every public information user group.

In relation to this, Ijiri (1983) has suggested that, from an accountability perspective, a situation in which the *accountee* can access more information about the *accountor* is not necessarily preferable. Some degree of managerial privacy is always required, and thus an excess of information disclosure may thus damage the local government, and, in turn, society. However, real financial disclosure practices are not considered as a threat to privacy. On these grounds, many governments consider that financial disclosure should be reinforced. The following section analyses the two fundamental elements in the disclosure process: the reports summarising the information and the communication channels.

2.1. The Reports: From Financial Statements To Annual Reports

Currently, annual financial statements constitute the main tool for demonstrating public accountability. As the GASB (1987) has pointed out, financial statements are not the only source of information, but are "the core of the financial reporting and are the principal means of communicating financial information to external users".

Traditional financial statements reveal little concern for information disclosure. In continental Europe, local government accountability has been limited to budgetary issues, with information on assets, financial structure, and economic results taking second place. Traditionally, the accounts in these countries have been almost exclusively oriented to satisfy audit offices, resulting in extremely large reports of scant utility for the other groups of users[3]. The most recent accounting reforms show a marked interest in adapting the structure and content of financial statements to the needs of the users and, at the same time, in impelling the elaboration of new reports, as a means to foster communication among parties.

a) *Contents Enhancement of Traditional Financial Statements.* The multiple proposals recently aimed at enhancing the content of financial statements had a twofold objective. On the one hand, the inclusion of new information in these reports is considered to be essential in aiding governments to comply with their accountability obligations at various levels (from legal to managerial accountability). On the other hand, it is deemed appropriate to include textual explanations that may contribute to a better understanding of the reports, embracing a new conception of accountability that involves not only "inform of" but also "explain" the nature of transactions and the reasons behind them (Ives, 1987). The proposals imply the following:

1. To incorporate data that is useful in the analysis of the environment and the financial condition of the local entity (GASB, 1987; CICA, 1990, 1993; IFAC, 1991)[4].
2. Preparation and distribution of performance measures that enable managerial performance to be evaluated in terms of economy, efficiency, effectiveness and services quality (IFAC, 1991; GASB, 1994)[5].
3. Preparation of consolidated information including all the activities within the scope of the local entity's financial accountability, regardless of how decentralised its activities are.

The recent enactment of the 34th Statement of GASB (1999) confirms the importance of the points discussed above in the enhancement of public financial statements. Among the new features introduced in the 34th Statement the elaboration of a new financial statement, the *Management's Discussion and Analysis (MD&A)* is of particular importance, and seeks to provide an analytic, objective, and understandable overview of the government's financial activities[6].

b) *Elaboration and Disclosure of Annual Reports.* Public accountability requires heterogeneous information to be processed, from which financial statements occupy a central, but in any case unique, position. In order to assess public accountability and to inform decision making, the simple processing of such information for the drafting of reports is not enough. Rather, an increasing concern with the communication strategy is emerging as a priority. These concerns have induced the development of the so-called "annual report" or "financial report", which attempt to facilitate user access to financial information, providing an overview of the government's performance and financial condition. In order to achieve this objective, annual reports contain enormous quantities of economic, social, demographic, and, of course, financial information, concerning not just the government as a service supplier, but also as a geopolitical unit.

c) *Development of Reports Meeting Specific Needs.* Local governments must attend to the demands for information from different groups of users, whose interests on occasions involve specific financial or operating details. To cater for those demands, local governments produce the so-called "special reports", oriented to meet the specific needs of certain groups of users (politicians, audit officials, financial institutions, different tiers of government, etc.). What distinguishes these documents from the annual reports, which are intended for the general public, is the user group for whom they are designed. The local entity may be required to elaborate a special report in order to prove solvency when applying for a new loan, when deciding the final destination for intergovernmental aid, or even to justify an unexpected turn in the capital investment or tax policy[7].

So far we have focused on surveying current and emerging trends in the evolution of the financial reports elaborated by local entities. The next question to examine is how local governments disclose the information to the addressees. In other words, which communication channels are used to keep the users appropriately informed?

2.2. Communication Channels: The Emerging Role of New Information Technologies in Financial Disclosure

Nowadays, the most widespread communication channel for the disclosure of financial information in local entities consists of a printed copy of the budget and the annual financial reports deposited in the entity. Even though this copy is kept for public consultation, applicants are frequently refused access. This difficulty to access public information considerably limits research possibilities in this field, especially when trying to gather panel data on a large number of entities. Even when access is granted, the high cost of data gathering in most entities is another serious limitation to the current situation.

Fortunately, many local governments have begun to show greater interest in the final objective of financial statements, and have adopted a fully communicative attitude. For instance, practices such as depositing financial information in public agencies and libraries (New Zealand) or publication in the media (U.K.) are becoming customary in some countries. The purpose of such practices is to enhance citizens' access to information on the reality of the situation in local government. Today, the search for enhanced accessibility has led to the inevitability of the use of new information technologies, namely the Internet.

The use of new information technologies has an enormous impact on the standards of availability and diffusion of information, by introducing determinant advantages such as readiness, minimum effort, and low cost in communication. A growing number of public entities, not just in the U.S., but around the world in Canada, Australia, New Zealand, the U.K., France or Italy, provide financial information on the web[8]. Many local governments in these countries include the legally adopted budget, or at least its most important magnitudes on their web pages. Although less frequently, local entity web pages can also be found that include the financial statements, the integral and abbreviated versions of the annual report, and other documents containing useful information for the assessment of the financial condition and performance of the entity (long-term strategies, performance indicators, tax rates, statistics on economic and demographic evolution, etc.).

Following this examination of current trends and practices in local financial information disclosure, the next section provides a detailed analysis of the annual reports. The objective is to highlight the features that characterise these reports and differentiate them from other documents, and focus on their typology, structure, content, and presentation.

3. ANNUAL REPORTS IN LOCAL GOVERNMENTS AROUND THE WORLD

Delimiting and describing the precise content of annual reports is not an easy task, given the enormous heterogeneity that pervades the drafting of these documents. However, a high degree of heterogeneity makes comparisons more interesting. Table 1 shows the most interesting features of the reports elaborated by the local governments of the United States, Australia, New Zealand, France, and Spain, as well as some proposals taken from the institutional and academic fields. Even though the analysis was oriented to highlight the common features of the reports from different countries, clear differences arise even among documents presented in the same country, some of which will be discussed below.

Table 1. Contents and structure of annual reports

Country		EE.UU.	Australia	New Zealand	France		Spain	
Source		several cities	several cities	several cities	several cities	OEC guidebook	City of Barcelona	City of Madrid
Title[a]		CAFR/popular reports	Annual Report	Annual Report	Rapport annuel	Rapport annuel	Informe anual	Anuario económico financiero
Size (pages)		Variable[b]	40-80	90-120	20-40	Variable[b]	> 100	> 100
Institutional contents								
Mayor/executive message		×××	×××	×××	×××	×××	×××	×××
Economic and demographic data		×××	×	×	×××	×××	×××	--
Organization / structure of the entity		×××	×××	×××	×××	×××	×××	×××
Labour relations report (human capital)		×	×	--	×	×××	×××	×××
Achievements	Textual inform. services/policies	×	×××	×××	×××	×××	×××	×××
	Performance measures	×	×××	×××	--	×××	×××	--
	Costs of services	--	×	×××	--	--	--	--
Projects		×	×××	--[c]	--	×××	×××	--
Financial contents								
Analysis of financial statements	Revenues/taxes	×××	×	×××	×××	×××	×××	×××
	Expenditures	×××	×	×××	×××	×××	×××	×××
	Investment	×××	×××	×××	×××	×××	×××	×××
	Debt	×××	×××	×××	×××	×××	×××	×××
Financial statements	Entity	×××	×××	×××	×××	×××	×××	×××
	Consolidated inform.	×××	--	×	×××	×××	×××	×××
Appendix		×	×××	×××	×	×××	--	--
Glossary		--	--	×	×××	×××	--	--

--, ×, ×××: None, several, all the reports consulted contained this information.
[a] The most common title is given
[b] These entities elaborate two models of annual report: normal (about 200 pp.) and abbreviated (about 30 pp.)
[c] These reports include information on long-term financial strategy

In Anglo-Saxon countries, the publication of annual reports by local authorities is widespread. Given the strong influence of the notion of public accountability in these countries, this task has been induced by tradition rather than by legal obligation, although over recent decades, notable efforts have been made to standardise the reports.

Governmental units in the U.S. prepare and publish a report annually called CAFR (Comprehensive Annual Financial Report), which is included in the NCGA Pronouncement #1. This report is divided into three sections: a) the *introductory section* shows general features of the entity, such as its organisation chart, the services it provides, and the activities carried out; b) the *financial section* includes the auditor's report and the financial statements, along with a set of explanatory notes aimed to provide a better understanding of these statements; and c) the *statistical section* shows socio-economic and demographic data, financial trends, and the composition of taxable base, for various financial years. Sometimes local governments summarise the information gathered in the CAFRs by means of abbreviated financial reports, known as "popular reports". They are less detailed documents, intended for users whose financial information needs can be met with aggregate magnitudes, for instance, average citizens (GASB, 1987; par. 6).

Besides drawing up the annual reports discussed above, some U.S. governments have begun to publish and distribute specific reports on the measurement of the financial condition. This is the case of the State of New York which for several years has published a report aimed to "provide an overview of the State' finances, how tax dollars are spent, and how the economy affects taxpayers" (McCall, 1997). It is a short document that begins by showing economic and demographic trends (education, income level), and then examines the financial condition by means of evaluating the main magnitudes of expending by programme, debt, and capital investment. Its content is not significantly different from the *Financial Condition Report* published by the City of Seattle. In this case, the measurement of the financial condition is done through an analysis of observed trends in a battery of indicators concerning revenues, expenditures, debt, and economic and demographic data[9].

Local entities in other Anglo-Saxon countries such as Canada, New Zealand or Australia also publish annual reports, although with a less formalised structure and content. We have examined the reports presented by several Australian and New Zealand local entities, and have noted certain interesting features worthy of discussion. First of all, most of these documents include information on the entity's objectives for the financial year, which facilitates comparison with actual results[10]. Likewise, most of these entities – particularly those from New Zealand– include information on the net cost of services, computed as the cost of providing the service minus all revenue that might be allocated to those activities. All these documents also include a section devoted to environmental information on issues such as control of noise levels, water resource management, compliance with health and hygiene norms, and the maintenance of parks and reserves[11].

In continental Europe, the publication of annual reports is a relatively incipient practice motivated by recent legal requirements on State and Local Administrations.

To provide an idea of how European local entities are taking up the preparation of annual reports, we have examined the content of the reports from several French and Spanish cities.

In France, the first annual report was published in 1992. Since then, a growing number of French local governments have prepared annual reports. A survey carried out at the end of 1999 reveals that 26% of towns with over 100.000 inhabitants, 34% of the departments and 50% of the regions publish this type of document in France (Angotti and Laurent, 2000; 13). These entities follow the 1994 OEC guidelines, which have become the norm for the preparation of annual reports. These guidelines establish a clear difference between two types of reports: *les rapports financiers* include strict financial information, while *les rapports annuels* include a more extensive content, which also includes the financial information.

The poor development of annual reports in the Spanish Local Administration has limited our survey to the report prepared by the city of Barcelona. This city council publishes a very thorough document that provides information on the political and administrative organisation of the city council, its economy, the services provided to its citizens, and management details. It also includes a summarised version of the government financial statements, which are drawn up in line with the 1994 *Plan de Contabilidad Pública* (which has yet to be developed for local entities), as well as its consolidated financial statements.

The discussion above provides an overview of the development of annual reports in these countries' local governments. In the absence of a set of common rules to guide the preparation of these documents, the observation of notable differences between countries and even within the same country is not surprising. However, a detailed examination of the content of the annual reports reveals a series of regularities that provide interesting guidelines for their preparation:

1) *Typology and extension.* Most of the local governments examined publish two versions of the annual report: a detailed and extended *integral* version and a schematic and *abbreviated* version. The integral version, with over 100 pages, not only meets the information needs of the public, but also informs decision making and fulfils the requirements of other user groups with a demand for detailed information. The abbreviated version, from 25 to 30 pages, is intended for the ordinary citizen, and highlights the results and effects of the policies adopted during the financial year[12].

2) *Content.* The purpose of the annual report is to gather the most relevant information on the situation of the municipality and the effects arising from local government activity. It is not limited, thus, to a summary of accounting magnitudes. Rather, it includes varied information on demographic, socio-economic, and financial issues, and reasonably provides a "picture" of the council. Although there is considerable heterogeneity, the elements making up the report can be summarised in two major sections: in the first section, the entity informs on the activities undertaken during the year, while the second reports on the financial magnitudes that enable financial management to be assessed. The guidelines outlined by the OEC in the *Guide d'élaboration du rapport annuel* (OEC, 1994; p. 36) illustrate this structure:

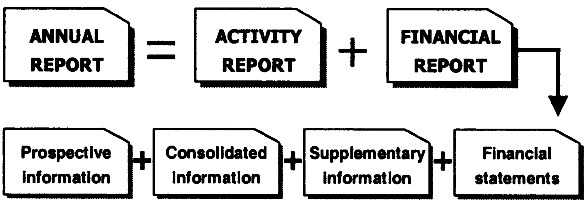

Figure 1. Structure of the annual report (Ordre des Experts Comptables, 1994)

The *activity report* begins with a message from the entity's political or financial leader, usually the mayor, who writes a brief message summarising and discussing the general trends in the evolution of the entity and its financial condition throughout the financial year, as well as initiatives planned for the future. Sometimes this message is accompanied or substituted by a letter written by the entity's chief financial manager, in which a more technical description of the report and a brief analysis of its main conclusions is presented.

The degree of complexity that sometimes characterises the structure of the local entity justifies the inclusion of an organisation chart in the report, indicating the divisions, commissions and departments that make up its political-administrative structure. A record must also be kept of all the entities involved in the provision of the services, in order to show the managerial pattern adopted by the entity and, consequently, provide an overview of the range of its services[13].

The report also includes information on the main demographic, economic, and social characteristics of the entity. This information is useful not only to describe the entity's environment, but also to assess the effects of public policies on the community. It covers population characteristics (age, sex, birth rate), the economic structure (productive structure, gross domestic product, unemployment), and environmental features (pollution levels, weather conditions, natural disasters). In the most elaborate reports, an exhaustive set of indicators can be found which evaluate quality of life, and enable the results of social welfare policies to be assessed. These variables summarise public services provided on aspects such as health, education, security, traffic, and culture.

In some of the entities examined, information on environmental features and quality of life is included in a separate statement, which reflects the importance attributed to these variables. For instance, the citizens of some Italian cities, such as Bologna and Rome, receive a brief report entitled *Lo stato (rapporto) della città*, with an abundance of charts and figures describing the demographic and socio-economic features of the city. Similarly, the *Perfil de la ciudad de Barcelona* reports a complete battery of indicators "oriented towards providing the citizen with a better knowledge of the current situation of the city, in an attempt to demonstrate public accountability" (Cotrina and Salvat, 1998).

A common occurrence in local government reporting is the complexity involved in the assessment of policy outcomes. In addition, the reports include detailed explanations about the actual provision of services, i.e. outputs. In some cases, this information is complemented with a set of performance indicators (especially British municipalities, which are obliged by the *Citizen's Charter* to publish periodic information on performance), and, sometimes, with estimates of the cost associated to each service.

The *financial report* constitutes the section of the annual report that is directly linked to the financial statements. All the reports examined analyse, to a greater or lesser extent, the content of the financial statements, focusing on features such as the budget implementation level, the volume and composition of the tax revenue, the importance of grants, the magnitude of capital expenditures, the evolution of indebtedness, solvency, and liquidity. The analysis normally examines the temporal evolution of a battery of financial indicators[14]. The financial statements follow this analysis, together with consolidated information (usually limited to budgetary data), and the audit report.

The information contained in the first section of the report, schematically presented, and some of the main financial indicators that summarise the second part, constitute the basic content of the abbreviated reports.

3) *Presentation.* The purpose of the annual report is not to amass an enormous quantity of information, but rather to communicate that information in a way that the average citizen can understand. To demonstrate accountability by means of the annual report is only feasible if the information offered, apart from rigorous, is also clear, understandable, and attractive to the citizenship. This objective justifies the wealth of charts, graphics, and pictures that illustrate the textual information.

The way chosen to present financial data is particularly important, since it may condition any subsequent analysis. The presentation may follow either of the following two approaches:

1) Figures and charts showing trends for the entity's main financial and economic magnitudes over a sufficiently long period. The *financial trend profile,* proposed by the ICMA (Groves, Godsey and Shulman, 1981), illustrates this approach.
2) Rankings comparing entities with similar characteristics. Despite the complexity involved in the elaboration of these rankings, a vast literature has embraced this approach. For example, Petro (1998) suggests presenting the average value of each financial indicator for each class of entities in the so-called *benchmark reports.*

4. PROPOSALS FOR THE PREPARATION OF THE ANNUAL REPORT AS A TOOL FOR FINANCIAL DISCLOSURE IN SPANISH LOCAL ADMINISTRATION

The lack of standardised guidelines for the preparation of annual reports is a significant barrier to the improvement of financial disclosure in Spanish local governments. The work in this field is limited to the contributions of Bolufer *et al.* (1996), and Pablos and Fernández (1999)[15], which describe the annual report as the device devoted to showing the essential magnitudes of the local entity's financial condition and performance. In an attempt to contribute to the further development of this field of research, we here formulate a series of proposals for the preparation of annual reports in Spanish local governments, by building on the existing literature cited above and on the practices observed in other countries.

The annual report should serve to assess the local government's performance, by providing an overview of the entity's situation. Its preparation therefore not only requires large quantities of financial and internal information to be processed, but also demographic, economic, and social information. These information requirements are normally available in the local entity, although in a less structured fashion.

The financial statements comprise the main task of the report, although this is not limited to the simple reporting of the statements, but rather constitutes a careful analysis of their content, complemented with other information from the implementation of public policies (objectives, outcomes, projects, and perspectives). The citizen should be able to find out the objectives and goals of the local government by consulting the documents generated in the planning process (strategic plan, investment plan, budget). However, the annual report provides an overview of the actual performance involved in the carrying out of these plans and the effects on the quality of life of the population.

Figure 2. The accountability cycle (Pablos and Fernández, 1999)

Thus, the true objective of the annual report should be to describe the cycle that begins and ends within each electoral period, when the elected representatives encounter the community in a certain situation, here called the *condition of the community*, and give an annual account of its evolution, which is determined by the policies undertaken, using the public resources that, at least partially, come from the local community (Figure 2). The content of the annual report meets this objective by incorporating: a) data concerning the environment and the financial condition, reflecting the outcomes on the *condition of the community*; b) data on the assessment of the entity's management in service provision, which will make up the *Management Report*; and c) information that allows an assessment of the entity's financial management to be made, in the *Financial Report*. Schematically:

- While the Condition of the Community Statement demonstrates the political accountability of the elected representatives, the Management Report and the Financial Report should contribute to financial accountability.
- The Condition of the Community Statement should contain enough information to assess the results of the activities of those involved in the development of the local community and, in particular, from the public policies undertaken. Even though these data could be summarised in the annual report, a separate presentation in an independent document may be preferable.
- The Management Report should contribute to determining the analytical results, by giving evidence of the outputs and costs of the services provided. If considered convenient, this section of the report could be presented in a separate document.
- The Financial Report should contribute to accounting for the financial management of the previous period, and be comprised of both legal and financial accountability.

The next section describes the content of the annual report in more detail. Questions about its presentation are also discussed (types, structure, diffusion). The purpose of this section is to formulate some comments and suggestions which will be helpful in the preparation of these documents.

4.1. Presentation

The reader should find the report appealing, rather than simply rigorous. A careful combination of numerical data, textual information, graphics, figures, and charts capture the reader's attention and make for a more understandable report. Two types of report must be prepared yearly:

- The integral report should contain exhaustive qualitative and quantitative information and a complete analysis of the entity's management and its financial and economic performance, in order to meet the needs of the most specialised user. It may be over 100 pages long, given the sizes of the financial statements it contains.
- The abbreviated report, intended for the average citizen's needs, should present the information and its analysis in a friendly way. In order to contain costs and facilitate its diffusion, it should not exceed 30 pages.

4.2. Content

The report should begin with a message from the Mayor or the President of the local entity, mentioning the legal requirements and the political will underlying the report[16]. Ideally, this should be followed by a second, more technical message from the Council's Treasurer and the chief financial manager describing the content of the report and the sources and criteria employed in its preparation. Information regarding the political and administrative organisation should follow. Finally, the main body of the report may be divided into three sections: the Condition of the Community Statement, the Management Report and the Financial Report.

a) The Condition of the Community Statement. The content of the first section of the report, on the assessment of the welfare outcomes of public policies, should follow these guidelines:

- It should reflect the evolution of a series of political, social, and economic indicators over the previous 4 or 5 years, to provide an overview of the situation of the city, and a discussion of the main projects carried during the current year.
- It should contain data on the ecological effects of the policies adopted by the entity, to demonstrate "ecological accountability"[17].
- It should contain the evolution of financial indicators over the previous 4 or 5 years, capable of showing the financial condition (strengths and weaknesses) of the city, and a discussion of the main projects carried during the current year.
- It should provide a long-term perspective on budgeting.

b) The Management Report. The second part of the annual report, known as the Management Report or Performance Report will demonstrate the management accountability of the entity, by showing the results obtained and the objectives pursued:

- It should contain accurate information on the composition and evolution of the entity's human resources. Similarly, it should reflect the activities carried out in promoting active workforce participation, equal employment opportunities, and training programmes.
- The *global analysis of economic management*, which focuses on the economic nature of the expenditure (i.e., which goods and services), should reflect the main sources of revenue and expenditure. Similarly, the most relevant economic ratios should be discussed.
- The *functional analysis of management* assesses the destination of the expenditure (i.e., to satisfy which needs), by means of a detailed examination of the costs and outcomes derived from each of the functions, services, and activities provided to the public. This task requires the enumeration of the objectives pursued, the structures and resources available for them to be attained, the net expenditure incurred, and the outcomes attained, including indicators showing the level of efficiency and effectiveness of the entity.

c) The Financial Report. The third part of the annual report demonstrates accountability in financial management, from both legal and managerial perspectives:

- The Financial Report can be broken down into two parts: the first analyses and interprets the entity's assets, liabilities, financial position and budgetary situation; the second contains the annual financial statements foreseen by the local regulations, accompanied by the audit report.
- The analysis of financial management requires an examination of the objectives and financial perspectives of the two years to which the financial statements refer. It should include an objective assessment of the circumstances that lead to deviations in the financial statements.

- It will contain an analysis of the most significant deviations in the budget. The financial report should also assess the extent to which the budget internal balances have been fulfilled, as well as the level and evolution of tax revenues.
- It should describe and analyse the indebtedness, and indicate whether this may affect the financing of future activities. It will also include an analysis of the financial position (solvency and liquidity), and indicate whether this has improved or deteriorated as a result of the activities undertaken during the year.
- It should contain an analysis of the commitments, events, and contingencies that may presumably affect the entity's financial position, its results, or its financial condition, including an assessment of the off balance sheet risk.

4.3. Disclosure

The communication process culminates with the disclosure of the annual report, i.e. with its being made available to the citizen. The entity should explain the main conclusions of the report in the local media, and also through public meetings involving those accountable for the management and the policies adopted. These activities give the citizen first hand contact with the report, and provide the government with an ideal opportunity for the presentation of the document.

The entity should have a physical copy of the integral report, which will be available for public consultation. It is also recommended that several copies be kept in public libraries and official agencies. The abbreviated report, which is shorter and less expensive, should be mailed to each household in the local authority area. As many of these citizens may not be familiar with this type of document, at least the first mailing should be accompanied by a brief presentation letter. The abbreviated report should clearly show how the integral report can be obtained.

The annual report should also be released through the entity's web page, in order to exploit the advantages of the Internet for the disclosure of financial information. The web facilitates the communication and interaction between the government and the citizenship in both directions. The availability of the report on the web reduces the costs and inconveniences associated with more traditional formats and also provides mechanisms which allow the citizen to formulate opinions and suggestions.

5. CONCLUDING REMARKS

In recent years, the limitations of the current model of public accounting in satisfying the needs of its users have gradually become more evident. First, the system has proved unable to meet the demands for new information that call for an increase in public entity accountability. Second, the system has not satisfied the demands for more transparency and quality in the preparation of information, nor has it been able to counteract its use as an instrument for political confrontation nor to prevent the inaccuracy with which the information is presented in the media.

Financial information must be given a wider scope to encourage greater accountability and to appropriately "communicate" –report, explain, and disclose– this information to its users. The gradual incorporation of the annual report into local governments' financial communication systems plays a central role in this process, given the importance of its content and purpose. In our view, this document may well become an essential resource for politicians and managers in order that accountability might be demonstrated, and its incorporation will become one of the dominant trends in local financial information disclosure in the coming years. To enable this to happen, advances must be made to normalise and harmonise the annual report, to strengthen the aspects that guarantee its usefulness: (a) rigorous and exhaustive content, (b) clear and appealing presentation, and (c) wide disclosure.

NOTES

[1] It is not the only institution that has invoked the notion of accountability to establish the objectives of governmental financial reporting. The importance of accountability is also evidenced in the pronouncements of the Australian Accounting Research Foundation (1990), the Canadian Institute of Chartered Accountants (1990), and the International Federation of Accountants (1991).

[2] A more in-depth discussion of the advantages of the correctn dissemination of financial information can be found in Angotti and Laurent (2000, pp. 14-16).

[3] The Spanish Local Administration provides a good example of this situation. Current accounting standards establish that a large number of statements and reports must be prepared and complemented with a series of annexes. A brief look to the documents prepared by any local government demonstrates the size and complexity of the General Account (*Cuenta General).* The *Plan General de Contabilidad,* which came into force in 1994, tried to simplify the accounting information to be provided by public entities, but this legal provision has yet to be adapted to local entities.

[4] It should not be forgotten that local public policies (and, consequently, the proposals included in the electoral programs) aim to increase the "welfare of the local community", and thus, appropriate indicators should be used to demonstrate accountability for welfare effects to the citizen.

[5] Nowadays, several local governments include information on costs and managerial results in their annual financial statements. For a survey of performance indicators in different countries see Poister (1999) and Guarini (2000).

[6] According to Statement nº 34, the minimum requirements for general purpose external financial reports are MD&A, basic financial statements (including government-wide financial statements, fund financial statements and notes to the financial statements), and required supplementary information.

[7] According to the GASB (1987, par. 7), special purpose financial reports are generally used to a) meet specific legal or contractual requirements, b) present financial statements using a basis of accounting that differs from generally accepted accounting principles, c) present financial information in prescribed formats, or d) report on specified accounts, or items taken from the general purpose financial statements.

[8] Sometimes, this procedure is explicitly supported by official institutions. This is the case in Belgium, where the *Agence Wallonne des Télécommunications* has elaborated a Vademecum for the construction of a municipal web site intended for citizens, which indicates that the site must contain "all the official information about the municipal services; for instance, in the case of financial services, a summary of the municipal budget and its financial statements".

[9] Both reports explicitly express a wish to offer the financial information in an easily understandable format. Thus, these documents are intended for the general public, and their preparation should clearly communicate the entity's "financial health" in an appealing format.

[10] In Australian local governments, the standards recommend that "the general purpose financial reports should form part of a overall report of the governing body. That report may usefully include commentary on the policies, objectives and achievements of the governing body" (AARF, 1993; par. 85). The annual report published by the city of Sydney graphically shows this type of information by means of a scheme that reports the objectives and goals pursued, and the results actually obtained.

[11] That phenomenon responds to the strong doctrinal current that postulates the use of the accounting reports as vehicle to demonstrate the ecological accountability of an organisation (Maunders and Burritt, 1991; Burritt and Welch, 1997, among others). The objective put forward by the authors of this article is

to reach a point where both public and private sector entities use their annual reports to reveal the effects of their activities on the environment.

[12] Any doubt about who the users of the abbreviated version of the annual report might be disappears if we take into account the terms used by local governments to refer to this document: popular report, citizen report, report to ratepayers.

[13] The annual reports prepared by various French cities include this information in the "périmètre d'intervention et participations", which is accompanied by an explanatory chart showing the links between the government and entities for which it is responsible.

[14] According to the GASB (1999), this part of the annual report constitutes the essential content of the MD&A.

[15] This work is the result of a study financed by the *Instituto de Estudios Fiscales* and carried by the following research group: José Luis Pablos and José Miguel Fernández (Coordinators), Isabel Brusca, Mª Belén Morala, Pilar Arbesú, and Ana Cárcaba.

[16] Politicians should not use financial information as propaganda to gain votes. Regardless of the dates in which the information is publicly presented, financial reports should only contain technical, neutral, and objective information.

[17] In the annual reports, local governments should reveal the environmental effects, both desirable and undesirable, resulting from their activities, as is already done in some industrial sectors. In order to demonstrate environmental or ecological accountability, the report should include descriptive information on issues as CO_2 emissions by entities linked to the government, the energy efficiency of the production processes, incentives for the introduction of alternative energies, etc.

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G. JAN VAN HELDEN
REMCO J. ADMIRAAL

EXPLORING THE BALANCING CONCEPT IN THE DESIGN OF A PERFORMANCE MEASUREMENT SYSTEM FOR WASTE WATER TREATMENT IN THE NETHERLANDS

1. INTRODUCTION

Water boards in the Netherlands recently completed a sector-wide performance measurement and evaluation project for waste water treatment. The project is supposed to achieve two goals. First, it should strengthen the accountability of water boards to their main stakeholders, such as taxpayers and governmental policy makers. Water boards are (partly) regional monopolies, and they are legally able to raise taxes for funding their activities. Therefore, they wish to show that they deliver value for money. Second, the project is supposed to identify relationships between various performance indicators, in order to provide information to enable individual water boards to improve their performance.

The project started in 1999 and was completed in the beginning of 2001. All Dutch water boards with waste water treatment plants participated in the project. Balanced Scorecards at two different levels were developed. The first one has to serve accountability purposes and entails a limited number of externally focused performance indicators. The second scorecard, which includes a large number of performance indicators related to various internal processes, can be used for learning and improvement. The two Balanced Scorecards are closely linked, in the sense that the former one contains a selection or aggregation of performance indicators of the latter one.

This paper focuses on the Balanced Scorecard (abbreviated to BSC) for external accountability. It will explore the balancing concept within this BSC. The original idea

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behind balancing points to a comprehensive performance measurement system, implying a broad rather than a financially focused set of performance indicators. However, emphasis has recently changed towards specifying cause-and-effect relationships between performance indicators, to be derived from a business model of the organization. The paper will address the question whether causal relationships or interdependencies between performance measures within the BSC can be expected. Moreover, statistical evidence for these relationships will be provided.

The structure of the paper is as follows. Section 2 will give background information on the waste water treatment task in the Netherlands, as well as on organizational aspects of the performance evaluation project. Section 3 will introduce the theoretical concepts for analysis of the project's outcomes. Section 4 will address the development of performance measurement systems. Section 5 elaborates on interrelationships between BSC perspectives and between key performance indicators. Finally, section 6 entails the conclusions of this project and indications for future research.

2. CONTEXTUAL BACKGROUNDS

A brief sketch of the project's context is useful for a proper understanding of its performance instruments and results. This section begins with a description of the waste water treatment task of Dutch water boards. Thereafter, some important organizational aspects of the waste water treatment performance project will be given.

2.1 Waste water treatment in the Netherlands

The main tasks of water boards in the Netherlands refer to water system management (water level control, including land draining) and surface water quality (predominantly waste water treatment). These tasks annually account for approx. 500 million Euros and 800 million Euros respectively. The paper deals exclusively with the waste water treatment task of water boards.

In 1970 the law on the Quality of Surface Waters (In Dutch: 'Wet Verontreiniging Oppervlaktewateren', abbreviated to WVO) was introduced. This law had to increase the surface water quality by giving instruments to regional and central government to regulate waste water flows into the surface waters and to improve the treatment of waste water. The law gave responsibilities for water quality to central and provincial government. Central government was made responsible for sea water quality and the water quality of the main rivers and lakes, whereas the responsibility of the provinces was directed to regional water quality. All provinces ultimately delegated their water quality tasks to the water boards.

In the year 2001 27 water boards are dealing with surface water quality in the Netherlands. The municipalities are responsible for the initial transport of the waste water mainly through their sewerage system. The waste water from households and industries is initially transported through the municipal sewerage systems, and then by the transport system of the water boards to their plants where it is treated to remove most of the nitrate, phosphate and other components. After treating the water to the required legal standards, the effluent is released into regional or national waters. Larger industries can choose whether to treat their own waste water or let the water boards do it. It has to be emphasized that in the Netherlands drinking water is supplied by separate public enterprises, owned by provinces and municipalities.

Each water board sets its own tax level, which has to be based on the annual full costs of the waste water treatment and other water quality tasks (in particular for regulation and treatment of polluted water soils). Water boards are not allowed to make profit, which means that a positive financial result in one year has to be used for additional investments or lower tax rates in another year.

The Dutch water boards have participated in comparative performance studies for several years. Most of these studies, however, have mainly concentrated on financial indicators. Moreover, these studies did not involve all Dutch water boards. In 1999 the Association of Dutch Water Boards initiated the performance evaluation project to be addressed in this paper. This project involves all Dutch water boards with waste water plants and it has a broader scope than just financial performance, e.g. tariffs and costs. The project should strengthen accountability (i.e. transparency) of the waste water treatment task and it also aims to develop an instrument for improvement of business processes that can be repeated regularly[1].

Benchmarking refers to information gathering in order to set performance targets which are realistic within the context of the external environment of a company and which lead to feasible best practice options for improvement (Camp, 1989, chapter 1). The current study on waste water treatment is therefore only a first step for benchmarking: it will provide data on the best performance, but it will not directly lead to recommendations regarding best practice operations. Furthermore, another project goal is relevant, in the sense that the project endeavours to contribute to accountability for a governmental sector as a whole.

As argued above, the water chain in the Netherlands encompasses three links: the collection of waste water, waste water treatment and the purification and delivery of drinking water. The drinking water companies, which are responsible for the latter task, conducted their first benchmarking study in 1997 (Andersen Consulting and VEWIN, 1997), which has been repeated in 2001. Recently, a feasibility study on comparative sewerage performance measurement was initiated. Consequently, this opens up a perspective on comparative performance measurement and evaluation of all links of the Dutch water chain.

2.2 Organization of the project

A project committee and a steering committee were instigated for the project. Several external members were involved in these committees, both to internalize external knowledge and to give an impulse to reach the goal of improving the transparency of waste water treatment. The project committee consisted of technical and financial specialists. The steering committee consisted of managers and members of the executive committees of water boards. In order to create a linking pin, the chairman of the project committee was also the secretary of the steering committee. Before the project started the Association of Water Boards decided to appoint an external chairman for the steering committee. Furthermore, there were three external members, one from central government (responsible for the control of local taxes), one from the private sector (from the Chambers of Commerce) and a representative of the municipalities. The first author of this paper was chairman of the steering committee and the second author was both secretary of the steering committee and chairman of the project committee.

In 1999 consultancy firms Arthur Andersen Business Consulting and Vertis were selected to implement the project. Arthur Andersen/Vertis proposed a concept for the project in which emphasis was put on four aspects. First, the development of methods was based on the principle of co-creation, in the sense that potential users of the results were invited to participate in teams that elaborated on the indicators needed in this benchmark. The results were discussed and tested in workshops, interviews and questionnaires. Second, the relevance, availability, reliability and validity of data as well as the costs of data gathering were closely tested to assure a maintainable and repeatable benchmark study. Third, the method required a broad scope, in order to enable a comparison with foreign and privately owned waste water treatment plants in the future. Finally, communication was considered to be a key issue, because some prior studies partly failed as a result of a lack of commitment due to poor communication. For this study a separate newsletter and a Website were launched.

During the realisation of the project members of the project committee were closely involved in the preparation of the performance evaluation method, the organization of the pilot project (in which the method was tested) and the draft of the final reports. The execution of the project was divided into two stages: the first stage included a restricted number of water boards (in order to test the data collection process, and to delete apparently redundant indicators) and in the second stage the remaining water boards were involved.

The project committee focused on the project as a vehicle to improve business processes and aimed at searching for detailed best practices. The focus of steering committee was mainly directed to the achievement of transparency of the waste water treatment task of the water boards.

3. THEORETICAL CONCEPT AND RESEARCH METHODS

The balancing concept in performance measurement systems is the main theoretical issue to be addressed in this paper. A critical appraisal of this concept will identify the research questions. Finally, the research methods, which are used, will be clarified.

3.1 The balancing concept

The exclusive usage of financial performance measures has already been criticized in management accounting literature for a long time (see for instance Johnson and Kaplan, 1987, pp. 195-204, 254-256; Emmanual, et al., 1990, pp. 232-238). Therefore, multidimensional performance measurement systems, in which both financial and non-financial performance indicators are included, are part of the current body of knowledge in management accounting.

Different proposals for such systems have been developed during the last decade, such as the Balanced Scorecard (BSC), the performance pyramid (Lynch and Cross, 1995), the Tableau de Bord (Epstein and Manzoni, 1997) and the EFQM model (Dijkstra, 1997; Seghezzi, 2000)[2]. The BSC is the most well-known concept (Ittner and Larcker, 1998) which is sufficiently flexible to take account of firm specific or branch specific considerations. Hence, the project focused on this concept, which was developed by Kaplan and Norton (1992). The BSC contains four performance measurement perspectives: the customer, the internal, the innovation and learning, and the financial perspective.

Originally, Kaplan and Norton (1992, p. 73) argue that balancing requires a comprehensive set of performance measures, rather than a focus on financial performance indicators. This is supposed to be a safeguard against suboptimization: the balanced scorecard lets the senior managers see "whether improvements in one area may have been achieved at the expense of another." They also emphasize that (p. 97) "the challenge is to learn how to make.....explicit linkages between operations and finance." Recently, Kaplan and Norton (1996a, p. 84) elaborate on this linkage concept: "A business strategy can be viewed as a set of hypotheses about cause-and-effect relationships." Moreover, Kaplan and Norton (1996b, pp. 149-150) put more emphasis on the integration of performance measures, which has to be developed from a theory of the business (see also Eccles, 1991; Atkinson, et al., 1997, pp. 28-29; Ittner and Larcker, 1998, p. 224). In this respect, causal relationships between performance drivers (leading indicators) and outcomes (lagging indicators) should be based on an understanding of the organization's business model.

The originally established concept of balancing refers to an explicit goal of the Dutch waste water treatment performance project, because it aims to achieve a broader scope than just financial aspects, such as tariffs and costs. The project also supposes to include the more recently established concept of balancing. Firstly, due to the value-for-money idea, which implies interrelationships between financial and process issues. And secondly, because the project aims to identify relationships between various performance indicators, in order to provide information to individual water boards for improving their performance.

Nørreklit (2000) has criticized Kaplan and Norton's claim that the BSC contains causal relationships between performance indicators. Apart from the fact that the BSC ignores possible time lags between performance indicators – for instance between indicators from the learning and internal perspective respectively – Nørreklit argues that Kaplan and Norton's causality claim is invalid. According to Kaplan and Norton (1996b, p. 4), "....A scorecard should contain outcome measures and performance drivers of those outcomes, linked together in cause and effect relationships...". This implies, for example, that:

- An increase in product quality (that can be part of the internal perspective) will cause a higher rate of customer satisfaction (which belongs to the customer perspective);
- And that, in turn, a higher rate of customer satisfaction causes higher profits (belonging to the financial perspective).

Nørreklit (2000, pp. 69-75) clarifies that a causal relationship between two variables can only exist if both variables are logically independent, otherwise such a relationship can only be considered to be logically true. For example, if a satisfied customer is defined as a customer who causes low costs to the company and is willing to pay a high price, this definition logically implies profitability, and hence a relationship between customer satisfaction and profitability is a logically true instead of a causal relationship. However, if customer satisfaction is measured by means of customer valuation of product characteristics, then customer satisfaction and profits can be causally related.

In this respect Nørreklit criticizes Kaplan and Norton for two reasons. First, these authors sometimes use indicator definitions that can only refer to logically true, rather than causal relationships. And second, that – whenever there may be a causal relationship between two variables – the evidence for causality is only poor. A reciprocal direction of causality may also be possible, or at least can not be excluded, for instance improved product quality might increase profitability, but a high profitability may also enable product quality improvements. Moreover, a causal effect between two variables may only occur if the effect of a third variable is taken into account. For example, a higher customer satisfaction will lead to higher profits, subject to the condition that delivery costs will not rise.

Nørreklit (2000, pp. 75-77) concludes that causal relationships between performance measures within the BSC are not likely, and instead only interdepencies may be expected. This implies that relationships between performance indicators of different perspectives become more ambiguous and complex. Based on Nørreklit's arguments, we will try to answer the following research questions:

- Which performance domains can be distinguished in the waste water treatment project;

- Whether relationships between these performance domains (or indicators within these domains) refer to interdepencies or logically true relationships;
- To what extent statistical evidence about the existence of these relationships can be given.

These questions are important within the context of the project, because water boards are faced by central governments' pressure to be accountable for delivering value for money, which requires information concerning the relationships between financial and non-financial issues of waste water treatment. Moreover, water boards want to improve their performance. Incentives for improvement may come from best practice cases, but also from the identification of relationships between performance indicators in the BSC.

3.2 Research methods

The framework, developed above, requires an in-depth description and analysis of the waste water treatment performance project. Issues regarding the performance measurement system – both the indicators to be used and the domains of interest for different stakeholder – will be addressed in section 4. Section 5 will elaborate on the interrelationships between the performance domains within the BSC.

Our investigations will use official documents of the project, such as reports on the performance measurement method, the performance indicators to be used, the performance indicator values and the evaluation of the entire project. Furthermore, we investigated the archives of both the steering committee and the project committee, in order to get access to the deliberations that led to certain decisions. Finally, statistical analysis of relationships between performance indicator values completed the research for this paper.

Because of their involvement in the steering and project committee, the authors actively contributed to the project reports. In this respect, the paper is the result of action research (Kaplan, 1998). However, the authors took a more distant position to the two other data sources, the project archives and the project results on performance indicators.

4. DESIGN OF PERFORMANCE MEASUREMENT SYSTEMS

This section addresses the design of the performance measurement systems within the waste water treatment project. First, we will show what performance measurement perspectives were used and how they are related to the Balanced Scorecard concept. This information is necessary for a proper understanding of interrelationships between performance domains or indicators. Thereafter, this section will elaborate on the way in which the performance indicators for external accountability were selected during the course of the project.

4.1 Selection of perspectives

As argued before, the BSC contains four performance measurement perspectives: the customer, the internal, the innovation and learning, and the financial perspective (Kaplan and Norton, 1992, p. 72). The BSC concept was primarily developed for business organizations. In order to use this concept in a governmental context, at least two questions have to be answered: do we have to change the contents of some BSC perspectives and do we need more than the four BSC perspectives? In answering these questions, we will refer to the specific characteristics of the waste water treatment task of Dutch water boards.

The customer perspective is crucial to business organizations because of their competitive environment: they will have to compete with other firms in order to satisfy customer needs. Consequently, performance measures like market share and customer satisfaction are needed. Water boards are (partly) regional monopolies and they are legally enabled to raise taxes for funding their activities. Moreover, they will also have to deal with other stakeholders than tax payers, such as central and provincial government because of their legislative powers towards water boards. Therefore, the customer perspective will be broadened to a diverse set of stakeholders, such as citizens, business firms and governmental bodies.

The internal perspective refers to the internal processes of organizations. This perspective is important both for business organizations and governmental bodies, like water boards. The waste water treatment task of water boards can be monitored by measures such as the efficiency or effectiveness of waste water treatment plants.

The innovative perspective is also appropriate for both business organizations and governmental bodies. With respect to waste water treatment the degree to which water boards take innovative initiatives could be measured.

The financial perspective generally plays another role in governmental bodies than in business organizations. The latter organizations will have to create financial value that can be measured by cash flow or profit. On the contrary, governmental bodies are often largely dependent on governmental funding. Therefore, performance indicators in the financial perspective might be shaped as budget restrictions, in the sense of the extent to which these organizations meet the externally established budget (Van Helden and Kamminga, 1996, p. 410). Water boards, however, are relatively independent from central or provincial government funding, as they can raise taxes for funding their activities. So, they are supposed to deliver services, e.g. waste water treatment, in which all costs are covered by revenues from tariffs. However, they are not allowed to make a profit. This implies that the tariff per unit of waste water treatment is an important performance indicator in the financial perspective of water boards.

One important issue of waste water treatment cannot be adequately addressed within the above mentioned perspectives. This issue relates to the way in which water boards deal with environmental affairs, such as the extent to which they eliminate phosphates and nitrogen above legal standards. Hence, an environmental perspective is included in the waste water treatment BSC.

Table 1 summarizes the relationships between the perspectives in the commonly used BSC and those in the BSC that was developed for the Dutch waste water treatment project.

Table 1. Relationships between the Kaplan and Norton perspectives and the perspectives of the Dutch waste water treatment project

Kaplan and Norton perspectives in the BSC	*Perspectives in the BSC of the waste water treatment project*	*Example of a typical performance indicator within each of the perspectives in the BSC of the waste water treatment project*
Customer	Stakeholders	Tax payer satisfaction (to be included in the next benchmarking study)
Internal	Operating performance	Efficiency of waste water treatment works
Innovative	Innovative	Score on innovative capability
Financial	Financial	Tariff per unit of waste water treatment
	Environmental	Elimination rate of phosphates above legal standards

4.2 Selection of performance indicators

The consultants selected the indicators in the BSC in close co-operation with the potential users and both committees. This development process started with the formulation of goals related to the perspectives in de BSC. Thereafter, key success factors were formulated which where translated into various performance indicators. Finally, there was a search for variables that might explain differences in performance indicator values. This development process resulted in a huge set of indicators. The great challenge was to reduce this set to a manageable scope. Selection was based on the criteria set out at the beginning of the project e.g. indicators had to be clearly defined, relevant to goals, unambiguous in their interpretation, insensible for manipulation and with relatively low costs of data gathering. The steering committee was not able to specify appropriate indicators for the stakeholder perspective and hence was forced to disregard this perspective in the current study. This committee recommended the water boards to introduce indicators on tax payer satisfaction and employee satisfaction for their next benchmarking study.

During the initial stages of the project two levels of performance measurement were distinguished. These levels are interrelated and therefore result in a performance pyramid. The lowest level is the BSC-INDIVIDUAL, which contains a large number of performance indicators, in order to enable individual water boards to compare their own performance with those of all water boards. The highest level is the BSC-GROUP in which all water boards are compared on a small number of the most important performance indicators. This comparison was supposed to be shaped by means of league tables for each of the performance perspectives.

The target group for BSC-INDIVIDUAL is the executive committee and the management of each of the water boards. This information may be used for learning and improvement. The target group of BSC-GROUP is supposed to consist of various subgroups:

- The water board's executive and general committee;
- The citizens and business firms within the jurisdiction of the water board, including the press as information channel for these stakeholders;
- The other governmental stakeholders with legislative powers towards waste water treatment, in particular central and provincial government.

These stakeholders are considered to be mainly interested in a more or less general insight into the value for money provided by an individual water board or by all water boards.

As was argued in section 1, this paper only deals with the BSC-GROUP. During the process of selecting performance indicators for this BSC, the steering committee reduced the number of indicators proposed by the project committee from twenty to eleven. Moreover, this committee selected four of these eleven indicators as key indicators. These four key indicators coincide with the issues that resulted from the interviews with the (mainly external) stakeholders. It goes beyond the scope of this paper to clarify the selection process in more detail. Table 2 shows the results of this process.

5. BALANCED PERFORMANCE?

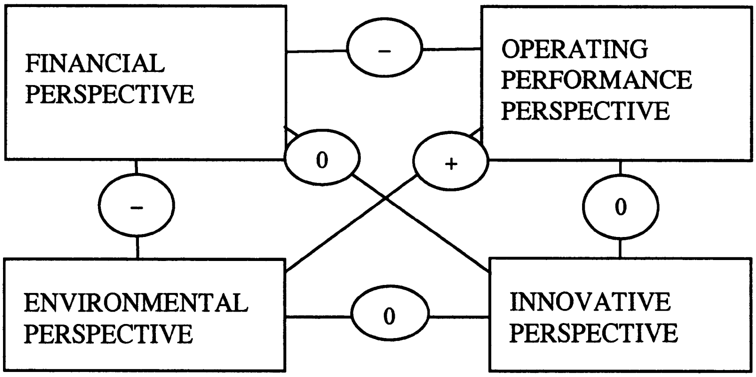
This section will provide statistical evidence on the interrelationships between perspective values of the BSC-GROUP, as well as between KEY INDICATORS values. First, the business model, that identifies possible relationships between performance indicators, will be introduced. Thereafter, the outcomes of the statistical tests will be provided. Two water boards could only provide information on financial indicators, due to their involvement in amalgamations. Therefore, the results regard the other 23 water boards; together they cover about 94% of the total waste water treatment task in the Netherlands.

Table 2. Results of the selection process of indicators in the top of the performance pyramid

Perspective	Indicators proposed by the project committee (BSC-GROUP)	Indicators selected by the steering committee (BSC-GROUP)	KEY INDICATORS selected by the steering committee
Financial	Tariff per unit of waste water treatment	Tariff per unit of waste water treatment	Tariff per unit of waste water treatment
	Cost per unit of waste water treatment	Cost per unit of waste water treatment	Cost per unit of waste water treatment
	Total costs of transport of waste water	-	-
	Total costs of waste water treatment	-	
	Total costs of sludge treatment	-	-
	Total costs and revenues of waste water treatment for third parties	-	-
Operating perfor-mance	Suitability of waste water transport capacity	Suitability of waste water transport capacity	-
	Suitability of waste water treatment capacity	Suitability of waste water treatment capacity	-
	Elimination rate according to legal standards	-	-
	Elimination rate of phosphates	-	-
	Elimination rate of nitrogen	-	-
	-	Effectiveness of waste water treatment	Effectiveness of waste water treatment
Environ-mental	Elimination rate of phosphates above legal standards	Elimination rate of phosphates above legal standards	-
	Elimination rate of nitrogen above legal standards	Elimination rate of nitrogen above legal standards	-
	Score on environmental operating	Score on environmental operating	Score on environmental operating
Innovative	Number of collaboration projects in the chain	Number of collaboration projects in the chain	-
	Number of new services	Number of new services	-
	Project proposals for Water research centre STOWA	-	
	-	External score on innovative capability	-
Stakehol-ders	Complaints of residents close to treatment plants	-	-
	Number of employees satisfaction surveys	-	-
	Take over rate of waste water treatment from and to water boards by business firms	Take over rate of waste water treatment from and to water boards by business firms	Was deleted in BSC-GROUP

5.1 The business model

Figure 1 shows whether the business model about waste water treatment – which was developed by the steering committee, the project committee and the project's consultants – expects the existence of relationships between the four performance perspectives. And, if so, the direction, in the sense of a positive or negative sign, of these relationships is also indicated. The business model only specifies associations (or correlations) between performance perspectives. Which perspective is the cause and which the effect in these relationships was not explicitly identified.



Legends: A line between two perspectives denotes the possible existence of a relationship between those perspectives: + or – refer to a positive or negative relationship respectively, and 0 means that there are no arguments for a relationship.

Figure 1. The business model of waste water treatment

The business model will be briefly explained.

1. The most important relationship refers to the value-for-money concept. A high value on the operating performance perspective (which implies a good service level) is expected to coincide with a low value on the financial perspective (indicating high cost per unit of waste water treatment). Analogously, a low value on the first perspective might also fit with a high value on the second one. Consequently, these two perspectives are negatively related.
2. The relationship between the financial perspective and the environmental perspective is also expected to be negative (the higher the elimination rate of phosphates and nitrogen, the larger the cost of waste water treatment).
3. The environmental perspective is expected to be positively related to the operating performance perspective. Because both perspectives partly refer to similar indicators, the relationship is mainly logical. This can be explained as follows. The effectiveness of waste water treatment in the operating performance perspective includes indicators

on elimination rates of phosphates and nitrogen, whereas the environmental perspective contains these elimination rates as separate indicators, but now defined as the degree to which actual values exceed legal standards.

Relationships 1 and 2 both refer to correlations between concepts that are logically independent. Hence, rather than logical, these performance domains can be interrelated. A cause-and-effect relationship could also exist, but a conclusive statement is impossible in this respect, due to lack of evidence about causality.

There are no clearly specified expectations about the following three relationships [3]:

- Between the operating performance perspective and the innovative perspective (a positive relationship is possible if innovations contribute to more efficiency and effectiveness, but a negative relationship might refer to risky investments in innovations which do not lead to more efficiency or effectiveness, at least in the short run);
- Between the financial perspective and the innovative perspective (for example more new services or new projects might harm financial results, but could also induce a better financial performance);
- Between the environmental perspective and the innovative perspective (the indicators in both perspectives refer to different issues of waste water treatment).

5.2 Relationships between performance perspectives

Before the empirical results are shown, we will first justify the way in which the rank values of the water boards for each of the perspectives were calculated.

The rank values of the water boards in each of the perspectives are calculated according to the following procedure. A perspective contains two or more performance indicators. First, for each indicator the registered values of the water boards are transformed into rank values, varying from 1 (the best) to 23 (the worst). Second, for each water board the average rank value is calculated by equally weighing the rank values of the indicators. Third, if two or more water boards receive an equal average rank value, this value is corrected in such a way that the value of the next best and the next worst water board are on equal distance from this value. For example, two water boards A and B have the same rank value on the financial perspective. They share the values 4 and 5 in the rank order and therefore they receive both a rank value of 4.5. Then the distance to the next best (with value 3) and next worst (with value 6) is the same. This procedure is repeated for each of the perspectives. The implication of this calculation procedure is that the average value of the rank values in each perspective is 12 (= (1 + 23)/2). An additional procedure was needed for three rank values of the operating performance perspective because three water boards could not deliver data on the indicators belonging to this perspective. Their rank values were estimated by looking at other water boards with comparable rank values in the three other perspectives. Then the rank value of the operating performance perspective of this comparable water board was used as an estimation of the rank value of the water board in question.

Table 3 shows the rank correlation coefficients between the four perspectives. Although a negative relationship between the financial and operating performance perspective exists, this relationship is not statistically significant. This implies that the value-for-money expectation cannot be confirmed. The expectation concerning the negative association between the financial and the environmental perspective is neither corroborated. The data in table 3 do confirm the positive relationship between the environmental and operating performance. However, as explained, above, the nature of this relationship is mainly logical. Finally, the data do neither show a positive nor a negative relationship, which is statistically significant, in the three occasions were a clear expectation about a relationship between perspectives is lacking.

Table 3. Rank order correlation coefficients between BSC perspectives (Spearman's Rho)

	Financial	Operating Performance	Environmental	Innovative
Financial	1.00			
Operating Performance	-0.184	1.00		
Environmental	0.060	0.425*	1.00	
Innovative	0.167	-0.126	-0.283	1.00

** the relationship is statistically significant at a 5% level (in the case of the relationship between the environmental and operating performance perspective Kendall's Tau is 0.317).*

5.3 Relationships between key performance indicator values

The previous subsection examined the relationships between the rank values of the four BSC perspectives. We will now investigate whether relationships between the key indicators (see table 2) do exist. The following symbols will be used for the four key indicators:

- TARIFF = tariff per unit of waste water treatment;
- COST = cost per unit of waste water treatment;
- EFFECT = effectiveness of waste water treatment;
- ENVIRON = score on environmental operating.

Table 4 shows the correlation coefficients between the four key variables. The relationship between TARIFF and COST is the only statistically significant relationship. However, this refers to a mainly logical relationship. There is no evidence for a value-for-money relationship, because the correlation coefficients between either TARIFF or COST on the one hand and EFFECT on the other are statistically insignificant. Contrary to table 3, the relationship between EFFECT and ENVIRON is statistically insignificant.

This may be due to the fact that EFFECT and ENVIRON in table 4 refer to logically independent variables, whereas the relationship between Operating performance and Environmental performance in table 3 is mainly a logically true relationship.

Table 4. Pearson correlation coefficients between key indicators in the BSC

	TARIFF	COST	EFFECT	ENVIRON
TARIFF	1.00			
COST	0.827*	1.00		
EFFECT	-0.025	0.025	1.00	
ENVIRON	-0.237	-0.205	-0.148	1.00

* = *The relationship is statistically significant at a 1% level.*

Because neither table 3 nor table 4 confirm a value-for-money relationship, we analysed the relationships between more desaggregated variables. This analysis shows that there is some evidence for a value-for-money-relationship at this more desaggregated level, for example between the capital costs and a measure for water quality and also between the remaining costs and the obligation rate for acceptance of waste water. It has to be emphasized that the statistical significance of some of these relationships is only poor. Moreover, an economies of scale effect (measured by the total number of waste water units) on the cost and tariff of waste water treatment has been found. Water boards with a high tariff seem to be faced with pressure to spend a small amount of money on water quality tasks not directly belonging to the waste water treatment task.

6. CONCLUSIONS AND RESEARCH SUGGESTIONS

This paper pertained to the top of the information pyramid of waste water treatment in the Netherlands. The BSC of the Dutch waste water treatment project contains four performance measurement perspectives: the financial, the operating performance (internal), the innovation and the environmental perspective (an external perspective will be developed in the future).

6.1. Conclusions

Referring to the research questions in section 3, we can draw the following conclusions. There is no empirical evidence for the balancing concept, in the sense of interrelated performance perspectives[4]. Whenever relationships between performance perspectives (or between indicators within these perspectives) exist, they mainly refer to logically true relationships. Obvious relationships between, for example, financial and operational key indicators, or between rank values of the perspectives in question turned out to be statistically insignificant. This absence of interrelated performance indicators can be explained by two reasons. First, relationships between highly aggregated variables are clouded by complex patterns of relationships between the underlying, more specific indicators. Second, statistical evidence was based on a cross section of a relatively small amount (23) of water boards. It may be more relevant to look at patterns in the course of time within individual water boards. Also time lags in the relationships between performance indicators can be taken into account then. In any case, the estimation results clearly show that – in the absence of relationships between highly aggregated variables – there was some evidence for relationships between more specific indicators at a less aggregated level.

6.2 Directions for future research

A longitudinal study regarding the application (and adaptation) of performance measures at the various levels of the performance pyramid might throw light on the way in which performance information will be used for leaning and improvement. As announced in section 2.1, the comparative analysis of waste water treatment performance will be repeated regularly by the Dutch water boards.

Another perspective for future research seems to be promising too. Opposite to the BSC-GROUP, which only entails eleven performance indicators, the BSC-INDIVIDUAL encompasses more than seventy performance indicators, which are specified at a more detailed level. The latter BSC may be an interesting concept for investigating both interrelationships between performance indicators, and relationships between indicators at different levels of the performance hierarchy.

NOTES

[1] Interorganizational comparison of performance indicators can be regarded as a 'next step' in the development of more businesslike instruments, particularly performance-oriented budgeting systems in Dutch water boards (in Dutch: 'Beleids- en Beheerproces bij waterschappen', abbreviated to BBP; Van Heemst and Dekking (1995)). BBP is similar to the policy and management instruments project (PMI) project for Dutch municipalities (Van Helden, 1998). Moreover, these developments belong to reforms in the public sector, which also took place in other Western countries and which are denoted as New Public Management (Hood, 1995; Pollitt and Bouckaert, 2000, chapter 4).

[2] An extensive example of a broad spectrum of non-financial performance indicators is given by Ezzamel,1992, pp. 118-119.

[3] In each case the two variables are logically independent, and hence, these variables may be interdependent.

[4] Ittner and Larcker's (1998, pp. 218-220) review of studies concerning interrelationships between financial and non-financial performance indicators produced mixed results.

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SHEILA ELWOOD

TOWARDS A CONTINGENCY THEORY FOR HOSPITAL COST ACCOUNTING SYSTEMS: A COMPARISON OF THE UK AND NEW ZEALAND

1. INTRODUCTION

In the early 1990s both the UK and New Zealand embarked on an internal market approach to allocating healthcare financial resources. However, the approaches adopted in both costing and pricing healthcare have differed markedly. The study uses event analysis and case studies to identify differences between the two countries in the development of case-mix costing and the pricing/ funding mechanism. A number of forces at work at the macro level are similar. The UK has seen the introduction of a quasi market within the health service in the early 1990s followed by a shift to a more co-operative approach since 1997. However, the purchaser-provider split has been maintained. New Zealand has undergone similar changes in the healthcare sector. The responsibilities of the formerly vertically integrated Area Health Boards were redefined in terms of purchasers and providers of healthcare in the early 1990s but were modified after substantial health service deficits arose, and are currently implementing a reorganization with elected District Health Boards (DHBs).

Within hospitals, cost systems have been found to serve a number of purposes. In the UK in the early 1990s heavy investment was made in case-mix systems. However, case-mix costing systems were not used for price setting and did not flourish. On the other hand, there are instances of sophisticated case-mix costing systems being effective in New Zealand.

The accounting literature on whether accounting systems make a difference and the extent to which they influence and are influenced by their external environment is inconclusive. The research study seeks to inform this debate; in particular it questions whether hospital cost accounting systems are influenced by observable national differences in the health care funding mechanisms rather than following an evolutionary path.

The paper is in three sections. The first part provides background material on healthcare spending and policy in the UK and New Zealand over the last decade and draws out similarities and differences between the two countries. The second section considers cost systems in a health care setting and introduces contingency theory and other theoretical approaches for analysing the development of management

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 265-281.

accounting systems. The third section identifies the research approach including the contingency model to be investigated.

2. BACKGROUND: UK AND NEW ZEALAND HEALTH CARE

A number of forces at work at the macro level are similar. Table 1 compares the proportion of publicly funded health expenditure.

Table 1: Publicly funded as a proportion of total health expenditure

	1988	1998
Australia	68.4	69.3
Austria	75.6	72.4
Belguim	89.1	87.7
Canada	75	69.8
Czech Republic	n/a	92.1
Denmark	84.5	83.8
Finland	79.4	75.5
France	74.7	74.4
Germany	77.2	76.4
Greece	61.9	57.5
Hungary	n/a	71.9
Iceland	87.1	84.7
Ireland	71.3	78.4
Italy	77.9	69.4
Japan	75.2	78.4
Korea	37.6	47.3
Luxembourg	92.9	92
Mexico	n/a	57.3
Netherlands	72.6	72.9
New Zealand	85.6	77.1
Norway	85.3	82.1
Poland	N/A	82.1
Portugal	53.7	64.6
Spain	79.2	76.1
Sweden	89.4	83
Switzerland	66.6	70.3
Turkey	51.2	78
United Kingdom	84.2	84.9
United States	40.4	46.7
Mean (unweighted)	73.4	74.4

Source 1988-97OECD 1999. 1999 OECD provisional data

In 1988 the healthcare systems in the UK and New Zealand could be considered to be broadly comparable with regard to the proportion of healthcare expenditure funded from the public purse. Overall in the OECD, public health expenditure accounts for about three-quarters of total health expenditure. In 1988 the proportion of publicly funded health expenditure was 84% and 86% for UK and New Zealand respectively. However, by 1998, the proportion publicly funded had fallen to 77% in New Zealand but in the UK it had increased slightly to just under 85%, Table 1. Private sources of funding are household out-of-pocket expenditure, health insurance and not-for-profit organisations. In New Zealand, out-of-pocket expenditure by private households is the largest component of private sector funding, contributing around 15.9% of total health expenditure in 1998/99, while health insurance and not-for-profit organisations contribute 6.2% and 0.4% respectively (Ministry of Health, 2000). In the UK, out-of-pocket expenditure by private individuals account for 8.4% (largely pharmaceuticals) in addition to National Health Service (NHS) user charges of 1.6%; 4% is contributed through medical insurance (half of which is company paid) and 1% is through charities (Keen, 2000).

On the other hand, both countries spent a similar amount per head of population on health care in 1998. Per capita expenditure in US$ is shown in Table 2.

Table 2: Health expenditure (US$) for OECD countries 1998

		Health Expenditure		
	GDP per capita	% of GDP	US$ per capita	Rank
Australia	23518	8.7	2040	10
Austria	24140	8.3	2000	12
Belguim	24249	7.6	1850	13
Canada	24292	9.3	2250	5
Czech Republic	13178	7.2	950	24
Denmark	26329	8	2100	8
Finland	21440	7.4	1600	17
France	22098	9.6	2120	7
Germany	22739	10.6	2400	4
Greece	14570	8.7	1270	21
Hungary	10453	6.4	665	26
Iceland	26530	8.3	2190	6
Ireland	22822	6.1	1390	20
Italy	21797	7.6	1660	16
Japan	23998	7.4	1780	15
Korea	13537	6.9	930	25
Luxembourg	34969	7	2440	3
Mexico	7932	4.7	365	28
Netherlands	23565	8.6	2030	11
New Zealand	17857	8	1440	19
Norway	27807	7.5	2090	9
Poland	7938	5.4	430	27

Table 2: Health expenditure (US$) for OECD countries 1998 (continued)

		Health Expenditure		
	GDP per capita	% of GDP	US$ per capita	Rank
Portugal	15324	8	1230	23
Spain	16666	7.8	1240	22
Sweden	21117	8.6	1820	14
Switzerland	26774	10.2	2740	2
Turkey	6273	3.5	220	29
United Kingdom	21117	6.9	1450	18
United States	30579	14	4270	1
Mean (unweighted)		7.9	1689	

Source 1988-97OECD 1999. 1999 OECD provisional data

In 1998, the USA had the highest per capita health expenditure of the OECD countries. New Zealand ranked 19th, after the UK but before Ireland. Whilst the UK has a higher GDP per head, the proportion spent on healthcare is considerably less, under 7% compared with 8% in New Zealand. The UK government has recently made a commitment to increase healthcare spending to the European average. Healthcare spending as a proportion of GDP is frequently used in international comparisons, but expenditure has both price and volume components –a higher level of spending can reflect a higher price rather than a higher volume of healthcare services.

In the early 1990s both countries embarked on similar internal market reforms of their national healthcare systems.

2.1. Healthcare Reforms: UK

The UK has seen the introduction of a quasi market within the health service in the early 1990s followed by a shift to a more co-operative approach since 1997. However, the purchaser-provider split has largely been maintained.

The NHS Internal Market was introduced in the 1989 White Paper, Working for Patients (DoH, 1989a). In the internal market, district health authorities (DHAs) contracted with hospitals to provide specified services in return for agreed funding, Figure 1. To facilitate competition between hospitals, the government introduced a number of self-governing trusts (Department of Health, 1989b). By April 1994, 95% of hospital and community health services were provided by trusts (Robinson and Le Grand 1994). Although part of the NHS, these hospitals are free from direct control by health authorities and operate as self-standing business units. Trust hospitals (initially directly managed hospitals) under the internal market earn their revenue according to the services they supply. Previously, the national NHS budget was allocated to regional health authorities which then allocated funds to district health authorities which in turn allocated a global budget to the individual hospitals/ units they managed. Large General Practitioner (GP) practices were given the opportunity to become budget holders to purchase selected hospital services (DoH,1989c). Similarly to DHA purchasers, the GP fundholder contracts with providers of healthcare for their services on behalf of the practice's patients. GP fundholders (GPFHs) grew rapidly and in 1993/94 covered one in four of the population.

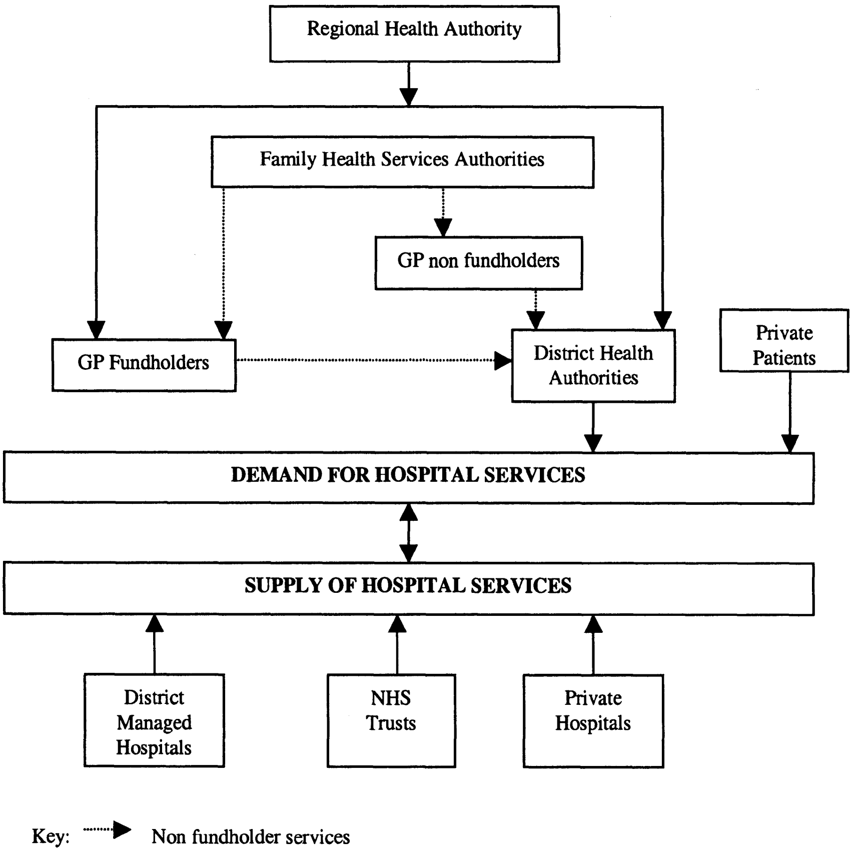

Figure 1: The NHS Internal Market.
Flow of Funds and Services 1991-1996.

At the commencement of the internal market the Department of Health specified pricing principles which required cost-based pricing i.e. full cost pricing including a return on capital (NHSME, 1990). These prices were intended to provide signals to healthcare purchasers to enable them to make efficient purchasing decisions.

> "Each DHA's duty will be to buy the best service it can from its own hospitals, from other authorities' hospitals, from self-governing hospitals or from the private health sector." Department of Health (1989a) paragraph 4.23

Contract funding brought about an effective separation of health authority functions: the responsibility for ensuring that the health needs of the population are met (i.e. the commissioning role) and the management of supply. Hospitals were encouraged to invest in new management accounting systems.

> "Hospitals need to keep their costs, including capital and other overheads, within the income they earn from contracts, and will accordingly need to aim for realistic pricing policies...The development of the contract system will require improved management information both for pricing and for control (including monitoring performance as well as financial control)." Department of Health (1989a) para 2.15.

The earlier resource management initiative (RMI) was extended to all acute hospitals and heavy investment in case-mix information systems was made.

In 1996 Regional Health Authorities were abolished (but regional offices of the NHS Executive were set up) and Family Health Service Authorities were merged with the District Health Authorities subsequently referred to simply as health authorities. The GP fundholding scheme ceased in 1998.

When the Labour Government was elected in May 1997, an end to the 'divisive' internal market was promised. The Government's proposals for the NHS were outlined in a White Paper issued at the end of 1997 -*The New NHS: Modern-Dependable.* The main proposals have been embodied in the Health Act 1999. The new arrangements consist of health authorities; Primary Care Groups and NHS Trusts.

- The health authorities' main function relates to assessing health need and determining the range and location of health services. They are also responsible for the management of local targets and standards and the development of Primary Care Groups (PCGs).
- PCGs are led by GPs and typically cover 100,000 population. PCGs commission and monitor health services; develop primary care and integrate primary and community services. Both health authorites and subsequently PCGs are funded according to population. PCGs evolve from an advisory position to the health authority to free-standing Primary Care Trusts that commissioning secondary care and providing community health services
- NHS Trusts are given a right to participate in strategy and planning quality and efficiency standards explicit in local agreements. Service and Financial Frameworks (SaFFs) that embrace health plans and targets replace the previous annual contracting process.

Specific responsibilities are underpinned by a national performance and quality framework together with a strengthened clinical governance process (DoH 1998a). The NHS Plan (DoH, 2000) emphasises the use of performance targets, for example, financial incentives are to be provided through a Performance Fund.

2.2. Healthcare Reforms: New Zealand

New Zealand has undergone similar changes in the healthcare sector. The 1938 Social Security Act created a comprehensive state health service with a commitment to universal access to healthcare for all citizens. In 1983 the Area Health Boards Act introduced structural change aimed at decentralising public health activities away from the Department of Health to regional agencies: 27 hospital boards were replaced with 14 Area Health Boards. The 1983 Act also introduced population based funding formula (a method of resource allocation introduced in England in 1977). This method of allocation was seen as the first serious attempt to cap hospital budgets (Lowe and Doolin, 1999).

In 1986 the Health Benefits Review recommended the creation of Regional Health Authorities to identify health needs but that these needs should be met by public, private or voluntary agencies. Each regional health authority would contract for health services on the basis of quality and value for money.

> "Under our proposal are health boards would become more like the boards of public companies. They would be able to concentrate on running efficient services helped greatly by a payment system which would give them an objective value of the services they provide. These prices would drive signals through the system, causing rapid improvements in resource use and clinical practice." Gibbs et al 1988 p28

Although at the time these ideas (reminiscent of Enthoven's *Reflections on the NHS*, 1985) were rejected, they were echoed in later reforms. By the end of the 1980s responsibilities of the formerly vertically integrated Area Health Boards were redefined in terms of purchasers and providers of healthcare (Blank, 1994). Four regional health authorities were created to act as purchasers of healthcare from public or private providers and most public providers of health services were reorganised into 23 Crown Health Enterprises that would operate as commercial entities.

After substantial health service deficits arose, the purchasers were merged into one health funding authority and a central price schedule introduced. The specified the unit of purchase or 'purchase units' aligning closely with DRGs. Data envelopment analysis (DEA) was applied to the services produced and their overall cost to determine an 'efficient level of expenditure for each sector service category which were then divided by the total equivalent purchase units to obtain an efficient cost per purchasing unit. Thus are paid from a national price book that has prices for different types of operations described in a standard unit (called a cost weight). Important adjustments to the standard cost weight are payments for complexity and payments for rurality (Health Funding Authority, 2000).

In New Zealand the health system is currently being restructured and contracting for both acute and primary care is to be the domain of the elected District Health Boards (DHBs), Figure 2.

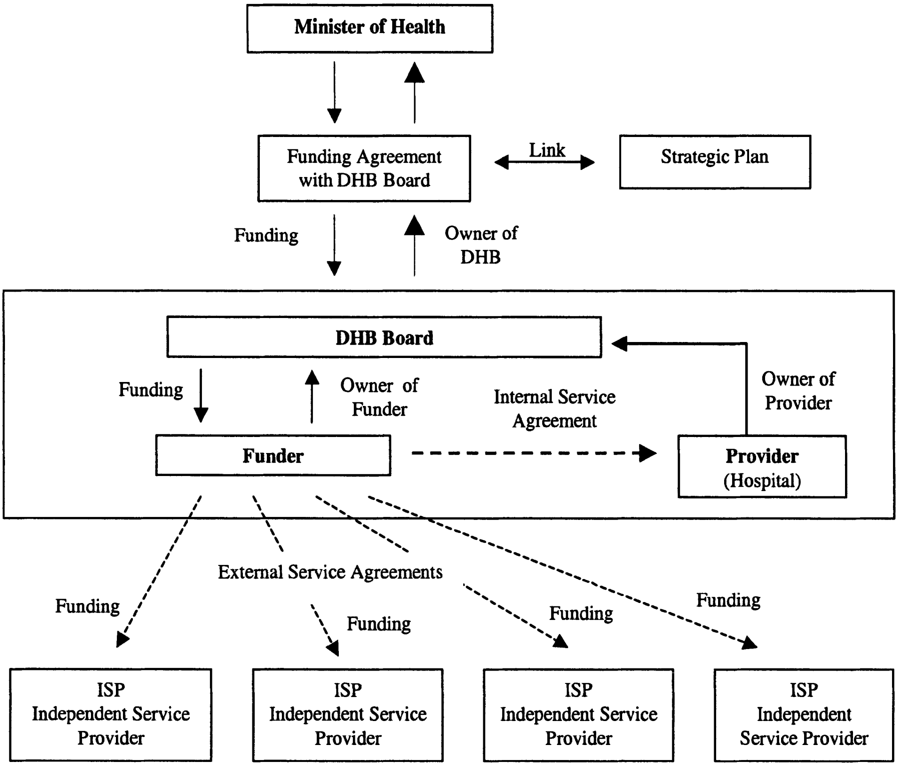

Figure 2: New Zealand Health System
Operation of DHB Funding Agreements

2.3. Similarities and Differences

There are common threads running through the reforms in both countries. Both embarked on a purchaser-provider split at the beginning of the 1990s but healthcare remained predominantly funded by central government. The regional health authorities in New Zealand provided a similar purchasing role to (district) health authorities in England. In England, NHS Trusts were set up as 'free-standing' within the NHS. In New Zealand, Crown Health Enterprises were established for Hospital and Health Services, although wholly owned by the Crown through two shareholding ministers, they were registered under the Companies Act. They had greater independence than NHS trusts, for example, access to capital markets.

Later reforms also contain similarities: the removal of competition and the replacement of contracts with service agreements. The blurring of the boundaries between purchasers and providers –for example Primary Care Trusts in England will commission health services but also provide some primary and community services. Likewise, DHBs in New Zealand have a hospital provider arm funded through an internal service agreement and negotiate external agreements with ISPs (the primary care providers). However, the leadership is quite different. PCTs will be dominated by GPs, DHBs develop from hospital CHEs and will have an elected board. There are no locally elected members on health authorities or NHS trust boards.

While a pricing regime was necessary under the purchaser-provider arrangements in both countries the approaches adopted have differed markedly. The NHS established pricing rules based on cost, (a principle still followed under SAFFs) but contracts with health authorities did not use HRGs as the 'contract currency'. In New Zealand pricing was left to the 'market', (a very imperfect market with few purchasers), initially and following financial crisis a central price schedule was established.

Performance measurement and monitoring, particularly in the UK, is placing greater emphasis on non-financial targets; quality of provision and clinical governance.

Population based funding formula were continued in the NHS internal market, as previously, in funding health authorities. The formulae are being modified to permit population based funding for PCGs (and PCTs). In New Zealand, a capitation formula is proposed for funding DHBs. Thus both countries are attempting to apply formula based funding down to smaller populations.

The reforms since 1990 in the UK and New Zealand increased the perceived need for management information and cost systems. This is considered further in the next section.

3. HOSPITAL COST ACCOUNTING SYSTEMS AND CONTINGENCY THEORY

Cost accounting systems have frequently been depicted in the conventional literature as faithfully representing the economic reality of the organization (Horngren 1977, Fetter 1989, Cooper and Kaplan, 1991). They are seen as functional systems intended to facilitate rational decision-making by organizations in the interests of efficiency. Casemix costing systems have been seen in this context in the USA. Fetter 1989 explains hospital casemix costing systems in terms of manufacturing industry-

> "In the context of these product lines, various aspects of production and operations management commonly employed by manufacturing firms –product selection and design, quality control, and cost accounting –can be applied to hospitals for the purpose of increasing efficiency and quality of care." Fetter 1989 p7.

Subsequently, casemix costing systems have been viewed in a similar manner in both the UK and New Zealand (Ellwood 1992, Lowe and Doolin 1999). In the USA, casemix is analysed by DRG (diagnosis related groups), these have been modified as HRGs (Healthcare Resource Groups) for use in England and New Zealand adopts cost weights obtained through the Australian DRG analysis.

In the UK in the early 1990s heavy investment was made in case-mix systems (Packwood et al 1991). In 1996 Ellwood found that although the number of trusts using case-mix activity systems increased significantly in the first few years of the NHS internal market, Table 3, few included costs within the systems.

Table 3: Computerised Activity Systems 1994 - West Midlands

COMPUTER SYSTEM	% OF PROVIDERS (NHS Trusts)	
	1991	1994
Case-mix	0	38
Nursing dependency	15	25
Pharmacy	44	88
Theatre	15	38
Pathology	36	50
Radiology	23	25

Case-mix costing systems were not used for price setting and did not flourish (Ellwood 1996a and 1996b). There were no case-mix costing systems operating within financial years in the west midlands health region in 2000. Case-mix costing was undertaken at the end of the year, after annual financial statements were published to obtain HRG costs as part of the Reference Costing exercise.

In the years of the NHS internal market, Ellwood (1996b) found conflict between the cost-based pricing rules set down by the NHS Executive and the incentives operating at NHS trust level, Table 4.

Table 4: Conflict between the external contracting rules and internal incentives

COSTING FOR CONTRACTING RULES: NHS EXECUTIVE	INDIVIDUAL TRUST OR UNIT
One "true" or acceptable cost	Full cost is imprecise. Sophisticated cost systems are expensive and little need for pricing purposes.
Comparable cost: uniform allocation and apportionment; uniform cost analysis and classification.	Local circumstances: budget structures ownership by managers/ clinicians
Uniform allocation /apportionment methods	Ownership by managers What decision/ purpose
Uniform analysis and classification	Local circumstances
Attribute all costs and a 6% return on capital. No cross-subsidisation	Use relevant costs Consider decision or purpose
Attribute all costs including a 6% return on capital. No cross-subsidisation	Use relevant costs Consider decision or purpose
Standard Contract Categories	Local need. Product and Purchaser differentiation

These conflicts may be alleviated somewhat in the 'new NHS' where HRG costs are used for performance comparison through the National Reference Exercise (Ellwood, 2000). In November 1998 detailed cost information was published on over 500 surgical procedures across all 249 NHS trusts delivering acute care in 1997/98 (DoH 1998b). The publication of unit cost information is a central feature of the new approach and fulfils a key commitment in the 'new NHS' to produce costs on a consistent basis and publish these in a National Schedule of Reference Costs. Thus the emphasis on costing moved from costing for pricing to costing for performance improvement. Similar exercises have been published in 1999 and 2000, Northcott and Llewellyn (2000) question whether such comparisons are valid.

Some researchers argue e.g. Laughlin et al 1994, that accounting changes produce only superficial effects on the workings of healthcare organizations. Others, e.g. Covelski et al 1993 in the United States, claim that case-mix systems are largely externally orientated.

> "Many elements of organizational structure , like case-mix accounting systems, reflect as much a need to conform to societal expectations of acceptable practice as the technical imperative of fostering rationality." Covelski et al (1993 p.65).

On the other hand, there are instances of sophisticated case-mix costing systems being effective in New Zealand (Lowe 2000):

> "The findings of my research are indicative of the pervasive and invasive nature of accounting systems at the hospital studied. Systems changes do affect the working practices of health professionals and other members of the hospital community and patients. This is not to say that there are not important ways in which these accounting systems also contribute to the external relationships and image of the organization....at the hospital studied there is considerable evidence of the effects of both casemix accounting and medical coding on internal operating processes and resource allocations. The accounting systems are constitutive of organizational reality rather than decoupled from it." Lowe (2000, p.206).

The incidence of case-mix costing systems as part of the financial planning and control system of the hospital is much higher in New Zealand. Of the 21 DHB sites, there are 9 sites that have the Transition system (as used by Health Waikato, referred to by Lowe above) and a small number of sites using similar systems. However, the largest DHB providing the most complex range of healthcare does not currently have a clinical costing system.

Given the large degree of similarity but subtle differences in healthcare policy and operation in recent years a comparison of UK and New Zealand hospitals should aid understanding of the effect of environment on cost accounting systems.

The contingency approach to management accounting is based on the premise that there is no universally appropriate accounting system applicable to all organisations in all circumstances. Rather a contingency theory attempts to specify aspects of an accounting system that are associated with certain defined circumstances and to demonstrate an appropriate matching." P57 Emmanuel et al (199)). It is agreed that the environment (internal and external) and production technology are two primary categories of contingent variables to be considered in choosing a management accounting system (Mauldin et al, 1999). The contingent relationship between internal and external environmental factors (organizational interdependence, decentralization, and perceived environmental uncertainty) and choice of a management accounting system (information scope, timeliness, aggregation, and integration). It is generally concluded that greater organizational interdependence, decentralization, and perceived environmental uncertainty are factors associated with either a greater perceived need for more sophisticated management accounting or higher firm performance with more sophisticated management accounting information (Mauldin et al, 1999).

Transaction cost economics (TCE) and agency theory may sharpen the focus of contingency theory by providing a justification for identifying factors that affect the choice of management accounting system. Under agency theory the role and value of information in organizations on the choice of system is considered. TCE focuses on the structure of the underlying economic transactions: standardization, frequency, uncertainty and investment in unique, or specific, assets. TCE is a comparative theory and, so, would be suited to empirical cross-sectional investigations of organizational differences in the design and implementation of a management accounting system (Williamson, 1995). In a US hospital setting, Kim (1988) found, that when tasks are highly predictable and impersonal communication is used, user satisfaction is higher.

In the public sector, Lüder has put forward a contingency model for governmental accounting innovations by investigating the social-political-administrative environment prevailing in a country and its impact on governmental accounting innovations (Lüder 1992, 1994). The model attempts to explain why government accounting systems, procedures and practices differ from one country to another and why innovation progresses at different pace. The crux of the model is the fundamental assumption that innovation involves interaction amongst three major players –the public, politicians and government administrators. Lüder's original model, Figure 3, contains three contextual variables –stimuli, socio-political factors and administrative factors, these contextual variables are expected to influence two categories of intervening variables: users of government accounting information (by changing their expectations about the data they want) and producers of information (by changing their behaviour). This complex interaction of contextual and intervening variables affects change either positively or negatively. This model was developed in a financial reporting context, but would seem to provide a logical way of examining management accounting innovations in the public sector. Earlier research informs its adaptation into this setting.

This study draws on earlier work on management accounting systems and public sector governmental accounting to provide a framework for examining comparative case-mix costing systems within public healthcare organisations. The literature on whether and how accounting systems make a difference and the extent to which they influence and are influenced by various factors is inconclusive. This study seeks to inform this debate by examining hospital cost accounting systems in their context.

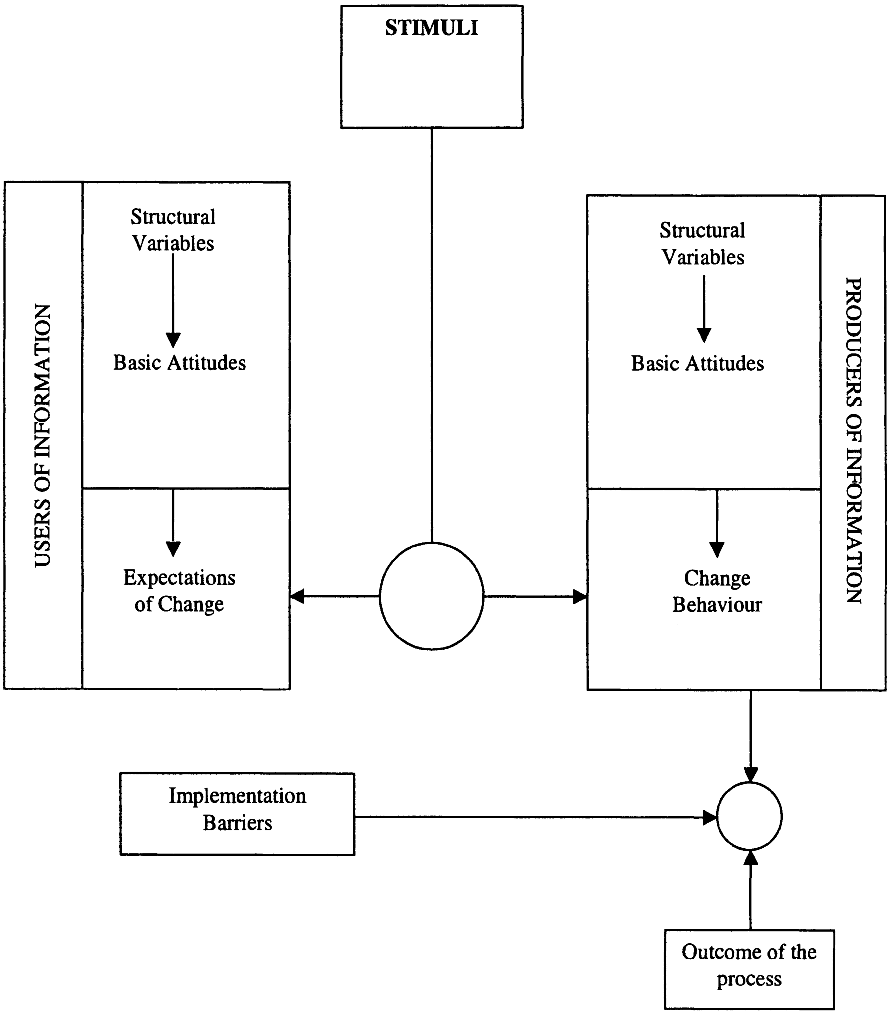

Figure 3: Contingency Model of Public Sector Accounting Innovations Basic Model (Lüder, 1992)

4. THE RESEARCH APPROACH AND INITIAL WORK

The exposition of the UK and New Zealand health care setting has drawn out similarities in the approach to healthcare provision between the two countries and marked differences, Table 5.

Table 5:Some key events in UK and New Zealand healthcare 1990 onwards

UK	New Zealand
1990 NHS and Community Care Act Case-mix systems 'rolled out'	Case-mix systems introduced
1991 Implementation of NHS internal market	1993 purchaser-provider split Four RHAs established
NHS trusts begin	Crown Health Enterprises
GP fundholding introduced	First budget holding Pegasus Steady growth in IPAs
Cost-based pricing rules	Limited co-ordination
1996 Regional offices supersede regional health authorities in England	1996 Four RHAs consolidated into Transitional Health Authority operating deficit problems standardised purchasing units and 'prices'
1997 The new NHS	1998 Health Funding Authority
1999 Quality/ Service Frameworks Reference Costs	
2000 First Primary Care Trusts 2000 NHS Plan	2000/01 District Health Boards set up Elected members Internal agreements

There is also some evidence that case-mix accounting systems have been embraced more readily in New Zealand than the UK. This aspect of accounting innovation can be explored using a contingency model enhanced by an understanding of institutional theory; transaction cost analysis and agency theory. The role and value of information fits well with Lüder's division of the model into producers and users of information. An outline of the contingency model to be investigated is set out below.

4.1. Contingency Model for Innovation in Healthcare Accounting

Stimuli	Financial deficits/ shortage of public financial resources Dominating doctrine (competitive; co-operative / partnership)
Societal Structural Variables	Relative power of clinicians Public expectations of healthcare provision
Political Structural Variables	Decentralisation or 'command and control' Equity/ Access to services

Administrative Structural Variables	External/ national price setting Contracting and budgetary arrangements Costing 'rules' External financial reporting framework Benchmarking Clinical governance Characteristics of senior staff
Implementation barriers	Financial investment Staff expertise

The model will be investigated and developed through case study analysis.

4.2. Case Studies

In the west midlands health region 23 acute hospitals serve approximately 5.2 million population. New Zealand has a population of 3.8 million people. Of the 21 District health Boards in New Zealand, three have been chosen for more detailed investigation.

Case Study A This is a large complex hospital that provides a full range of services, but does not operate a sophisticated case-mix management accounting system. The hospital treated 65,000 cases in 1998/9 of which 36% were tertiary.

Case Study B This is a large acute hospital that has been successfully operating a sophisticated case-mix management system for several years. The hospital treated 45,500 cases in 1998/9 of which 7% were tertiary.

Case Study C This hospital has acquired a sophisticated case-mix management accounting system within the last two years. The hospital treated 24,000 cases in 1998/9, the level of tertiary work is insignificant.

The case studies comprise interviews with personnel, documentation of the management accounting systems, establishing the costs of a small number of clearly defined treatments and identifying how managers use the cost information. The New Zealand case study hospitals will be matched with hospitals from the West Midlands region of the UK.

5. CONCLUSION

In the early 1990s both the UK and New Zealand embarked on an internal market approach to allocating healthcare financial resources. However, the approaches adopted in both costing and pricing healthcare have differed markedly. A number of forces at work at the macro level are similar. The UK has seen the introduction of a quasi market within the health service in the early 1990s followed by a shift to a more co-operative approach since 1997. However, the purchaser-provider split has been maintained. New Zealand has undergone similar changes in the healthcare sector: the responsibilities of the formerly vertically integrated Area Health Boards were redefined in terms of purchasers and providers of healthcare in the early 1990s; but health authorities were later merged into one funding authority and a central price schedule introduced. Both the UK and New Zealand are currently reconfiguring their health structures.

Both countries made heavy investment in case-mix systems in the 1990s. In the UK, detailed case-mix analysis did not form the basis of healthcare contracts and case-mix costing systems did not flourish. On the other hand, there are instances of sophisticated case-mix costing systems being effective in New Zealand. The accounting literature on whether healthcare cost accounting systems make a difference and the extent to which they influence and are influenced by their external environment is inconclusive. The on-going study seeks to inform this debate; in particular it questions whether hospital cost accounting systems are influenced by observable national differences in the health care funding mechanisms rather than following an evolutionary path. The comparative case studies, by identifying differences and similarities in case-mix costing systems between hospitals in the UK and New Zealand, will inform the debate on how management accounting systems in healthcare are influenced by their contextual setting and how such systems are used.

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HELGE MAULAND
FRODE MELLEMVIK

PROGRAMME, FUNDING AND ACCOUNTING INNOVATIONS IN NORWEGIAN UNIVERSITY COLLEGES

1. INTRODUCTION

In Norway there are 26 university colleges located all over the country. They vary considerably in terms of number of students, scientific positions, number of educational programmes etc. The smallest university college has a couple of hundred students while the bigger ones have 6-7000 students and 400-500 scientific positions. The central government funds all university colleges. The educational programmes are mainly undergraduate with a duration of two or three years. During the period 1970-1990 university colleges expanded rapidly both in size and number, and central government funded this expansion.

Growth in university college budgets was slowed down and even came to a halt in the nineties. Nevertheless university colleges have been very ambitious expanding their educational programmes both in duration and variety. Many of them want to offer graduate programmes as a part of their portfolio. To do so governmental approval has to be obtained. When arguing for graduate programmes the explanation of the financial foundation for these programmes is often weak, insufficient and in some cases absent. The normal budgetary procedure is to explain the need for extra scientific positions to run the additional programmes and the yearly costs of these positions. Capacity costs of all kinds, to say nothing of opportunity costs, are not accounted for. For the last years the Ministry of Education, Research and Church Affairs (MER) has granted numerous approvals to establish new educational programmes, but MER has only in a few exceptional cases funded the new programmes. The new governmental trend is that additional and new programmes have to be funded by reallocation of existing resources, which means no fresh money for new programmes. This should normally lead to the shutdown of some other activities.

The purpose of this paper is to describe and analyse whether changes in educational programmes and changes in MER's funding of new programmes influence accounting in Norwegian university colleges (NUCs). This is done by a study of accounting and budgetary procedures in NUCs when they are arguing for and establishing new educational programmes. To give a background for this study the first section gives a short description of a new idea of the Norwegian government, i.e. value for money. In the second section the funding system for NUCs is described. The third section comprises a discussion on what are relevant

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costs when new educational programmes are introduced. In the forth and fifth sections two cases are described and discussed. The first case deals with budgetary allocations and cost calculations in a specific NUC, i.e., Stavanger University College. The second case focuses on budgetary procedures when establishing new programs in several NUCs. The paper ends with a discussion of how to understand changes and continuities in production (programmes) and calculation, and whether there are links between changes in programmes and changes in accounting and calculations.

2. A NEW IDEA: VALUE FOR MONEY

During the last years the Norwegian government has at several occasions proclaimed the renewal of government. The general impression in the public is that there has been much talking and little action. As a matter of fact there has been a reorientation but there is still a long way to go. A thorough discussion of renewal and management in the university sector can be found in a governmental report on the organising and management of the university sector in Norway (NOU:2000:14).

The Norwegian Parliament, Stortinget, has its own set of regulations for the preparation and decision of the budget of central government. Grants by the Norwegian Parliament are allotted in accordance with the regulations stated in the rules for parliamentary grants. The parliamentary rules originate from 1959 but of course there has been a lot of adjustments during the years. In one of the major revisions it was stated that governmental institutions have to account for the results obtained by the governmental grant. In other words parliamentarians wanted to know what they got out of the money and not only a report on whether activities were kept within budgetary limits.

Since the middle of the nineties the parliamentary rules for budgetary grants state that the results aimed at in the budgetary year have to be accounted for in the budget document. How is this provision put into practice for the NUC-system? The MER has formulated no less than 17 different result indexes. None of the results are expressed in monetary terms, they are all physical standards and a kind of good wishes. Nevertheless the regulation is a breakthrough for the idea of value for money, in fact it must be characterised as a kind of management by objectives.

Until the introduction of the regulation governmental management was set up to control that activities were kept within budgetary limits. No one asked if activities were necessary and questioned the performances delivered. In the former budgetary regime resources were allocated in great detail. Since the middle of the nineties resources are allotted to institutions in one amount. In principle institutions can do whatever they want to do within total margin of expenditure. The priority of activities within the budgetary limits is a matter for institutional management. Focus is now on managerial activities while in earlier days control activities were heavily emphasised. The problem is that the management and accounting systems have not been essentially changed. Though institutions are allowed to work out their internal accounts based on the accrual accounting principle, the government accounting system is based on a modified but complicated cash principle. An additional problem is that there is a considerable shortage of management accounting competence in many governmental institutions in spite of many re-schooling programmes for the accounting staff.

In 1996 a new set of financial management regulations for governmental institutions was introduced. The concepts of efficiency and effectiveness were to become an integrated part of everyday financial management in governmental organizations at all levels. In lack of market standards a set of performance indicators came into use measuring performances. Much focus was also put on the autonomy of institutions. In practice the implementation of the new set of regulations has been a troublesome affair. In many governmental organizations financial management is still mainly budget control. Management in governmental organizations is, however, in an increasing degree confronted with the performance measures.

In the early summer of the year 2000 a governmental report on innovations in university sector organization and management was published (NOU:2000:14). Olsen (2000) gives an interesting discussion on several aspects of the governmental report. Only 4,5 pages out of 628 are devoted to funding and financial management questions and challenges.

3. FUNDING OF NORWEGIAN UNIVERSITIES AND UNIVERSITY COLLEGES

So far the NUCs are financed by yearly governmental budgetary grants. The institutions have been receiving a grant, which in principle is divided into two parts. The first part is a basic grant dependent on the judgement (discretion) of the MER. The second part is proportional until a certain limit with the planned number of students. The grant is decreasing by increasing number of planned student (decreasing marginal income). It is not possible, however, to read out of the budgetary document the different parts of the grant, which means lack of transparency in this context.

Until year 2000 university budgets were worked out according to the gross principle, which means that incomes and expenses are reported separately in full numbers. From year 2001 the net principle is used in many institutions, which means that income is deducted from expenses. Probably this is a first step towards budgetary independence. Net budgeting implies that the institution can use as much money they want if they can provide necessary income. The MER will in principle no longer control the activity level.

The NUCs have so far been excellent examples of budgetary linked organizations receiving their financial resources through governmental grants. The MER has signalled very explicitly that income earned by the NUCs themselves have to be increased. This means reductions in budgetary grants, and that resources in a larger scale than today have to be funded by market operations. Fund raising is in fact becoming the everyday reality of Norwegian universities and NUCs, and problems well known to universities in Great Britain and USA seem to be introduced in Norway.

In a management context the consequence of the budgetary coupling is that focus is mainly on the budgetary process and work. The work on accounts and the accounting process are in such organizations more a case of duty and auditing claims than of management control. The accounts are of minor interest for managing purposes. To the extent it is used it is normally only as a tool for budgetary control ensuring that expenses do not exceed grants. As we have pointed out earlier the government has focus on results and performance measures, and this is reflected in the rules for parliamentary grants. The concepts of costs and income (on an accrual basis) are utilised. The institutions can even, if they find it suitable for their purposes, prepare internal cost accounts which deviate from the principles of the standard reporting model. The accounting system must of course be set up in such a manner that it is easy to integrate with the central government system.

The governmental budget is annually presented in the Parliamentary Proposal no 1 (PP1) (Stortingsproposisjon nr 1). The proposals from the particular ministries are part of the PP1, but the detailed ministry budget proposal is submitted in a separate document. In the proposals for the individual ministries, in our case the MER, information of budget grants for the individual NUC is available. This grant cannot be used for funding expenses until the institution has received a particular letter of confirmation or instruction. In this letter the institutions are instructed on how to spend the grant. Some years the instructions have been fairly detailed, and here we are at a point of collision. The MER wants the NUCs to take on responsibility. According to the NUC the administrative performance is to be judged by standards and indexes. On the other hand the NUCs are instructed in detail through an instruction letters. The result is that managers often do not know what to believe in. The escape is to run the business as they have always done, focusing on budget control. They simply do not believe in modern index constructions and performance measures, expecting them to last only for a few years and then there will be new creations to cope with. So far this neglect has been of no consequence for the NUCs. However, from year 2003 budget grants will be linked up with performance in the forthcoming year. Many managers welcome this development, but quite a lot of them are at uneasiness about the future. They fear heavy reductions in budgetary grants as a consequence of not attaining performance standards.

In a white paper to the Norwegian Parliament (Stortingsmelding 27, 2000-2001) entitled 'Do your duties, demand your rights, a quality reform of higher education', a new funding system proposal for the NUCs and the universities was launched. The funding system was approved by the Parliament, and will be in effect from year 2003. From that year the grants will be determined by three factors: (i) a basic grant, (ii) an educational quality premium, and (iii) a research quality premium.

4. WHAT ARE RELEVANT COSTS INTRODUCING NEW EDUCATIONAL PROGRAMMES?

Questions and challenges associated with the introduction of new educational programmes can be approached and considered from different angles, for instance from a pedagogical point of view, and a scientific point of view(see e.g. Whittington, 1994). In this context we will concentrate on exploring the challenges connected with fund raising. What are relevant costs associated with phasing in a new programme in an existing organizational NUC-structure? What are the alternative ways of funding such a programme in a governmental NUC?

How does the question of a new educational programme in a NUC arise? Traditionally new programmes in academic institutions are initiated internally. In the last years both politicians and enterprise people have argued for more influence from the outside on the inner life of the NUCs. Every NUC has external representatives as members of the board. In some institutions the external members have a majority of the board. For the last years many new educational programmes have been initiated from outside the educational institutions.

In 1999 a new graduate programme in resilience management was launched at the NUC of Stavanger. Resilience (safety) management is an excellent example of a programme fought through by institutional outsiders, mainly governmental institutions outside the educational sector. The programme was in reality unwelcome by most scientific parts of the NUC. At last it was fit into the activities of the management and business school and the school of science and technology on a fifty-fifty basis. No fresh money was in sight even it was fought through and heavily wanted by "foreigners". Consequently the board decided a reallocation or structural readjustment of resources. Then the crucial question was raised: Which resources were to be reallocated? Was the intention to restructure the whole NUC including also departments and schools not directly involved in the new programme? The board made a decision that could be interpreted in many ways. The funding of this new programme was still a foggy matter. Probably this was a good decision. In the early winter of 1999 the only way of muddling through this project to have it started in August 1999 was to postpone funding troubles. When the board made its decision the arguing about resources was a question of scientific positions dedicated to the programme. There was no arguing about increased need for administration and equipment.

Listing the activities of a NUC is not a rather straightforward matter. The final products of a NUC are the production of skills (teaching is a mean) and research results. The question of quantifying these final products is, however, not straightforward. Activities are much easier caught sight of. The main activities in a NUC can be classified into the following groups; (i) teaching activities, (ii) research and development activities, and (iii) administrative activities.

The teaching activities are meant to result in the production of skills among the students, and the research activities in publications of all kinds. Administrative activities are necessary supporting functions for the main activities. In the old vocabulary administrative activities cause indirect costs. Normally NUCs do not sell their products in a market, though it could meaningfully have been done. There are in Norway non-governmental institutions, which may be defined as market actors. Most non-governmental institutions receive essential contributions from government. In the forthcoming years the NUCs will have to operate in the educational market. If not acting voluntarily, the MER seems to be willing to force them to go into market operations by drastically reducing grants to institutions which do not adapt to this situation.

What are the cost drivers linked up with the teaching activities? As we know the NUCs, the most important cost drivers connected with teaching activities are number of educational programmes, number of classes, number of subjects, number of lessons taught, number of examinations, and number of students. When we turn to research activities the picture the situation is far less clearly set out. The number of hours spent on research activities is an important cost driver. Research activities also trigger considerable administrative activities.

5. BUDGETARY ALLOCATIONS AT THE NUC OF STAVANGER

The NUC of Stavanger is the second biggest in Norway. The number of students is more than 6.000. There are 614 employees, of which 413 are in scientific positions. Organizationally the NUC of Stavanger is divided into seven schools and two centres. The centres are scientific departments without students and teaching responsibilities. The naming of the schools is evident from the table 1 below.

Table 1. Budget proposal allocation: NUC of Stavanger 1999

School of:	*Limit*	*Strategic measures*	*Total cost*	*Planned number of students*	*Total costs / planned number of students*
Health and social work education	35 526	470	35 996	1 252	28 751
Humanities	19 986	720	20 706	987	20 979
Arts education	11 289	220	11 509	148	77 764
Teachers' education	41 098	1 220	42 318	996	42 488
Hotel management	11 381	1 470	12 851	425	30 238
Science and technology	57 158	1 720	58 878	1 485	39 648
Business administration, culture and social sciences	19 628	720	20 348	879	23 149
Sum primary activities (direct costs)	196 066	6 540	202 606	6 172	32 827
Centre of behavioural research	2 895	130	3 025		
Centre of dyslexia and reading skills	4 165	630	4 795		
University college library	10 134	2 050	12 184		
Administration	53 884	6 650	60 534		
Rent	68 698		68 698		
Common operating costs	26 292		26 292		
Sum indirect costs	166 068	9 460	175 528		

Total budgetary grant from government was NOK 378 134 000 for 1999. Of this amount NOK 202 606 000 is allocated to the schools while the remaining is allocated to the library and administrative services of all kinds. This means that 53,7 % of total grant is allocated directly to the primary activities while the remaining 46,7 % must be characterised as indirect costs. This implies that the ratio between school costs and the number of students must be interpreted with caution. The ratio is of interest as an internal indicator of resource allocation, but it cannot uncritically be applied in inter-NUC comparisons. This is due to the fact that internal organization and internal budget procedures differ among the NUCs.

There is a particular allocation for strategic measures. Examples of such measures are organizational innovations within the schools and administrative departments. For 1999 NOK 16 mill were allocated to such measures. In principle the different schools can spend the money in the way they find most convenient. Reality is somewhat different. Approximately 90 % of the allocations are bound up in full-time posts (tenures), which means that financial freedom of action is very restricted. The cost allocation will be easier reviewed if we aggregate costs in the way done in table 2 below:

Table 2. Cost allocation for main groups at NUC of Stavanger

	Costs	*Relative proportion*
Costs allocated to the schools	202 606	54 %
Costs allocated to the centres	7 820	2 %
Costs allocated to administrative and operational units	167 708	44 %
Total costs of the NUC of Stavanger	378 134	100 %

Of the total costs of NOK 378 mill, about 44 % is allocated to what may be classified as indirect activities. In his survey Bourn (1994) found that this proportion varied between 23 and 40 % in British universities. Costs allocated to indirect activities are considerable viewed in an international perspective.

An innovation of the last years' governmental accounting regulations is the delegation of authority in economic matters. With nearly half of the budgetary amount not allocated to primary activities, it may be questioned if the delegation of authority is real. In our discussion it is referred to budgetary figures. It is a well-known fact that budget and accounting figures may deviate substantially in public sector organizations (Høgheim *et al.*, 1989). Another problem is that accounting reports according to the template in table 1 are not worked out.

Cost per planned student does not reflect a "true and fair view" of the situation, particularly if figures are to be compared with other NUCs. This is due to the fact that activities are organised in different ways around the country. It is a matter of question whether allocations of indirect costs are meaningful at all, but we shall not enter into the debate of absorption versus variable costing at this occasion. If comparisons of costs are to be of any use, cost distributions have to be made in one way or another. It holds for private sector as well as public sector organizations.

When indirect costs are allocated to different cost objects, the discussion of cost drivers becomes relevant. Which activities trigger the use of resources and in which ways? Readers with further interest in this subject are referred to Bjørnenak (1998) and Whittington (1994).

The two scientific centres are particular for the NUC of Stavanger compared to other NUCs. As mentioned above the centres have no students but perform research activities and consultant work at a pay basis. It is therefore reasonable to allocate indirect or undistributed costs to the centres in the same way as to the schools.

5.1 Cost allocations with different consequences

Let us assume that the number of employees is the cost driver. This way of thinking is very simple, the greater the number of employees, the bigger the consumption of indirect costs. As a consequence of this assumption undistributed costs will be allocated in accordance with the relative number of fixed positions in each unit. Several objections can be made to this way of distributing costs, but a central point is to reach a operative distribution method easily grasped by everybody in non-accounting surroundings. In table 3 planned number of students are made use of.

Table 3. Cost allocations to schools and centres

School of:	*Relative portion of fixed positions*	*Allocated costs**	*Direct costs**	*Total costs**	*Planned number of students*	*Cost per Student**	*Ranking*
Arts education	5 %	8 702	11 509	20 211	148	137	1
Science and technology	30 %	49 679	58 878	108 557	1 485	73	2
Teachers' education	14 %	23 826	42 318	66 144	996	66	3
Health and social work education	19 %	31 260	35 996	67 256	1 252	54	4
Hotel management	6 %	9 294	12 851	22 145	425	52	5
Business administration, culture and social sciences	10 %	17 067	20 348	37 415	879	43	6
Humanities	10 %	17 067	20 706	37 773	987	38	7
Centre of behavioural research	3 %	5 745	3 025	8 770			
Centre of dyslexia and reading skills	3 %	5 069	4 795	9 864			
Totally	100 %	167 708	210 426	378 134	6 172	61	

** Data in thousands*

The national average student cost including all the NUCs and all the programmes was this year NOK 65 883. This means that student costs are above national average in three schools and below for the remaining three. From table 3 it is evident that the arts education (primarily music) is by far the most expensive. The art student is 3,56 times more expensive than the student of foreign languages and history (humanities). This is in no way a sensational finding. It has to be accepted that some programmes are more expensive than others. However, there is little consciousness about these differences in the NUC of Stavanger.

For insiders none of the figures above are astonishing. It is, however, hard to give an understanding for and arguments for some of the cost differences. Hotel management and business administration could be relevant examples. The programmes are almost identical, except for the focus on hotels in the hotel management school. During the years many have advocated for merging of the two schools, but so far this has not been done. The cost per student of one of these (the hotel management school) is more than 20 % higher than the cost per student in the other school. Another school with a relative high cost per student is that of teachers' training. The reason for this is probably that all students have to practice teaching as part of their education, and the NUC has to pay much for this practice.

5.2 Is measurement of cost per student a meaningful standard?

This way of reasoning implicitly assumes that the cost per student is a meaningful performance indicator. In this context the student must be considered the final product. As we have discussed above, this is not a straightforward assumption. Let us now apply another method of cost assignment. We will now use planned number of students as cost assignment criterion. Once again, the centres are excluded from our ranking list because there are no students. The results are presented in the table 4 below.

The student of arts is still by far the most expensive, but it is a remarkable fall in student cost or price as a consequence of an alternative cost assignment method. The teachers' education student has now advanced to a second position and relegated the student of science and technology to position four. Bottom positions are still occupied by the students of business and humanities, but unit cost or prices have risen considerably. A relevant question is now what the true cost is. It is not a straightforward matter deciding on how much resources should be allocated to the particular programmes. Probably the most expensive programmes are too expensive and the cheapest too cheap. No doubt the learning and studying conditions of the art student are far beyond those of the student of humanities.

What is the point with these exercises of calculation? At a first glance they just confirm what accountants already know, there is no true cost or price. There are few or none principal guidelines for how resources can be allocated internally. The budgeting procedure is a time-consuming process. The management of the Stavanger NUC plans to simplify the budgeting process introducing a budgetary model in many ways predetermining resource allocation to the different schools. The starting point for this model is extremely important. If costs are underestimated at the very beginning, this may have fatal consequences for the forthcoming years. Adjustments of the model cannot be expected before several years of experience has been attained of how the model has functioned.

Table 4. Indirect costs assigned in accordance with planned number of students

School of	*Planned number of students*	*Relative portion of students*	*Allocated costs**	*Direct costs**	*Total costs**	*Cost per Student**	*Ranking*
Arts education	148	3 %	4 022	11 509	15 531	105	1
Teachers' education	996	16 %	27 064	42 318	69 382	70	2
Science and technology	1 485	24 %	40 351	58 878	99 229	67	3
Hotel management	425	7 %	11 548	12 851	24 399	57	4
Health and social work education	1 252	20 %	34 020	35 996	70 016	56	5
Business administration, culture and social sciences	879	14 %	23 885	20 348	44 233	50	6
Humanities	987	16 %	26 819	20 706	47 525	48	7
Centre of behavioural research				3 025	3 025		
Centre of dyslexia and reading skills				4 795	4 795		
Totally	6 172	100%	167 708	210 426	378 134	61	

** Data in thousands*

Until now the NUCs are mainly funded by governmental budget grants. The MER has several years ago signalled that the NUCs have to increase their earnings, which means selling teaching and research services in the market. To some extent the NUCs have to adjust to market prices, but the situation of today is that a majority of the NUCs only have vague ideas of the costing of these services. Market activities will necessitate development of a costing system within the institutions. Normally it is impossible to operate in a market without knowing the costs of the services you are selling.

6. ESTABLISHING NEW PROGRAMMES: BUDGETARY PROCEDURES AND ARGUMENTS

Several NUCs have in the last years expanded their undergraduate programmes in business and administration from 120 ECTS to 180 ECTS. Such an expansion has to be approved of by the MER. According to the MER guidelines for this kind of applications the applicant has to explain how the expansion is to be financed. Normally an applicant does not bother going into details in these matters but simply refer to the fact that the programme is being financed by reallocation of resources. There is no explanation of the need of resources (equipment, premises, library services, administrative staff etc.), and no explanation of programmes or activities being phased out. We have looked into the application documents of five NUCs applying for an expansion of their undergraduate programmes by 60 ECTS in business and administration (one year's educational programme). Our findings are listed in table 5 below.

Table 5. Funding of expansion of undergraduate programmes

University college of	*Programme*	*Termination of other activities*	*Financing*	*Explanation of expansion costs*
Finnmark	Expansion of undergraduate programme	No	Reallocation of resources	No
Hedmark	Expansion of undergraduate programme	No	Reallocation of resources	No
Sogn og Fjordane	Expansion of undergraduate programme	No	Reallocation of resources	No
Sør-Trøndelag	Expansion of undergraduate programme	No	Reallocation of resources	No
Telemark	Expansion of undergraduate programme	No	Reallocation of resources	No

The NUC of Hedmark is the most explicit institution regarding the question of financing. According to the application document, a planned number of students in one programme are going to be transferred to the new programme. The original programme is still going to be run, however, but with a lower number of students. Reasoning along this line is valid if the student is the cost driver. In the financing system of today the student is, however, the resource driver. An extra approved planned student trigger off money from the government. The reason why these

NUCs have been able to expand their undergraduate programmes without adding fresh money may be organizational slack. Institutions receive resources based on the planned number of students though there is nearly always a considerable deviation between the planned student number and the actual number.

6.1 Introducing master programmes

In 1999 five NUCs (see table 6 below) were allowed to introduce graduate programmes in different areas as pilot projects. The invitation from MER to apply for the establishment of graduate programmes came very unexpectedly to most of the NUCs. Only a few of them had ready plans in their drawers to take part in the application round. The operation of the different programmes is now being evaluated.

The question of financing the graduate programmes has been accounted for in different and mostly "non-accounting" ways in all those institutions. Figures illuminating and illustrating the financial questions are more or less absent in all application documents. Maybe these are deliberate tactics of getting programmes established. Each NUC management is probably aware of the danger of accounting for all costs and consequences knowing very well that illustrating consequences in an explicit way would impede the realisation of the programmes. However, from reports prepared by these NUCs it is unexpected, nearly paradoxical, that consequences cannot be sorted out after the programmes have been in operation for two years.

Table 6. Funding of graduate programmes expansion

University college of	*Programme*	*Termination of other activities*	*Financing*	*Explanation of expansion costs*
Agder	Graduate programme in public sector administration, graduate programme in IT	No	Reallocation of resources	No
Finnmark	Graduate programme in tourism	No	Reallocation of resources	No
Molde	Graduate programme in logistics	Yes	Reallocation of resources	Yes
Stavanger	Graduate programme in resilience (safety) management	No	Reallocation of resources, NOK 500000 as compensation for expansion (permanent yearly grant)	No
Volda	Graduate programme in planning	No	Reallocation of resources	No

Table 6 illustrates an identical situation as in table 5. Funding of the expansion is not accounted for in any detail. Financial problems are resolved by referring to the key words of reallocation of resources. In none of the cases plans were presented to the boards of the NUCs explaining the phasing out of already existing educational programmes. Though, we do not know how these expansions are financed, they can in general be explained in three ways; (i) substantial organizational slack, (ii) reduction of research and development activities in the NUCs, or (iii) a combination of both of these. If these expansions have been financed from organizational slack, the institutions have been over-funded. We have no clear answer to how these expansions have been financed. However, we have notices that accounting systems and procedures are not changed in the wake of the expansion of the educational programmes. Seemingly, there are in these institutions no explicit expressed needs for further information or accounting system development.

7. CHANGES, CONTINUITY AND IMPLICATIONS

The purpose of this study has been to describe and analyse whether changes in educational programmes and changes in MER's funding of new programmes influence accounting in the NUCs. There are a lot of different theoretical approaches that could be used as part of departure for such a discussion, i.e. population ecology, organizational economics, contingency theory, theories of interpretation and translation, institutional theory (see e.g. Clegg and Hardy, 1999; Czarniawska and Sevon, 1996; DiMaggio and Powell, 1991; Giddens, 1993;Weick and Westley, 1996). In this study we are influenced by several of these approaches. As indicated above this study is, however, more driven by empirical observations and ideas of practical implications than by a specific theoretical frame work. The analysis starts with a discussion of where do changes in programmes and accounting come from, and what kind of understanding of the public sector do they imply? Thereafter, we discuss links between changes in programmes and accounting/calculations. Thirdly, and as a conclusion we focus on implications of the structure revealed in this study of changes and continuity (no changes) in programmes and accounting/calculations.

7.1 How to understand changes in programmes and accounting?

Changes could be discussed from visions/assumptions on future that is found in these organizations (NUCs and the MER). These visions/assumptions could be developed internally in the Norwegian public sector, but they can also be influences by interested parties external to the Norwegian public sector, i.e. from public sector development in other countries or from the private sector. Changes in programmes and accounting can, therefore, be generated internally, externally, or in a combination of influences from both inside and outside the Norwegian public sector. In table 7 we have focussed on whether the influence comes from either internal or external forces.

Inherent in these changes there can be an understanding of the public sector as a closed or an open sector. An understanding of the public sector as closed implies that public sector organizations are regarded as special with tasks and functions that cannot be solved or taken care of by organizations outside the public sector. However, on the contrary changes can imply an understanding of public sector organizations as open and in interactions with organizations located and embedded in other contexts that the public sector. Such an understanding easily opens for competition between organizations located in different sectors, i.e. other organizations can take over or fulfil the tasks and functions of public sector organizations. In table 7 this is indicated as "closed" and "open".

Table 7. How to understand changes?

		Where do changes come from?	
		Internal	*External*
Understanding of public sector	*Closed*	Degeneration	Sectorization
	Open	Adaptation	Uniformity and fashion

From these two perspectives four scenarios for changes implying different understandings of changes or continuity occur. If changes are internally developed with emphasis on public sector as closed, changes can be characterized as a kind of degeneration. The space for inspiration and ideas is limited to what has been going on inside the organization or sector, and this limitation implies reproduction with refinement of models and structures as the basic and only opportunity. As soon as the space for inspiration is more open, other opportunities for changes will be present. Though changes are generated internally, an understanding of public sector organizations as open and in some competition with or in tension to other organizations, will imply opportunities for reflections about how other organizations would handle some of the same tasks and functions as public sector organizations. Plans and proposals for changes will then be influenced by these other organizations. In table 7 this is described as "adaptation". Such adaptation does not, however, have to mean copying others. It can simply mean that other organizations' ways of coping with reality are at least partly premises for the changes. If changes are generated externally but with a view of public sector as closed, new structures and processes will be explicitly public sector oriented. It means that independent of the specific problem that the change is meant to handle, the change builds on a vision or assumption that some solutions go while others do not for public sector organizations. The change is therefore characterised as "sectorization" meaning that the change is explicitly sector specific. If changes are externally developed and based on an understanding of public sector as open and in competition and interaction with other organizations, the changes will be influenced by what is regarded as proper and appropriate. In this way the change will tend to lead to what could be described as global uniformity characterised by what is regarded as fashion or modern (see e.g. Røvik, 1998).

Changes in programmes and calculations in Norwegian University Colleges have to a large degree been developed internally inside the sector or inside each NUC or in the MER. The MER's introduction of "operational targets" and introduction of new programmes at a NUC could indirectly be influenced from external parties. We have, however, no observations of change directly influenced from external parties. We, therefore, conclude that changes in programmes and calculations can be characterised mostly as either degeneration or adaptation.

7.2 Links between changes in calculations and programmes.

Independent on how changes can be characterised different links between changes in calculations and accounting respectively can be deducted and discussed. Programmes, organizations and organising can change while accounting and calculation methods and routines are unchanged and vice versa. In table 8 we present four different links between accounting and programmes depending on whether there are changes in either programmes or accounting.

Table 8. Links between changes in accounting and programmes

		Changes in accounting/calculations: *No*	*Yes*
Organizational/ programme changes	*No*	Belief in past	Belief in accounting
	Yes	Belief in innovations	Belief in new ways/ entrepreneurial spirit

If there is a strong belief in the solutions of the past, there are naturally no needs for changes. It means that programmes offered are expected to be attractive also in future, and that the way financial resources are allocated and consumed is regarded as suitable and as a security for the future of the organization. If the present situation is regarded as comfortable, changes in programmes and accounting systems would only imply expenses and threats to, for instance, existing structure of power allocation in the organizations. Continuity is preferred by the rulers of the organization.

If there are changes in accounting/calculation but not in organization/-programmes, there is a belief in accounting, and that changes in accounting/calculation either will improve the financial situation and flexibility of the organization or reduce some kinds of problems internally. Fights for more resources from some organizational units, e.g. departments, easily lead to the quest for new accounting systems or calculation methods with the belief that a new system will solve or at least lead to improvements in handling production problems of today.

On the other hand, if there is no change in accounting but programmes / organization are changed, there is a belief in necessity of innovations of programmes. There can be a variety of reasons why there is such a belief in innovations, for instance, changes in legislation or ministry norms, technological changes in education methods and/or market forces (e.g. reduction or increase in demand for specific programmes). This scenario implies no changes in accounting/calculations. In this way ideas of importance of innovations in programmes are not matched with such ideas when it comes to the accounting system. There is, therefore, a kind of a trust in the accounting system/calculation methods implying that the accounting reports or the specific calculations portray what eventually are of importance and relevance for changes in production.

The fourth link illustrated in table 8 between changes in programmes and accounting, implies beliefs in new ways of doing calculations/management control as well as of developing programmes. In this situation there is a kind of entrepreneurial spirit in the organization. There can be many reasons for such a spirit depending on what are recognized as the forces behind the changes (e.g., new technology, market forces, regulations or deregulations). This situation can be characterized as radical in the sense that there is a pressure to develop both new programmes and new methods for management control.

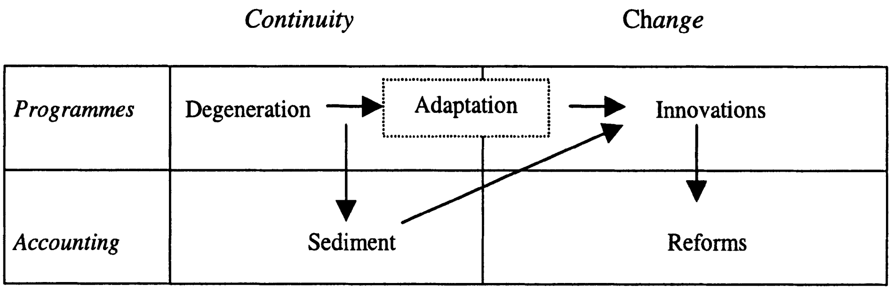
Neither the NUCs studied in this project nor the MER have introduced new accounting systems or new calculations methods. Though the MER requires comments on "operational targets" and that there are some lines and hints in the MER's annual instruction letter to the NUCs about management control purposes, these requirements are so vague that we conclude that there have been no changes in accounting or calculations. However, there have been some changes in programmes. Some of these changes have been initiated by ideas presented by the MER, while others as in the case of the NUC of Stavanger have been locally initiated and developed. Though these tendencies of changes in programmes do not characterise the production and development of NUCs' education programmes in generally, we conclude that there is today a belief in Norway in innovations of education programmes. This belief is matched with a belief in that existing accounting systems and calculation methods are suitable for management control of the NUCs.

8. CONCLUSION

In this concluding section we will focus on two of the main findings in this study, and implications of them. Firstly, there are changes in the education programmes signalling a belief in innovations, which in one or another way is founded on an understanding of a changed context for NUCs. However, this belief does not imply that programmes to any large extend are changed based on external influence. It is quite the opposite. To a large extent changes are internally initiated either in the NUC or in the MER. In this way the innovations are characterized not only by adaptation to a new context but also by copying former solutions, i.e. innovations are including elements of degeneration. Secondly, there are no substantial changes in the accounting systems or in the calculation methods, meaning that the understanding of a changing context has not implied observable wishes or pressures for changes in accounting.

In table 9 we indicate some implications that can be deducted, and some that can be discussed, based on this study. The directions of change and continuity (none changes) in programmes and accounting are illustrated by the arrows. Degeneration means that new programmes reflect former programmes without taking into account changes in the NUCs' context or in the demand for programmes offered by the NUCs . However, the changed programmes do not only focus on an understanding of a NUC as a closed organization. Expectations and ideas from outside NUCs and the MER are also parts of the proposals for changes in programmes. In this way there is a movement from continuity to change, i.e. from degeneration to innovation via adaptations implying an understanding of NUCs as open organizations in interaction and competition with other organizations.

Table 9. Implications



When it comes to accounting there have been no changes. In this way there is a continuity in calculation methods and in an understanding that available accounting information gives, if necessary, reliable and relevant descriptions of financial and economic consequences of changes in programmes. The reason why there is such an understanding is probably because there is organizational slack in the NUCs, and that initiations for changes from outside do not imply pressure for internal reallocation of resources. In the movement from degeneration to innovations in programmes there is some kind of a link to accounting in the way that the accounting system at hand and the calculation methods used, can serve as security creating stability. In this way the accounting system can be regarded as a sediment from the past, giving security when changing programmes. From such a perspective changes in programmes are made possible partly because there is an accounting system that does not change, and at the same time accounting information legitimizing programme innovations. It is, however, an open question what will happen when or if the programme innovations are so thoroughly that they will imply a quest for reallocation of resources. Probably will such a situation mean that accounting also will change because it will be necessary to do calculations and economic reflections about consequences of programme changes. In table 9 we illustrate this with an arrow from innovations to reforms. However, there are not in Norway any accounting system or calculation methods developed for use in NUCs. A reform will therefore implying the development of new models and methods. As a point of departure there is of course both accounting theory and theory of calculation methods available that can help in this development. These theories need, however, to be translated and formed to the practice in which accounting/calculations are to be used. Experimentation is therefore needed in the field of accounting and calculations especially in the NUCs and generally in the Norwegian governmental sector.

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MARC A. RUBIN

AN INTERNATIONAL COMPARISON OF SCHOOL PERFORMANCE REPORTING

INTRODUCTION

Since education expenditures are a sizable portion of government spending in most countries citizens have an interest in the return on educational investments. Yet, there does not exist universally accepted processes for obtaining educational accountability or methods of measuring and communicating the performance of school administrators, teachers, and students. Consistent and comparable information concerning the return on funds invested in education remains elusive. Examples of programs that are intended to increase school performance and accountability include school or school district report cards, accountability audits, resource allocations based on school or student performance, charter schools, and school choice programs. Each of these programs requires stakeholders to use extensive amounts of information on the performance of schools, teachers and students.

This article describes and compares the current state of providing school accountability information for five English-speaking countries. These five countries are selected for comparison because they are similar in the type of government (democratic), the percentage of gross domestic product spent on education (five to seven percent) and in the ease of obtaining current information. The next section of this article presents an overall view of school accountability programs and their information needs. This is followed by the description of methods of providing and financing schools and for holding the educational service providers accountable in the following five countries; New Zealand, Australia, Canada, Great Britain and the United States. The final sections will compare education provision and accountability methods among the five countries, evaluate the current status of educational accountability, and offer suggestions for improving accountability reporting.

1. INFORMATION NEEDS OF SCHOOL ACCOUNTABILITY PROGRAMS

Accountability programs are designed by governments to assess the success of education providers in the use of resources committed to schools. Some of these accountability programs attempt to hold educators accountable through a top-down process. In a top-down accountability process information is provided to a higher

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 301-318.

authority and that authority is responsible for using the information to assess and possibly change the process for providing educational services. An example of top-down accountability is when performance information relating to teachers is collected and reviewed by school or school district administrators. It is up to the administrator to decide whether any actions are needed to change and improve the method for delivering educational services. The amount of information needed by administrators using a top-down accountability process is often considerable.

Top-down accountability in schools depends on understanding the relationship between educational inputs and performance. The relationship between educational inputs and outputs is the focus of a considerable number of research studies (Hanushek, 1997). In these studies, achievement test scores and graduation rates are typically used as measures of student or school performance. The selection of input measures is less consistent with numerous characteristics being studied as determinants of school or student performance. Research results have not provided conclusive evidence relating a consistent set of specific education resources to school or student performance. A broad examination of the research evidence suggests that student achievement is generally associated with factors related to family influences, peer groups, and the school environment. Education service providers may directly influence only school environment, and even the responsibility for school environment may be shared among a number of service providers and administrators, making it difficult to determine whose performance is impacting outcomes. The problem of determining the appropriate educational inputs and assigning responsibility for their control contributes to the overall difficulty of instituting effective top-down educational accountability.

A second process for holding education service providers accountable is a bottom-up process. Instead of accountability being the responsibility of school administrators, the process of bottom-up accountability requires the recipients of educational services to have leverage over service providers. Service recipients can exert their leverage by having the ability to select desirable service providers or opt out of inadequate or unsuitable service providers. Examples of educational programs that allow for bottom-up accountability include choice programs, voucher programs, and charter school programs. In programs where educational service recipients have at least some ability to select educational service providers, information is needed by education recipients to make informed selections. Service recipients require information that allows for assessment of the adequacy of a service provider in meeting the educational goals of the recipient. The specific information that is required by service recipients to make choices may generally coincide with the information that is required by administrators in top-down accountability processes.

It is clear that both top-down and bottom-up accountability require that decision-makers have information available that allows them to assess the performance of providers of educational services. The information needed by decision-makers should enable them to relate educational inputs to outputs and determine a return on educational investments.

The next section of the article provides a description of the provision and financing of education and of accountability methods in five English-speaking countries. Education accountability is defined as a process for providing information to education stakeholders to be used for assessing and decision-making regarding the provision of educational services. This article does not examine how individual students are assessed and reported upon nor does it examine broad indicators of student achievement used to compare the overall progress of the students in one jurisdiction with students in another jurisdiction (such as a comparison of student achievement between two countries). This article focuses on assessing the quality of an individual school or school district.

2. COUNTRY DESCRIPTION

2.1 New Zealand

2.1.1 Provision of Education

In New Zealand compulsory education is categorized into primary, intermediate and secondary schooling. Schools, either private or state, must follow the provisions of the Education Act of 1989. The Parliament is responsible for making law applicable to education, providing funding for schools, and developing accountability programs to determine the efficiency and effectiveness of monies spent. Various ministries and agencies are then charged with carrying out the provision of educational services. A board of trustees and principal manages individual schools. Trustee boards are composed of elected parent and community members, the principal and a staff representative. The trustees are considered to be the group accountable for assuring that a school meets its objectives. New Zealand has National Education Guidelines (NEG), which are obligations that schools are required to meet. Public school funding is provided, in part, by the national government and is augmented by the local community. Private schools also receive a government subsidy. Public schools receive national funding (allocated by the Ministry of Education) in four component parts: operating grants, staffing, school property and school transport assistance. Additional government funding is provided for special categories of students such as those with learning disabilities and low socio-economic status. Local school trustees may also raise funds, through programs such as sponsorships with local businesses, to provide extra activities and opportunities. Currently, local boards administer operational grants while most staffing funds are provided and managed by the Ministry of Education. The government also allows for local boards to administer funds provided by the national government using a set formula.

The New Zealand State school system allows for variation in teaching philosophies and methods. Parents are allowed to choose between various programs offered at different schools. The New Zealand Curriculum guides teaching, learning and assessment for all students in all schools. Objectives are provided for significant learning areas and are subsequently used to assess teachers and students.

2.1.2 Accountability

New Zealand has a national goal to improve the effectiveness and efficiency of resources use in education. The Education Review Office (ERO) is the agency directly charged with evaluating schools and providing accountability reports. The ERO provides accountability reviews that report on the quality of education for students in individual schools. The evaluation is based upon the National Education Guidelines, the school's own charter and the school's own expectations of its students. Currently, there is no national assessment system to ascertain improvements in student or school achievement. Examples of New Zealand accountability reviews can be found at http://www.ero.govt.nz/publish/reppub.ns4 /Schools. New Zealand is currently moving away from norm-referenced towards standards-based assessment. School accountability reviews are prepared using a rotation of three to five years depending on the type of school, quality of performance, or risk factors of the student population. While the reports are written for the school's governing body and the Ministry, all are made available to public. In addition to accountability reviews, the ERO provides homeschool reviews, cluster reviews, contract evaluation services, and education evaluation reports, which are national assessments of various aspects of the educational system.

2.2 Australia

2.2.1 Provision of Education

Responsibility for the provision of education in Australia is given to the states and territories. Each state and territory determines the responsibility individual schools have on matters of curriculum, staffing, resources and assessment. The national government contributes approximately 45% of the funding for all schools, although this percentage is a bit smaller for primary and secondary education as compared to post-secondary education. The trend has been toward the national government undertaking a larger percentage of education costs. National funding is in the forms of recurrent and capital grants. The remaining funding for education is the responsibility of the state and territory governments. Funding from parents and communities helps in the purchase of additional equipment and learning materials. Private expenditures for education, while growing, remain relatively small compared to government spending.

2.2.2 Accountability

Currently, schools have considerable flexibility in providing accountability reports. The individual state ministers have broadly agreed on general education objectives. These objectives are grouped into three classifications: learning outcomes; social and other objectives; and equity objectives. The Ministerial Council for Education, Employment, Training and Youth Affairs (MCEETYA) is the national forum for cooperation in schooling. MCEETYA is developing a common framework for reporting student progress. In 1996 MCEETYA commenced a project to develop a small number of common outcome indicators in language and mathematics. School systems may prescribe how individual schools report to their constituents or leave it to the discretion of the schools. In a few instances, independent auditors are used to verify the information reported. Most school systems that report on the achievement of individual schools use either an annual report or external review process. An example of a state report can be found at http://home.vicnet.net.au/~vicaud1/. A thorough analysis of educational assessment, including the need for accountability information, can be found in Cuttance and Stokes (2000).

2.3 Canada

2.3.1 Provision of Education

In Canada, education provision is the exclusive responsibility of the ten provinces and two territories. Each Ministry and Department of Education typically controls school curriculum, financing, teacher certification, and assessment methods. There is neither a national curriculum nor national education standards. For practical purposes, there are twelve education systems. There are some common aspects in the provision of education among the provinces, but a number of differences as well. Local school governance is the responsibility of elected school boards and trustees.

Financing is also at the discretion of the provincial government. Each province or territory determines how much school funding is the responsibility of the local government and how much is provided by the provincial government. Federal support for primary and secondary schools is limited, with most support for particular programs (such as language). Education budgets have been tightening in recent years.

2.3.2 Accountability

Recent trends in Canadian schooling include increase emphasis on standards, accountability and reporting. More attention is now being paid to outcomes and performance measurement. Reporting to the public on progress toward policy objectives is more commonplace because of demands from constituents.

The Council of Ministers of Education, Canada (CMEC) is a group that helps in the sharing of information between the different educational jurisdictions. The CMEC works on initiatives of interest to all jurisdictions as well as issues that are only of interest to selected provinces or territories. Current initiatives include collecting information on educational performance (the School Achievement Indicators Programme or SAIP) and producing reports on various aspects of education in Canada. The SAIP program augments any current local or provincial assessment and attempts to provide information on the overall progress of 13 and 16-year-old students across Canada in regards to achievement levels in mathematics, writing, reading and science. The data collected for SAIP is not intended to evaluate specific students or schools, but to allow evaluation of the overall achievement of students and its relationship with school, home, and social environment. For more information on CMEC initiatives, see their web site at http://www.cmec.ca. For an example of a provincial financial accountability report, see the British Columbia Ministry of Education web site at http://www.bced.gov.bc.ca/accountability/. The British Columbian government, while providing broad principals of assessment, monitoring, and reporting, does not require local school districts to compute and report specific measures of outcomes or efficiency.

2.4 United Kingdom

2.4.1 Provision of Education

Most of the information about the UK included in this section is specifically about England. Much of what is described for England is similar for Wales, Northern Ireland and to a lesser degree Scotland. The major governmental department responsible for national education policy in England is the Department for Education and Employment (DfEE). In England, the general approach to school management is decentralization and delegation to the immediate service providers to allow them to be self-managing. Local Education Authorities (LEAs) are charged with ensuring that their area has sufficient primary and secondary schools. Schools are of three types: community, voluntary (controlled or aided), or foundation. The differences in the categories relate to the responsibility of employment and ownership of the land. Most schools (approximately 60%) are community schools.

The LEA is responsible for providing the operational funds for all school and the capital funds for community, voluntary controlled and foundation schools. Capital funds for voluntary aided schools use a different system. Capital funding decisions for all school categories should be consistent with the LEAs Asset Management Plan, which is used to prioritize local capital funding needs.

The governing bodies of LEAs are given the authority for school budgeting, staffing, curriculum, pupil admissions and exclusions. School funds are primarily (80%) received from grants administered by the Department of the Environment, Transport, and Regions (DETR). Remaining funds are from local sources, primarily the Council Tax. LEAs determine the budget for local schools and then allocate those funds to specific schools by a formula that is mostly related to the number of students. Individual schools can determine how to allocate funds received as long as they are consistent with LEA guidelines. Although LEAs have considerable autonomy for school funding, they can be constrained by the national government.

2.4.2 Accountability

LEAs are required to have an independent audit of their accounts. Many LEAs have developed financial benchmarks to assist school management in assessing costs. LEAs provide guidance to schools for financial reporting. Schools are usually allowed to determine their own accounting systems. LEAs can require individual schools to have audits of their financial records.

Statistical reports on LEAs are available from the DfEE. See the website at http://www.dfee.gov.uk/statistics/DB/LEA/leas.html. These reports, while not detailed, contain four years of information on performance, specific initiatives, and finance. The DfEE also provides information on the Beacon Council Scheme, which is intended to make available case studies of best practices for various aspects of local government, including education. Additional information on the Beacon Council Scheme can be found at http://www.standards.dfee.gov.uk/lea/scheme.html.

Performance and Assessment Reports (PANDA) are distributed annually to all schools in order to provide them guidance in self-evaluation, target setting and the development of plans to raise standards. PANDA reports contain information about schools and a summary of key performance data. These reports are not published for the public, but are distributed to the LEA and the DfEE.

Schools are encouraged to receive the best service value for the funds spent and are provided guidance on how to achieve this objective. Recently the DfEE established a research team (Value for Money Unit) to provide information to schools on how to assess their efficiency and effectiveness. Information about this activity can be found at http://www.dfee.gov.uk/vfm/index.shtml. The VfM Unit has suggested a number of indicators to help assess the value of the school. Categories of indicators include cost/efficiency, service delivery outcome, quality, and fair access. For a listing of indicators see Exhibit 1.

Recently, all LEAs are required to publish assessment test results and selected background information for all 11-year-old pupils in state schools. Some LEAs chose to provide additional supplementary data as well. This information can be found at http://www.dfee.gov.uk/performance/primary_00.htm.

In the last decade, England has established the Office for Standards in Education (OFSTED). The purpose of this agency is to inspect schools and LEAs. Starting in the past few years, schools are inspected every six years. OFSTED inspections and reports cover the educational and financial efficiency and effectiveness of a school. The inspection team reviews the goals and objectives of the LEA and individual school in the LEA and then ascertains the progress of the institution toward attaining those goals. OFSTED reports are made public and example can be found at the following website: http://www.ofsted.gov.uk/inspect/index.htm.

2.5 United States

2.5.1 Provision of Education

Under the United States Constitution, the federal government does not retain the authority to establish a national education system. Federal agencies ordinarily do not dictate school policies or curriculum for local schools. The responsibility for the provision of education rests with each state or territory, which then typically delegates most of the responsibility for the provision of education to local school districts. Each state has a state Board of Education. States determine the funding methods, teacher certification requirements, and certain policies that are followed by the local school districts. Local school districts typically have an elected board of education and superintendent who are responsible for making and executing local policies and carrying out all federal and state policies.

The source for most school funding is state and local taxes, with the state share slightly higher in recent years. Some funds may also come from the federal government, although these funds have proportionately decreased in recent years. Federal funds are often designated for particular programs. Various states have different funding formulas that are used to determine how much state funding a particular school district will receive.

2.5.2 Accountability

Although there has been recent interest by the federal government for instituting national assessment criteria, school and school district accountability remains the responsibility of the state and local government. The most common format used by states for providing school district performance information to the general public is the "report card." In most cases, report cards are issued by the state and made available by contacting state education agencies or through agency websites. The formats and information contained in the report cards are not consistent across states, and in a number of instances they are not comparable over time for the same state. A recent study analyzing information included on report cards found a wide range of reported measures (Education Week, 1999). In general, current state report cards have a primary emphasis on factors related to school environment and intellectual achievement, while less attention is paid to other characteristics found to relate to student performance such as family and peer groups. A summary of the report card study is found in Exhibit 2.

In addition to school report cards issued by states, schools and school districts may provide external constituents with performance information. The information reported is usually at the discretion of the school or district.

In order to obtain preliminary insights into the type of performance information made available by schools and districts, the websites of fifty public school districts and individual schools in these districts were examined. The schools and districts were selected from a list maintained by Web66 (http://web66.coled.umn.edu/schools.html). The examined websites were from schools and districts located in each of the fifty states (list is available from the author). For the purpose of describing the information contained on school and district websites, four categories of information are used. The first category is administrative information that includes items such as descriptive information, directories, event calendars, and announcements. A second category is public relations or publicity information. This category includes mission and vision statements, goals and policy statements. The third category is performance information. This includes information such as college entrance test scores, graduation rates, awards, and accreditation information. The final category is financial information, such as budget and expenditure data. Exhibit 3 summarizes the categories of information and the number of school districts or schools providing the specific information on their websites. District websites generally contained more of all types of information than websites for individual schools. Analysis of individual school websites suggests that high schools contain more information than the websites of schools for younger age children. The most common form of information reported on school and school district websites falls in either the administrative or public relations categories. The intended audience for most school websites appears to be the children and parents involved with the school. One conclusion from the analysis of school and school district websites is that they are used minimally as a means for providing performance information and are not being utilized as a means for conveying financial and efficiency information to constituents. Examples of web sites for representative school districts include Bay District Schools in Panama City, Florida (http://www.bay.k12.fl.us/) and Calcasieu Parish Schools in Louisiana (http://www.cpsb.org/). From these web sites, you are able to link to the web sits of the individual schools in these districts.

Beside schools and school districts providing performance information to interested parties, independent organizations are also becoming involved in reporting school performance information. For example, one independent organization developed a model of expected student achievement as measured by test scores using socio-economic characteristics of a school's student population (US News Online, 1999). Schools are categorized based upon the amount a school exceeded its expected performance results

In 1989, the Government Accounting Standards Board (GASB) in the United States published a study on the external reporting of service efforts and accomplishments (SEA) of elementary and secondary education (Hatry, Alexander and Fountain, 1989). As part of the study, the authors suggested information that would help interested parties evaluate the provision of educational services (Exhibit 4). The study contains suggestions for financial and non-financial measures of inputs, outputs, outcomes, and efficiency. The GASB report also emphasizes providing users with explanatory information as an important component for appropriate use of performance reports. The GASB report and subsequent Concept Statement Number 2 encourages schools administrators to experiment with SEA reporting (Government Accounting Standards Board, 1994). Although a significant amount of attention is being paid to performance reporting since the publication of the GASB report, it appears that only a limited number of these suggestions have been implemented by states and school districts. The next section reviews recent efforts toward providing educational accountability information.

3. COMPARISON OF EDUCATIONAL ACCOUNTABILITY REPORTING AMONG THE SELECTED COUNTRIES

Although this article reviews educational accountability reporting in five countries, it allows for the following insights. First, methods of financing education vary even in countries with similar forms of government and living standards. In some instances the central government is largely responsible for financing education and in others the state and local government are primarily responsible for school funding. The methods of financing schools may well have an impact on the process of accountability reporting and the content and format of the reports. If most school funding is coming from a single source, such as the central government, then it is more likely that accountability reporting can be mandated for all schools or school districts and the reports are likely to be more consistent or standardized.

Both New Zealand and the UK, countries with a major portion of educational funding provided by the central government, have recently instituted national accountability review processes. The accountability reviews in both of these countries is extensive and to a large degree considers the individual environment and objectives of the school or district. The United States, Canada, and Australia, countries where local governments have a substantial responsibility for funding education, have not instituted national accountability reporting. Although in many instances local or state governments have adopted some form of performance reporting, it has not been consistent across jurisdictions. In these countries, the central government has performed to a greater extent the role of facilitator, which is bringing the various education providers together to obtain agreement on standards and reporting methods.

A second observation is that accountability and performance reporting is receiving considerably more attention in the past decade compared to prior periods of time. Most accountability reports and reviews have been instituted in their respective countries in the past few years. For example, in England the inspection reports from the Office of Standards in Education have yet to complete a reporting cycle for all schools. In the United States, school report cards have only been provided by most states for a few years. In most countries there are continued efforts toward improving the information received by constituents on education investments and this is expected to remain the case in the future.

A final observation is that the uses and users of educational performance and accountability reports are not clearly articulated in many instances. For example, in countries where education is funded by the central government, central government administrators and legislators for top-down decision-making may directly use the information contained in performance reports. An alternative use for these reports is for students' parents and taxpayers to use the information to determine the performance of schools and then lobby decision-makers for any changes that they believe are appropriate to improve schools and districts. The format and content of reports should reflect the intended uses and users for such reports in order for the reports to be effective and cost beneficial. In countries where education is mostly locally funded, similar issues arise about the intended audience for performance and accountability information. In these countries ascertaining the intended use of performance and accountability reports may be even more difficult because each state or local jurisdiction decides on the report form and content.

4. EVALUATION OF THE CURRENT STATUS OF EDUCATIONAL ACCOUNTABILITY REPORTING

Although many countries and most states in the U.S. require schools and school districts to make performance and accountability reports available to constituents, a variety of weaknesses remain with these reports. One problem with current education performance reports is the lack of information comparability between schools located in different countries as well as schools within the countries. Performance reports differ considerably in both content and format. The content variability of performance reports is likely caused by the lack of agreement on the key characteristics of schools to measure. An examination of the current research evidence suggests that student achievement is generally associated with broad dimensions such as family influences, peer groups and the school environment (Hanushek, 1997). But, education researchers continue debating specific measures that capture these dimensions, thereby creating the variability in reported information.

Another content problem with school performance reports is the lack of efficiency measures provided by schools. Although the GASB and England's Department for Education and Employment report on Value for Money recommend that school districts offer constituents measures relating inputs to outputs, it is difficult to find schools or school districts providing such measures.

The design and quality of information systems also presents a problem in education performance reporting. The variability in system design and quality may cause schools and districts to report information in a non-comparable and inconsistent manner. For example, there is no assurance in performance reports that all school districts in a country or state are similarly computing a measure, such as drop out rate. Also, there is typically no assurance that the measure is computed in the same way by the same school district from one period to the next.

Another problem of educational accountability reports is the desire by some providers and users of these reports to have a single aggregate measure of performance in order to reduce their information processing costs. This is particularly evident in some state report cards in the US. The difficulty in providing an overall aggregate measure of school performance is the validity of the process used to aggregate the information and the possible misinterpretation of such data. Just as income is determined and interpreted a number of ways for a business, multiple interpretations of aggregate grades or scores for schools and school districts is likely to occur for users of school performance reports.

The integrity of the information contained in educational accountability reports presents another problem. A survey conducted in the United States about the credibility of different sources of accountability information indicated that only nonprofit watchdog organizations were rated as highly credible by parents, taxpayers, and educators (A-Plus Communications, 1999). This suggests that users are sensitive to the source of the information. If users are to rely on the quality of the information contained in the reports for decision-making, then they require assurances that the information is accurate and unbiased.

A final problem related to educational accountability reports is one of format and implementation. Users need to be made aware of the reports and how to properly analyze and act on the information contained in the reports. Reports can be too brief with highly aggregated information and little detail or may be lengthy and overloaded with statistics and other information. In either instance, the accountability report may be of little use to those responsible for analyzing the reports and making decisions. Information intended to hold schools accountable is only useful if the audience for the reports has the ability to properly and efficiently assess the information and make appropriate decisions.

5. IMPROVING EDUCATIONAL ACCOUNTABILITY INFORMATION

One implementation problem for school accountability reporting may be the lack of consensus regarding the education production function and associated difficulties with measurement. An articulated relationship between educational inputs, outputs, and outcomes is certainly a significant factor in providing educational accountability reports. Additional research and experimentation with measures of these constructs, especially efficiency measures, is also a critical task. Although the continual research focus on the key factors in educational productivity is important for educational accountability reporting, other issues also need resolution.

Some of the problems related to educational accountability reporting are systemic because the environment in which the information is supplied and demanded potentially needs to change. If the perceived benefits of educational accountability reports increase in relation to the cost of providing these reports, then the supply and demand for these reports should increase. If government overseers, taxpayers, parents, and other interested constituents request and appropriately use performance and accountability reports in the decision-making process, then responsible officials will likely be motivated to provide this information. A comprehensive program to inform and educate users about educational accountability information may help to address this issue.

In order for change to take place in the environment in which educational accountability is used, it is usually more effective for coalitions or groups of constituents rather than individuals to successfully motivate school officials to provide newly requested information. An appropriate environment is necessary for the groups to successfully form. This includes a method for similar constituents to identify one another and to communicate. Already established organizations (such as a parent organization or taxpayer watchdog group), websites, and the media are useful in helping to foster the growth and activity of coalitions of educational information stakeholders. These coalitions and groups can effectively request accountability information from schools by negotiating with current elected or appointed school officials, or by supporting the election of school officials willing to help with the provision of accountability information.

Another issue that needs to be addressed to improve educational performance reporting is sufficient funding for informational activities. Constituents need to request that school budgets contain an appropriate amount of funds for the development of quality information systems to gather the required data and the means to adequately disseminate school accountability reports. Sufficient funding increases the likelihood that quality performance information is available to users.

In order for accountability information to be reliable, constituents should request that audits be performed on accountability reports. Information can only help improve performance if users believe that the information is unbiased, timely, credible and accurate. Audits can be an important tool for increasing the credibility of educational accountability information.

Finally, users need the ability to compare educational accountability information over time for the same school or district, as well as between schools and districts.

User groups need to establish databases of benchmarking information to improve the decision-making capability of users.

6. CONCLUDING COMMENTS

Governments are increasing their efforts in educational performance reporting. While the form and content of accountability reports may vary by government because of the processes of funding and providing educational services, all governments need to assess educational investments. Educational accountability can be either top-down or bottom-up, both processes require similar information regarding the inputs, outputs, outcomes and efficiency of the educational process. Both forms of accountability can benefit from improved information. Increasing the constituent demand for information, as well as allocating additional resources to the development of this information enhance the likelihood for better educational accountability information. The creation and enhancement of existing coalitions of education constituents also increases the possibility that this will occur.

EXHIBIT 1

The Education Best Value Performance Indicators for 2000-2001

Cost/Efficiency

1 31 Individual schools budget as a percentage of local schools budget.
2 32 Expenditure on adult education per head of adult population.
3 33 Youth Service expenditure per head of population in the Youth Service target age range.
4 34a Percentage of primary schools with 25% or more of their places unfilled.
5 34b Percentage of secondary schools with 25% or more of their places unfilled.
6 35a Surplus places in all primary schools as a percentage of the total school capacity.
7 35b Surplus places in all secondary schools as a percentage of the total school capacity.
8 36a Expenditure per pupil in local education authority schools in respect of nursery and primary pupils aged under five.
9 36b Expenditure per pupil in local education authority schools in respect of primary pupils aged five and over.
10 36c Expenditure per pupil in local education authority schools in respect of secondary pupils aged under 16.
11 36d Expenditure per pupil in local education authority schools in respect of secondary pupils aged 16 or over.

Service Delivery Outcome

12 30 Percentage of 3-year-olds who have access to a good quality free early years education place in the voluntary, private or maintained sectors.

13 37 Average GCSE/GNVQ points score of 15 year olds pupils in schools maintained by the local education authority.
14 38 Percentage of 15 year old pupils in schools maintained by the local education authority achieving five or more GCSEs at grades A* to C or equivalent.
15 39 Percentage of 15 year old pupils in schools maintained by the local education authority achieving one or more GCSEs at grades A* to G or equivalent.
16 40 Percentage of pupils in schools maintained by the local education authority achieving Level 4 or above in the Key Stage 2 Mathematics test.
17 41 Percentage of pupils in schools maintained by the local education authority achieving Level 4 or above in the Key Stage 2 English test.

Quality

18 42 Enrolments on adult education courses per 1000 adult population.
19 43a Percentage of statements of special educational need issued by the authority in a financial year and prepared within 18 weeks, excluding exception cases.
20 43b Percentage of statements of special educational need issued by the authority in a financial year and prepared within 18 weeks.

Fair Access

21 44a Number of pupils permanently excluded during the year from primary schools maintained by the local education authority per 1000 pupils at primary schools.
22 44b Number of pupils permanently excluded during the year from secondary schools maintained by the local education authority per 1000 pupils at secondary schools.
23 44c Number of pupils permanently excluded during the year from special schools maintained by the local education authority per 1000 pupils at special schools.
24 45 Percentage of half days missed due to unauthorised absence in primary schools maintained by the local education authority but excluding special schools.
25 46 Percentage of half days missed due to unauthorised absence in secondary schools maintained by the local education authority but excluding special schools.
26 47 Percentage of schools maintained by the local education authority with serious weakness.
27 48 Percentage of schools maintained by the local education authority subject to special measures.

EXHIBIT 2

Summary of Education Week Study of School Report Cards

Dimension	Attribute	N° of states including attribute in report card (%)
Publishing and Disseminating	Does the state have an annual report card on each of its schools?	36* (100%)
	Does the state make all the school report cards available on its web site?	26 (72)
	Does the state require the school report cards to be sent home?	13 (26)
Comparing student performance	National average	17 (47)
	State average	25 (69)
	District average	20 (56)
	Previous year	25 (69)
	Scores in similar schools or districts	9 (25)
	Scores predicted by student demographics	3 (8)
	Scores in top-performing schools	1 (3)
Academics and achievement	Test scores	36 (100)
	Graduation rate	24 (67)
	Dropout rate	33 (92)
	AP courses or tests	14 (39)
	Course-taking	11 (31)
	SAT/ACT data	20 (56)
	Post secondary plans/experiences	15 (42)
Students	Student characteristics	23 (64)
	Student mobility	12 (33)
Teachers, resources and school climate	Teacher qualifications	16 (44)
	Salaries or other financial data	17 (47)
	Safety of discipline	17 (47)
	Class size/pupil-teacher ratio	20 (56)
	Student attendance	30 (83)
	Parent involvement	11 (31)
	Satisfaction/opinion data	5 (14)
Other information about school	Accountability rating	9 (25)
	Description of programs/philosophy	15 (42)

* Five additional states will have reports starting in 2000 or 2001. Six other states provide individual school test score results.

EXHIBIT 3

Information Reported on School and School District Websites

Type of Information Reported	Number of District (n=50)	Number of Schools High	Middle	Elementary
Administrative				
Calendar of events	26	25	20	19
Contact information	25	23	23	20
Description of school or district	16	10	11	16
Description of curriculum	12	11		2
Announcements	17	19		11
Meal menus	11		1	12
Athletic and extracurricular event schedules	11	22	14	
Public Relations				
Mission or vision statements	22	1	14	16
Goals and beliefs	10			
Policy statements	10			
Technology initiatives				9
Principal's message				11
Employee profiles			12	
Student/Parent newsletters	10	7	12	
Alumni news and contacts	7	9		
Employment opportunities	18			
Performance				
College entrance test scores	9	13		
Graduation rates	10			
Test results			1	
Awards	12	4	7	7
Curriculum projects				6
Scholarship recipients	3			
Enrollment information	10		6	5
Accreditation information	7	6		
Financial				
Budgets	3			
Expenditure information	4			

EXHIBIT 4

GASB report suggestions on Information for School Performance Reports

COMPONENT	MEASURE
Inputs	Expenditures
	Total number of personnel
Outputs	Number of student-days
	Number of students promoted
	Carnegie units as percentage requirement
	Absenteeism rate
	Dropout rate and/or retention
Outcomes	Types of tests
	Test scores by major area
	Measure of gain on achievement test
	Measure of self-esteem
	Measure of physical fitness
	Measure of post-grad employment/education
	Self-assessment by students of skills
	Parent assessment of student skills
Efficiency (input to output or outcome)	Cost per student (student, student-day)
	Cost per outcome (cost per achieve.)
	Cost/program
	Cost/school
Explanatory Data	*Controllable*
	Class Size or pupil/teacher ratio
	Non-controllable
	Attendance
	Measure of minority students
	Measure of student on reduced lunch
	Measure of need for remedial programs
	Student mobility rate measure
	English as a second language
	Student enrollment

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AAD D. BAC

AN ANALYSIS OF THE ARISE OF AUDITING INSTITUTIONS IN THE DUTCH PROVINCIAL AND LOCAL GOVERNMENTS

1. INTRODUCTION

The subject of Auditing Institutions on the provincial and local government level is increasingly claiming attention in the Netherlands. In a number of municipalities a certain type of instituting such bodies has been realised. A number of municipalities and provinces are considering doing so. A committee appointed by the Minister of Interior Affairs and Kingdom Relationships dealing with the public law arrangements regarding to lower governments has expressed interest in the importance of such institutions for public administration and accountability. The Minister is considering legislation on this topic directed at a mandatory introduction of such institutions for all municipalities and provinces.

This phenomenon is an incentive to ask a number of questions such as:
- why such needs are felt;
- what ways of answering the needs are being seen;
- what a comparison of chosen solutions shows;
- what limitations are encountered;
- what solutions are at hand for smaller municipalities;
- which legislation is considered to institutionalise this type of supervision?

This paper enters into these questions from several perspectives such as:
- the public law status of these institutions in comparison with the Dutch Court of Audit at the central government level;
- the place of such institutions in public administration and especially in the accountability chain in comparison with the requirements of adequate accountability;
- the relationship between these institutions and financial audit as existing.

In order to reach the goal of this paper it will start with the accountability required, followed by a preliminary insight in the Dutch constitutional system in public law. Thereafter it will deal with a view on the desirable monitoring of the accountability process and the function of such institutions. The next part of the paper will deal with an inventory of variants already seen and possibilities for

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 319-330.

smaller governments to reach the same or at least comparable effects. At the end an evaluation of considered legislation in this area would be given.

2. ACCOUNTABILITY OF PROVINCIAL AND MUNICIPAL GOVERNMENTS

The accountability process traditionally attracting the most attention is the financial accountability in which the financial statements take a central place. Especially in the private sector this will be an adequate way of accountability, because the accountability in the private sector has a dominant financial character, where the primary goal of an enterprise will be financial success. As far as the public sector is concerned some remarks have to be made.

In the first place the public sector in contrast to the private sector also publishes its extensive budget. The budget too is an example of rendering account being it about the allocate-choices that have been made in advance with respect to the resources available for a certain budget-year. In appropriating the budget items, authorisation is given for the active spending of public resources. Thus the budget is starting to function as the regulating instrument for the management and control of public spending. This is the primary reason why appropriated amounts are an explicit part of the financial accounts because accountability also comprises budget compliance.

In the second place in the public sector success usually cannot be measured in financial terms but in policy-effects and not in general but per policy-area. This offers clues to efficiency as well as effectiveness questions, which can be asked to policy-execution and policy as such. In the ideal situation the notes to the financial statements would contain information on efficiency ands effectiveness too. A functional presentation of the accounts according to a functional budget is the natural form of such accounts. The possibilities to present this type of information together with the financial accounts are regretfully limited.

As far as accountability on policy and policy-effects is concerned Dutch public administration traditionally uses the instrument of periodic policy-reports. These reports are made up and presented to the elected representatives in the municipal council and the provincial parliament with a frequency of more than one year and sometimes several years, depending on the political dynamics attributed to the applicable policy-area. A general disadvantage of these policy-reports is that they contain as well information ex post referring to policy execution in the past with an accountability character, as information ex ante with respect to the desired continuation of the policy in the future with a pleading character. A useful recommendation would be that these two types of information would be explicitly differentiated between and visibly divided in these reports. This would support the policy-reconsideration function of these reports and contribute to the transparent presentation of the decisions at stake when these reports are tabled in the municipal council or the provincial parliament.

The financial accountability track and the policy accountability track thus have their own dynamics. The financial accountability has a fixed frequency of once every year. As far as the policy accountability is concerned a variable frequency of different numbers of years per policy area is used. This implies a risk that the comprehensiveness of overall accountability over time is not sure. It is especially not sure that over time every policy area will come at stake, some policy areas may be "forgotten". This circumstance demands for measures, directly safeguarding such will not happen. A recommendation to explicitly mention in the notes to the financial statements for every policy-area (budget-item),from which date the last policy-report dates and with which frequency the next may be awaited. Thus an important contribution to control over the comprehensiveness of accountability will be delivered.

3. DUTCH PUBLIC LAW ON ACCOUNTABILITY AND AUDITING

The Netherlands is a so-called decentralised unitary state. This implies an autonomous position for provinces and municipalities to such an extent that only national legislation that concerns policy surpassing the geographical area over which a lower government has authority can limit the freedom of policy of lower governments. Central government can demand co-government from lower governments if the execution of central governments policy makes such necessary, which will normally imply special funding of such activities. This relatively autonomous position which is laid down in the Dutch constitution implies a reluctant supervisory role of central government on lower governments. So administrative supervision is limited to the soundness of financial management of lower government, concentrating itself on balancing budgets. Until now municipalities and provinces have a so-called monistic (one-tier) system in which the Executive makes part of the elected Municipal Council or Provincial Parliament. The according to our constitution crown-appointed Mayor and provincial Commissioner of the Queen are exceptions. In this system given the autonomous position the Executive accounts to the Municipal Council respectively the Provincial Parliament, although the Executive have the right as elected members to vote on their own accountability. Therefore the system needs completion by means of administrative supervision, which takes their constitutional position into account.

Supervision on municipalities is attributed to the Executive of the provinces and supervision on provinces is attributed to the Minister of Interior Affairs and Kingdom Relationships. Supervision on the execution of co-government is attributed to central government in the specific laws in which the lower government is called in co-government. Supervision on central government cannot be attributed to a higher government level because there is none. That is why at the central government level the Netherlands has a dualistic (two-tier) system in which there is a complete division between government (the Queen and her Ministers) at one side and Parliament and the Senate as two chambers of the elected representatives of the people. Parliament is supported in their supervisory role by an independent Court of Audit, of which the independence is arranged in the constitution and because of that circumstance of a very strong character. Because of their constitutional position the court of audit has no authority over provinces and municipalities.

In line with the administrative structure at the central government level the Court of Audit has a role as the external auditor of the central governments' financial statements as well as a role as an administrative supervisor of central governments' policy-execution. The Court of Audit's independence is assured by means of regulating its position in the Constitution, the strongest instrument in public law.

This implies that from the Court of Audit come

- opinions and reports on the fairness of the financial accounts;
- opinions and reports on the legality of financial management;
- opinions and reports on the efficiency of policy-execution;
- opinions and reports on the effectiveness of policy.

The court of audit will never express opinions on the content of policy leaving this to democratic bodies and neither on uncompleted policy. The Court of Audit always hears a responsible minister before reporting but will always retain the right to decide afterwards whether to report and in what way.

4. MONITORING OF THE ACCOUNTABILITY PROCESS

The actual way of dealing with accountability documents in the Municipal Council and the Provincial Parliament is as follows. As far as the financial accountability track is concerned discussions and decision-making is prepared by the Accounts Committee of the Council or the Parliament. The Committees for Advice and Support of the Council and the Parliament on the other hand prepare discussions and decision-making with respect to the policy accountability track.

As far as reasonable expectations and possible improvements of the discharging process is concerned the following comments on the actual procedures can be made: An Accounts Committee may have the assignment to supervise and monitor that new policy reports really are published with the frequency and at moments in time as planned. Thus the Accounts Committee takes up the role of the guardian of the comprehensiveness of the accountability process and receives a new impulse.

To the extent that budget and financial accounts also provide compact information on efficiency and effectiveness it is logic to table them in the applicable Committees for Advice and Support. In this way political supervision on the policy execution accounted for in the financial accounts is made possible. In the period in between publishing of successive policy reports such limited accountability complementary with and going in advance of a more comprehensive accountability may fulfil a useful role, especially because the period between two successive policy reports may be several years. Thus representatives retain sight on the complete- this means financial as well as policy- accountability process. Auditors can afford assurance on the reliability of accountability information. As far as financial statements is concerned this is already mandatory by law. As far as the policy reports is concerned such could be considered.

In some cases common meetings are organised, of the Accounts Committee and a Committee for Advice and Support in a certain policy area. Such in order to discuss in preparation of the discharging process in the Municipal council or Provincial Parliament the financial accounts as such as well as the policy aspects behind them concurrently. Practice has shown in the past that members of Accounts Committees, although at other moments also members of some Committee for Advice and Support, are positively surprising able to act a-political and neutral in their special role as members of the Accounts Committees. When they are acting as members of the Accounts Committee and confronted with political comments of their colleague members of Council or Parliament, although the latter are then acting as members of Committees of Advice and Support rightfully are entering in policy aspects. The purity of their functioning is much more served when such committees are meeting separately. Members of Accounts Committees realise themselves very well that their role as a guardian of the accountability process requires an objective approach. This non-partisan method of working very much contributes to the preparatory and monitoring role with respect to the quality improvement of the accountability process.

The policy aspects in the accountability process, as well intermediate at the occasion of and in addition to the financial discharge as periodically at the occasion of tabled policy reports need on the contrary not to be dealt with a-politically and non-partisan. The culture in Committees for Advice and Support therefore is a very suitable one. These committees judge from the content of a policy area.

From this point of view common meetings are less likely to be useful.

5. THE DESIRABILITY OF AUDITING INSTITUTIONS AND MANIFESTATIONS OF THIS PHENOMENON

Society is served with every strengthening of the quality of the accountability process. It was concluded that the accountability process in government organisations consists of two tracks with different purposes and different dynamics and which nevertheless very much are two aspects of the comprehensive accountability that the public sector requires. The question this paper is dealing with is whether the installation of a local or provincial Auditing Institution can contribute thereto or is necessary therefore.

The Dutch public sector has known mandatory financial audit for the provincial and municipal governments for numbers of decades now. Rather recently the legislation has additionally obliged auditors to pay attention to efficiency matters in their long form reports on the financial accounts. It is clear that this cannot cover the overall activities of municipalities and provinces in every year. That is why the attention for efficiency matters is limited in two ways:

- It is not supposed to be as comprehensive as is expected from the traditional opinion on the financial statements, although of course all information making part of the explanatory notes fully is part of the auditor's responsibility. But the legislation does not point only at the information on efficiency, but expects comments on the efficiency as such too and it is clear that comprehensiveness there cannot be realised every year.
- As far as judgements on efficiency as such are concerned the legislator has recognised that no general standards for efficiency are at hand. In order to be sure to imply legislation of which compliance will really be possible, the legislation only demands from the auditor to comment on the systems governmental management has put in place to get and to remain in control of efficiency matters.

This scope of the financial audit affords enough support in the financial accountability track.

As far as the policy accountability track is concerned a comparable support for the discharging authority is needed. Now that the attention for accountability in a broad sense is winning interest it is logic that the need for professional support in this area is increasing. Local and provincial Auditing Institutions may satisfy such needs. Especially as far as policy accountability and the effectiveness aspects is concerned there is a need for evaluation of policy and deeper investigation of efficiency matters also entering into questions concerning the level of efficiency reached. This would complete the accountability infrastructure in the public sector. Practice shows that an increasing number of especially municipalities have, in the recent years, developed initiatives directed at improvement of the attention for these matters and instrumented the support of that.

The manifestations of such initiatives are diverse. Especially the fact is interesting that although many municipalities are expanding auditing type of activities around the policy accountability track, different structures are used in doing so.

- In some municipalities the existing Accounts Committee has been given a wider mandate and is expected to pay attention to a limited number of topics esteemed te be worthwhile an investigation or just a policy-evaluation.
- In other municipalities a new Committee is installed with a separate mandate to pay attention to evaluations and policy-audits. In some cases the committee consists not only of council-members but also a limited number of external members or experts.
- In one case, the municipality of Rotterdam instituted a local Auditing Institute, not being a committee from the council, but headed by a director who is appointed by the Municipal Council and fully independent from the bureaucratic organisation.

Because of this variety in manifestations it may be better to preliminarily speak of Auditing Institution Facilities and an Auditing-Institution-function.

It has to be concluded that independence, comparable to the national Court of Audit laid down in the Constitution is unreachable for a Local Auditing Institution.

6. THE STATE OF THE ART OF THE AUDITING-INSTITUTION FUNCTION

An investigation of 1999 among the 25 largest municipalities in the Netherlands shows the following facts:

- 13 larger municipalities have already implemented some manifestation of a local 'Auditing-Institution-function'

  9 larger municipalities were discussing whether to introduce a local "Auditing-Institution-function"

  3 larger municipalities were at that time not yet considering such introduction Since than some of these have started discussions and some have already decided to join the first group
- The 13 as above have as their special responsibility area efficiency of activities; only 8 of them look also after the lawfulness of expenditure.

12 of them have predominantly an auditing role of which 6 combine this with a role in policy development. Only one is only dealing with policy-development matters.

- In all 13 cases members are appointed by Council and cannot be members of the Executive.
  In 8 cases members are only recruited from council-members whilst in 5 cases members come (also) from other sources for example from experts.
- The chairperson of the Auditing Institution Facility will be appointed by Council in 7 cases and by the Auditing Institution Facility itself in 6 cases. In all cases the chairperson cannot be a member of the Executive.
  The chairperson comes from outside the Council in 2 cases.
- As far as pre-selection of subjects is concerned there is a wide variety:
  in 9 cases the Auditing Institution selects on its own
  in 2 cases Council is involved too
  in 4 cases the Executive is involved too
  in 3 cases the procedure is even different from the former ones
- Definitive selection of subjects is only in 4 cases done by the Auditing Institution Facility itself. In 11 cases, this is done by Council. In 2 cases Council as well as the Auditing Institution Facility can decide to subjects to be dealt with.
- The allowed number of investigations per year is
  in 6 cases unlimited
  in 2 cases limited to 2 or 3
  in 1 case limited to 2
  in 4 cases limited to 1
- The available budget varies from Euro 0,11 to 0,82 per inhabitant
- Realised investigations in 1988 varied also:
  0 (in 1 case),
  1 (in 8 cases),
  2 (in 3 cases) and
  3 (in 1 case).
- The name of the Auditing Institution Facility also varied importantly like:
  (Local) or (Municipal) Auditing Institution (5 cases)
  Auditing Committee (3 cases)
  Committee for effectiveness-investigation (1 case)
  Committee for Financial Management Affairs (1 case)
  in 4 cases the committee is still called Accounts Committee and here the new initiative has been implied by enlarging the mandate of this committee.
- In the majority of cases (10) investigations are executed with external support. In 6 cases this can also be bureaucratic support and in 1 case this is only by means of bureaucratic support. The case of Rotterdam is very special and is best characterised as completely on its own. This is because of the independently institutionalised form because of course nothing withholds the possibility to contract out some assignments here too.
- In 7 cases the Auditing Institution Facility is obliged to hear the audited entities. In 5 cases a request for comment has to be done to the Executive or

Committees for Advice and Support from Council. In 1 case both is applicable and in 1 case nothing of the kind has been arranged for.

The research aforementioned did not address municipalities smaller than 100.000 inhabitants but among this kind of municipalities number of initiatives can be found. All these initiatives have in common that they are all of an experimental character. A general best practice type of Auditing Institution Facility has not been defined and it is even doubtful whether it will be possible to reach that stage, just because of the important differences in size that we see among municipalities.

Although this research concerned larger municipalities seminars with elected representatives and officials in 2000 has proved out that a large number of less large cities are also experimenting with this subject. It is however clear that the small municipalities will have serious trouble in instituting Auditing Institution Facilities because of the constraints coming from their size. In these seminars we have advised them to consider the slimmest model of extension of the mandate of the Accounts Committee, together with occasional support of external experts and contracting out of the investigations to be executed.

As far as provinces is concerned in recent years 6 out of the 12 provinces have installed Committees for Policy Evaluation, also with different names. Very recently a committee of IPO ("inter-provincial-consultation", a body in which all the provinces are preparing their collective communication with central government) has produced a draft for a common model of Provincial Auditing Institutions.

For municipalities such is not yet the case. It could be useful to define some minimum conditions to which all (experimental) solutions should answer in order to adequately contribute to the strengthening of the accountability process. An Audit Institution Facility should in the first place have a minimal scale to permit an institutionalised structure. That is why the Rotterdam model until now has remained unique.

To solve this problem the suggestion has been made to choose for supra-local solutions for example by means of

- voluntary co-operation between neighbouring municipalities (the bottom-up variant) or;
- by means of by law instituted so-called Regional Auditing Institutions (the top-down variant) or;
- by "buying" services from the Auditing Institution of a large neighbouring municipality (the sideways variant).

The top-down variant does not fit in with the constitutional structure of public administration in the Netherlands (although we will later see that the Ministry of Interior Affairs and Kingdom Relationships is eriosly considering this option).

The bottom-up and the sideways variant do not have this objection and would therefore be possible. They have the disadvantage that the programming authority would pass the borders of the administrative entity, which could be conflicting with the spirit of the Constitution because it sacrifices the autonomy.

It should not be forgotten that a serious possibility remains in the option to enlarge the mandate of the Accounts Committee of Council. This remains at least an option in that situation in which it is accepted that in autonomous municipalities and provinces the comprehensive responsibility for accountability and discharging remains to be the unlimited authority of the Municipal Council or Provincial Parliament.

Whatever type one chooses, some requirements have to be met always. These are the authorities, which have to safeguard the highest level of independence possible:
- the independent authority of programming (the selection of subjects to investigate);
- the independent authority of investigation (no limitations with respect to the scope of investigations and neither with respect to access of information);
- the independent authority to decide what and how to report.

During the year 2000 a number of seminars on this subject have been organised in which a presentation of the above described topics has been made and discussions been held with an audience of about 60 % elected representatives and 40 % bureaucrats. Questioning the audience proved out that:
- 15 % came from municipalities with some type of an Auditing Institution Function;
- 27 % came from municipalities, which have extended the mandate of the Accounts Committee to policy matters;
- 19 % came from municipalities, where in the policy program of the Executive a paragraph is mentioned about the organisation of the supervisory function;
- 10 % came from municipalities, where this has also been materialised in a description of the organisational structure;
- 38 % came from municipalities, where the intention was existing to create some type of an Auditing-Institution Function within one year.

Although the population of this group has been predetermined towards the subject, because a special interest in the subject may be expected for people subscribing to such seminars the answers to the questions raised indicate a very wide interest in the topic in the municipalities.

7. LEGISLATION IN DEVELOPMENT

During the year 2000 a special State Committee installed by the Minister of Interior Affairs and Kingdom Relationships dealing with the assignment to report on the subject 'Dualism and Local Democracy' published its report. This report amongst other recommendations contained the advice to consider whether the implementation of some type of an Auditing-Institution Function could be useful. The first reaction of Parliament was a widespread opinion that it was not desirable yet to oblige municipalities and provinces to institutionalise such function in one and only legislative model.

Nevertheless the official point of view of the Council of Ministers went into this direction. It was of the opinion that such an Auditing Institution is an indispensable institution that has to be prescribed to be mandatory. The reasons of the Cabinet were the following:
- Local Auditing Institutions strengthen the position of the Municipal Council and Provincial Parliament with regard to the execution of their supervisory role.

- The attention for and the importance of efficiency and effectiveness is increasing; citizens are increasingly judging government thereon.
- A further improvement of the test on lawfulness and efficiency is desirable.
- The reports of Local Auditing Institutions constitute a good starting point for accountability to citizens.

Reason enough to analyse this dilemma.

At first an overview of the draft legislation is given. In order to keep everything simple only the intended changes in the Municipal Law will be given, the changes in the Provincial Law will be comparative.

- Every municipality will have an Auditing Institution consisting of three persons.
- The mandate of the Auditing Institution, will primarily concentrate on efficiency and effectiveness matters. The financial auditor of the municipality will have a mandate concentrating on a fair view of the financial statements, compliance to the Accounting Rules and the lawfulness of income and expenditure.
- The Municipal Council will appoint and dismiss (in a limited number of cases) the members as well as the chairperson and may appoint deputy members and can re-appoint members.
- The Council will consult the Auditing Institution before appointing new members.
- The Law names a number of positions, which are esteemed to be incompatible with membership.
- Members accept appointment under oath.
- The Auditing Institution will make its own by-law of order.
- The Auditing Institution may impose secrecy, which ends not earlier than the Auditing Institution decides so.
- The Council affords to the Auditing Institution the resources it needs for an adequate execution of its task.
- On nomination by the chairperson of the Auditing Institution the Executive of the municipality will appoint sufficient officials on behalf of the Auditing Institution as necessary for an adequate execution of its task.
- The officials working on behalf of the Auditing Institution will not also perform tasks on behalf of the Council, the Executive, the Mayor or committees from council.
- Officials working on behalf of the Auditing Institution are with respect to such tasks only accountable to the Auditing Institution.
- Members of the Auditing Institution will receive compensation for their work as well as for their cost.

For this part the legislation seems to be solid. More problematic is the possibility, which the draft legislation is intending to open, to have some municipalities to institute a common Auditing Institution. This has the disadvantage that the Auditing Institution will be experienced as something from outside the municipality. This may be endangering the fact, that Municipal Councils will not give the same attention to their reports as would be the case if it would have been their 'own' Auditing Institution.

8. CONCLUSIONS

The comprehensiveness of accountability in the public sector is in danger because of the fact that two different accountability processes (a financial accountability track and a policy accountability track) are in use separated from each other. It would be useful to interrelate these two tracks by means of mentioning in the notes to the financial accounts for every policy area what the date and identification of the last policy report is and when the next may be expected.

Policy reports contain as well accountability information as pleading information. It is recommended to formulate formats for policy reports directed at a clear separation of these two types of information in order to contribute to the accountability quality in the policy accountability track.

Accountability is much more an attitude than only compliance to rules. This goes for holding accountable as well.

The increasing attention of elected representatives for some type of an Auditing Institution Function shows a start of realisation of this attitude.

Experimenting (with the way in which Council-members want to give exposure to their interest in efficiency and effectiveness matters in the financial accountability track at one hand and in the policy accountability track on the other hand) promotes the development of the accountability attitude towards the electorate and towards their responsibility to hold the Executive and the officials accountable.

Independence of a Local Auditing Institution will impossibly reach the same level as is the case with the national Court of Audit because this Court's position is regulated in the Constitution.

Legislation in a primary stage of development of an accountability attitude may kill the inclination to self-development and thus be disadvantageous to the quality of accountability awareness at the end of the day.

The intended legislation cannot be criticised as far as its solidity is concerned. An exception must be made as far as the possibility of so-called Common Auditing Institutions is concerned. Such institutions risk to be experienced as too far away from the local accountability process and thus miss its contribution to this accountability process. Such institutions have at least a semblance of conflict with the spirit of the Constitution.

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MARY BOWERMAN
CHRISTOPHER HUMPHREY

LIMITING THE SCOPE OF CENTRAL GOVERNMENT AUDIT: A CONSTITUTIONAL PROBLEM OR A SENSIBLE SOLUTION?

1. INTRODUCTION

A comprehensive system of performance measurement for all UK central government departments was introduced in 1998. Each department now has 'high level and focused commitments' or Public Service Agreements (PSAs) with the Treasury plus detailed departmental targets (Service Delivery Agreements or SDAs). Each PSA includes statements of central government departmental aims and objectives, allocated resources, key performance targets and details of how departments propose to increase the productivity of their operations (see Cm 4181 1998).

Within this system, the question of whether performance information should be validated (and who should do it) has been the subject of intense debate. The National Audit Office (NAO) has wanted its role to be extended to include the routine audit of PSAs so as to provide Parliament with independent assurance that departments have used the monies voted to them for the purpose intended. The government, however, has taken the view that a formal role for an external auditing body would be very resource intensive with doubtful benefits either for transparency or the robustness of the data (HM Treasury Select Committee 1999, response to q. 188). The NAO received significant support for its position from two influential parliamentary committees (see HM Treasury Select Committee 1999, 2001); Public Accounts Committee 2000), leading the government to propose a compromise arrangement whereby the NAO will be responsible for ensuring that data systems that are crucial to the measurement of PSA targets systems are reviewed during their "lifetime" - normally once every three years (see HM Treasury 2002). This will not involve a change to the NAO's existing powers and need not involve the NAO in undertaking reviews themselves. Rather they have been advised to rely on 'wider expertise, drawing on the work and recognising the independence and authority of the Audit Commission, The National Statistician and the Statistics Commission' (HM Treasury 2002, p. 22). The government's position reflects the view laid down in an independent review of central government audit and accountability, although the review did see external validation of departmental information systems as a 'first

V. Montesinos and J.M. Vela (eds.), Innovations in Governmental Accounting, 331-341.

step' in the process of validating key published data, rather than an end in itself (see Sharman 2001, p. 39).

As the government's decision will not necessitate a change in the NAO's existing powers and will not see the direct validation or audit of the performance measures being generated by PSAs, it is tempting to see the decision as a set-back or hollow victory for the NAO; a case of the government unduly controlling or restricting the remit of the 'independent' public auditor. However, we would argue that this is not the case and that the decision is a sensible one, reflecting both audit traditions internationally and acknowledging, albeit implicitly, limits as to what auditors can achieve. Such audit activity is not necessarily a 'good thing' and any claims for such an extension in the responsibilities of the NAO really need to be supported by more than general assertions.

This chapter seeks to contribute to discussion in this area by reviewing different national requirements with respect to the audit of performance information and summarising some of the practical issues that any such audits have to address in public sector organisations (for a more detailed analysis of such issues, see Bowerman and Humphrey, 2001). The chapter is divided into four subsequent parts. The next section briefly introduces the PSA system and is followed in section three by a comparative review of different national requirements relating to the audit of performance information. Section four considers the operational dimensions associated with the audit of the type of performance information commonly included in PSAs. The chapter closes by considering the implications for both public audit and publicly available performance information.

2. PUBLIC SERVICE AGREEMENTS (PSAs)

PSAs are a major development in UK central government performance measurement. Each departmental PSA sets out its aims and objectives, the resources made available to it, the approach to modernising services, the outputs and outcomes the department is working to deliver, its performance targets and the efficiency with which it plans to use its resources over the Comprehensive Spending Review period. There are also PSAs for a number of cross-departmental initiatives. The PSAs (HM Treasury 2000a) comprises around 160 targets covering 17 main government departments. Service delivery agreements (SDAs) set out how departments will meet their PSA targets together with the key output targets that are critical to the delivery of PSA target outcomes. They cover issues such as the quality of service, the development of new processes and progress towards objectives such as those relating to ethnicity, procurement and the prevention of fraud. Some of these performance measures are also designed to promote 'joined up government', reflecting the view that many government aims cannot be achieved by a single department or agency acting alone (see Bowerman and Humphrey 2001, pp. 36-38). Initial guidance (HM Treasury et al. 2001, p. 22) noted that a performance measure should have "clear documentation behind it, so that the processes which produce the measure can be validated" but was not specific on who should conduct the validation.

This lack of specificity has helped to stimulate a fair amount of debate over whether PSAs should be audited and by whom. Valuable reference points for evaluating some of the claims made for extending auditing remits in UK central government are existing regulations in other parts of the UK public sector and those in other countries with a tradition for auditing performance information. It is to such contexts that we now turn.

3. AUDITING PERFORMANCE INFORMATION: AN INTERNATIONAL PERSPECTIVE

Performance audits can take a number of forms. Barzelay (1997), for example, identified four main types of performance audit: efficiency audits, program effectiveness audits, performance management capacity audits and performance information audits. Bowerman (1996) drew distinctions between reviews of management systems, arrangements and procedures; value for money procedures' audits; policy audits; audits of management representations of value for money; comparative performance audits; and quality audits. The type of performance audit being proposed for the PSAs therefore represents just one particular dimension of performance auditing. It corresponds to Bowerman's 'audits of management representations' and to Barzelay's 'performance information audits'. In Barzelay's review of public sector audit practices in thirteen countries, just three (Finland, New Zealand and Sweden) routinely audited performance information. He suggested that such an audit form is only possible in the context of a results-oriented public management regime. For the majority of countries, information to judge performance has not been available (at least until recently) and auditors have had to construct such information for themselves (see Brown et al. 1991, p. 189). Bowerman et al. (2000) commented that, in a so-called 'audit society' era, it was surprising to find that there were so few statutory provisions requiring the external verification of public sector performance information. Pollitt et al. (1999, p. 57) suggest that increased emphasis on performance measurement under new public management has encouraged state audit bodies to give more attention to scrutinising performance data.

3.1. Other Audit of Performance Information in The UK

The extent to which sets of public sector performance indicators are verified by an external auditor (or regulatory body) is very variable. At one extreme, a major role was given to the auditors of UK local authorities in 1992 under the Citizen's Charter initiative (see Bowerman 1995) involving them in designing and specifying performance indicators. This introduced a statutory obligation for the Audit Commission to develop sets of indicators to facilitate comparisons of the performance of individual local authorities. The role of local auditors was to review the systems in place, to collect the data, and to confirm that authorities have appropriate arrangements. These indicators have since been subsumed into a new 'Best Value' regime and the Audit Commission has also been given a statutory power to trigger an 'intervention' in local services where an authority is perceived as failing either to discharge its functions adequately or failing to meet its statutory obligations (see Sheffield and Bowerman 1999). This could lead to the appointment of an external body to take over the running of a local authority service. Further, under 'best value', the auditor's role is not just concerned with past performance data but includes a future orientation through the requirement to ensure that information in local authority performance plans is accurate and realistic.

Local authority auditors, therefore have a large and influential role in the audit of performance information - a role that potentially contrasts quite significantly with the government's reluctance to give an extended role in respect of performance validation to the NAO (as auditors of central government).

3.2. International Requirements Governing Performance Information Audits

Outside of the UK, three national audit offices have statutory responsibilities for the routine audit of performance measurement systems and data – Finland, New Zealand, and Sweden (see Barzelay 1997; NAO 2001). In many other countries, including the Netherlands, Australia, Canada and Denmark, while there is no general requirement for such validation, the national audit bodies do examine performance measurement systems and data from time to time. The role of auditors in examining performance information, in those countries where it is a formal responsibility, is now briefly examined.

3.2.1. Sweden

The Swedish National Audit Office has developed a strong system of performance auditing and is responsible for auditing the performance information published by agencies in their annual reports (Swedish Ministry of Finance 1995). The audit involves: critical evaluation of the source(s) of disclosure, computational verification, evaluation of methods for data collection, checks to see if any essential disclosures have been omitted, and evaluation of the reasonableness of management's conclusions. In addition, the auditors are concerned to see whether the whole performance report is relevant and meets stipulated requirements. Auditors have commented that the performance measures reported are not yet fully satisfactory as they tend to focus on workload and activities rather than service quality and outcomes (Talbot et al. 2001, p. 27).

3.2.2. Finland

In Finland, the State Audit Office carries out routine audits of performance data supplied by agencies and departments, as well as performing periodic performance audits. Pollitt et al. (1999, p. 82) explain that the audit office's mandate includes examining "the correctness and adequacy of external information regarding results' and 'the truthfulness of grounds for setting objectives". However state auditors in Finland do not have the authority to specify indicators - Pollitt et al. (1999) cite an example of the State Audit Office proposing an indicator for prisons, which was vigorously rejected by the auditee (p. 95).

3.2.3. New Zealand

In New Zealand public service agreements have led to contracts between ministers and departmental chief executives. The New Zealand Audit Office is responsible for auditing performance information and other performance matters based on their assessment of the risks in the organisation. It can also carry out specific audits of performance information included in an organisation's annual report (statements measuring actual outputs and comparing them with outputs agreed at the start of the year). During the first year of such audit activity, virtually all the authorities involved received qualified audits (Pallot 1992) - typically because many objectives and goals adopted were not readily measurable. More 'suitable' performance indicators were subsequently developed following advice from the Audit Office. The New Zealand Audit Office provides guidance on setting performance indicators but, unlike the UK Audit Commission, has not had a direct role in specifying them.

3.2.4. Elsewhere

In Australia there is no general requirement for audit and validation of performance information. However, as part of its value for money audits, the Australian National Audit Office examines resource usage; related information systems; outputs and outcomes, including performance targets, indicators, assessments and measures; monitoring systems; and legal compliance with delivery of outputs and outcomes. In Canada, again, the Office of Auditor General does not automatically audit performance data, although it may do so as part of a value for money audit or where they feel there is a specific need for such an audit. In Denmark the Office of Auditor General regularly reports on performance information supplied by departments and agencies in addition to carrying out specific performance audits. In the Netherlands the Court of Audit conducts reviews of performance measurement and administrative systems but performance data produced as part of the government accounts is not subject to a separate audit by the Court of Audit (although it may draw attention to inaccuracies where it sees fit).

In the United States the Government Performance and Results Act (1993) required federal agencies to report against performance goals, targets (from 2000), and issue a performance plan (from 2001). The General Accounting Office (GAO) itself does not verify and validate performance data but it has produced lengthy assessments (e.g. 25 pages) of performance reports and plans for each programme area - commenting on whether measures are appropriate and adequate to assess whether the specified goals and essential outcomes are being met. The GAO also comments on goals and measures in the performance plan for the forthcoming year. The overall conclusion from the GAO review (see GAO 2000) was that there was only limited confidence that agencies' performance data would be credible. The review stated that few agencies had provided explicit discussions of how they intend to verify and validate performance data. It also expressed concerns over the limitations in the availability of quality financial data.

The overall picture is therefore one of the majority of public audit bodies regularly reviewing performance information and systems of performance measurement but with only a minority having a direct 'verification' audit of performance information as part of their routine statutory duties. The NAO's position has much in common with the majority of state audit bodies. Without extending its remit it has discretion to conduct periodic reviews of performance measurement systems and, indeed, has done so in the past (e.g., the Benefits Agency, the Meteorological Office and Highlands and Islands Enterprise - see HM Treasury Select Committee 1999, Appendix 7). It can also comment on the integrity of performance measures if it wishes - and some departments have even commissioned such a validation service. It can use performance information for audit planning purposes and as central evidence in its value for money studies. In short, it can do pretty what it likes with performance information within its existing remit. Placing the verification of performance information on a statutory basis would add a whole new dimension to the activity of the NAO and to the Public Accounts Committee (PAC) to which it reports. Both would undoubtedly require more resources in order to undertake the increased workload. The fundamental question is then whether such additional activity and expenditure worth it? Or in today's managerial speak, would it 'add value'?

4. AUDITING PERFORMANCE MEASURES: AN OPERATIONAL PERSPECTIVE

In an earlier piece (see Bowerman and Humphrey, 2001), we questioned whether it was sensible to demand that PSAs be subject to external verification (or audit) by an external audit body, whether it be the NAO or the Audit Commission etc. We have found little in subsequent debate and discussion to counter such criticisms. Performance measurement in the public sector remains a highly problematic, subjective process – with doubts and concerns over: what is meant by 'good performance'; the reductionist nature of much published performance information; and the intended audience for such information (for example, see Smith, 1988 and 1992; Leeuw, 1996; Midwinter 1994; Stewart and Walsh 1994; Humphrey et al. 1993; Day and Klein, 1987). Our analysis of the PSA regime and supporting literature found that many of these highly practical concerns had not been resolved in its design. The main operational problems revealed by our review are summarised below:

In the first place, doubts have been raised over the conceptual clarity associated with definitions of performance and whether (PSA) measures should be based on inputs, outputs, outcomes or social impacts (e.g., see Talbot, 2000). PSAs do not appear to be lending themselves readily to audit largely because they have remained at a very general level in terms of the specification of targets and key performance indicators. For instance, the Foreign and Commonwealth Office's official intention is to 'improve the quality of life around the world on issues of concern to Britain including the environment, human rights, good governance and crime reduction' (HM Treasury 2000a, p.23). For some of the cross-service PSAs, responsibility is being shared between a number of government departments and other groups. The ability to define and allocate accountabilities and responsibilities between these stakeholders and across agreed timeframes for action plans, however, is still unproven. Further, there are also considerable uncertainties over the main users of PSA information. The government has often stressed the public accountability aspects of the PSA system (HM Treasury 2000b; HM Treasury et al. 2001) but key policy documents (e.g. see Cabinet Office, 2001) also suggest that the PSAs are very much ways for the government, rather than the public per se, to monitor and control service delivery: establishing 'machinery for monitoring implementation - including prime ministerial stock-takes- to enable quick adjustment of priorities, resources and targets' (p. 9).

Arguments in favour of the audit of PSAs have tended to take for granted that PSAs have a citizen focus and are intended primarily for external accountability purposes. For instance, a HM Treasury Select Committee (2001, para 23) has argued that reporting of progress by central government departments against quantifiable targets needs to be made credible by being externally validated. It saw this as 'essential to the interests of transparency and accountability to the taxpayer'.

The NAO initially established a performance measurement division in anticipation of undertaking a more extensive external validation role with respect to PSAs (see Gosling 1998) and remains a strong supporter of such a function. The government, however, has resisted giving the NAO such a role. On one level, it has taken steps to try and ensure that PSA information has integrity without requiring detailed verification/auditing by the NAO. The government has set up a working party to review the construction of targets specified in PSAs (NAO 2001, para. 4.25) and stressed the need for internal controls over the validation of data systems (HM Treasury et al. 2001). It has also emphasised that data in PSAs is being collected by reputable bodies such as the Office of National Statistics and does not need further verification. Likewise, PSA information being collected by local authorities and the Department of Health is being overseen by the Audit Commission and is supposed to be reasonably robust (NAO 2001, para 4.29). Finally, where departments are relying on their own data collection systems, they have to detail their quality assurance procedures. Some departments have set up performance review boards to validate data or have used the NAO to carry out annual reviews of sensitive aspects of the data (NAO 2001, para 4.30). On another level, the government has argued that the audit of PSAs would represent a fundamental shift in the role of the NAO. As one Treasury minister officially observed, it could lead the NAO too far into the political arena (PAC, 2000, response to Q 25). The Chief Secretary of the Treasury backed up such a view with some practical concerns when addressing a HM Treasury Select Committee hearing (1999, response to q. 188). He said that 'on a whole host of counts, I have some very real tangible concerns about the idea that just automatically we should sign up for external audit'. He went on to cite concerns about the involvement of audit too early in the process when targets and measures were still being developed and when there were no agreed national standards for auditing performance measures. He was also concerned about the cost of the audit work and questioned whether the NAO was the only, or best, body given the work being done by internal audit and other bodies.

The principal argument for extending the role of the NAO or a related public audit body has been one of public accountability: "the (external) validator (of PSAs) should also provide assurance that the information as presented is not likely to mislead the reader. We therefore consider that each year the validator should assess and report upon whether the performance information as presented is accurate and whether it fairly represents the overall performance of the Agency and their progress towards meeting their objectives" (NAO 1999, para 5.39). Such arguments, however, make big assumptions over the use and value of such information. For instance, if PSAs are going to be more of an internal management tool within central government, then external validation seems less essential. If the data is deemed to be trivial or excessively detailed and complex, is it worth auditing? Can it be audited? Are there better things that auditors can be spending their time on? For instance, rather than monitoring data reliability, should auditors not be reporting publicly on how well central government departments have performed? Surprisingly, debates so far have given little attention to such issues. As we have stressed elsewhere (see Bowerman and Humphrey 2001, pp. 40-41), the supporters of an external audit function in relation to PSAs have largely presumed the value of such a monitoring process. Their arguments have tended to remain at the level of general and unsubstantiated belief statements that audit is 'good' and appear to be driven more by a worry over inconsistencies in the scope of public sector auditing. They also ignore much that has been written on the limited nature of formal performance measurement systems and the benefits of viewing them in less static and rationalistic forms (see Meyer and Gupta, 1994).

There are some grounds for arguing that central government appears keen to impose audit regimes on other parts of the public sector that are more extensive than it is prepared to sanction in relation to the monitoring of its own activities (see Bowerman et al. 2002). There is also some evidence that the government's desire to limit or cutback on audit activity and auditor access is being driven less by accountability concerns and more by a feeling that auditing in the public sector is hindering entrepreneurial activity on the part of public service providers and managers (see Cabinet Office, 2001, p. 10) – raising concerns that audit activity is potentially going to be restricted in areas where it is most needed (e.g. where risk taking is most pronounced). Nevertheless, such inconsistencies and worries over the government's intentions should not be seen as automatic justifications for extending audit obligations and work-loads in monitoring PSAs. At a time of increasing criticisms of the ever-expanding nature of (public sector) auditing and a displacement of service delivery activities by monitoring functions (e.g. see Power 1997), any extensions in auditing have to be based on substantial claims (and, if possible, practical evidence) regarding the value of such work. On the basis of the above arguments and international experiences with the monitoring of performance information, we believe that the case for external verification of PSAs is still largely unproven.

Ultimately, any discussion on PSAs has to be driven beyond audit and back to the relative usefulness of the data being collected and reported by central government departments and the range of institutions within their control/supervision. What appears to be most crucial is the provision of better, more informative data - not the process of verifying data of questionable value. As far as public accountability is concerned it appears unhelpful to make available large quantities of (albeit 'audited') information, as this puts the burden of interpretation on the public. The Sharman report (2001) suggested a rather different approach - with auditors taking a more active role - publishing an annual report showing departmental progress against targets and making recommendations for improvement. However this role does not appear to have been endorsed in the government's recent response to Sharman (HM Treasury 2002). The concept would, in any case, require careful consideration as it raises the longstanding issue as to the essential distinctions between audit and inspection functions in the public sector and the extent to which the audit is a disinterested observer of organisational activity or an active participant in processes of organisational change. However, this seems to be a more fundamental and necessary audit debate than the one that has so far taken place with respect to PSAs. This is especially so given previous criticisms of the lack of public visibility given to some existing performance based, value-for-money audit reports within public sector organisations (see Bowerman et al. 2000) and continuing concerns over the value of traditional, compliance-based audits (i.e. information credibility assessments) – for reviews, see Humphrey (1997) and Power (1997).

5. CONCLUSION

This chapter has reviewed international regulations with respect to the audit of performance information and related these to the ongoing debate in the UK as to whether Public Service Agreements (PSAs) should be audited and by whom. In this respect, the UK government's chosen policy does not appear to be out of line with international audit practice. Further, while its policy may not be the one desired by the National Audit Office and some influential parliamentary select committees, it could well be an opportune one – allowing the NAO to focus on more significant and productive audit work. The 'added value' that might be obtained from a 'compliance' audit of PSAs has still not been comprehensively addressed. Indeed the proponents of this role for audit have largely argued their case based on the (questionable) assumption that the information has a primary focus on external accountability – when there is a major managerialist 'command and control' rationale underpinning the performance information regime. Additionally, a range of other arguments suggest that the nature and scope of the PSA data-sets matters more than whether the information has been independently verified, especially given some fundamental limitations in contemporary auditing practice.

While the UK is witnessing an important tussle over the future direction of public sector audit, there is much to be gained from more detailed discussion and practical analyses. This relates not just to the audit of performance measures but also in terms of determining where audit activity is most needed and most effective (across different national audit regimes) in enhancing the performance and accountability of government and associated public services.

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ROWAN JONES
GARY GIROUX

COMPARATIVE LOCAL GOVERNMENT AUDITING: AUDIT TIMING IN THE US AND THE UK

1. COMPARATIVE LOCAL GOVERNMENT AUDITING: AUDIT TIMING IN THE US AND THE UK

Assuming that regulations and incentives are the same, local government auditing should be similar across countries. Therefore, audit timing (the number of days from the end of the fiscal year to the date of the audit opinion on the financial statements) also should be similar across countries. The purpose of this analysis is to compare samples of local governments from the two countries using OLS regression to see what factors may explain these differences. The focus is comparative, rather than explanatory. That is, a single model is used across a sample of local governments in the two countries. If the purpose had been explanatory, the models would have been developed separately to capture unique factors in each country. While either approach has advantages, this study is an attempt to begin empirical comparative research in local government accounting and auditing. While each country has unique cultural, historical and regulatory systems, comparing empirical findings should result in a better understanding of accounting and auditing structures and theories.

2.REGULATORY STRUCTURES

In a recent comparative study of local government accounting in the US and the UK, Giroux, Jones, and Pendlebury (forthcoming) reported significant similarities between the two audit regimes, but with important differences. An important factor is regulatory differences, with current regulations basically established in 1982 for the UK and 1984 in the US, but for different reasons.

In the UK, the requirement for an annual report and audited financial statements, for each local government as a whole, emerged in 1974. Until 1982, the auditors only reported on exceptions to "clean opinions"; from 1982 a positive opinion has been required (whether clean or not) (Local Government Finance Act 1982, s18). The auditors' report is required within nine months of the fiscal year-end. The auditors are either District Auditors (public sector) or private sector (often, but not necessarily, Big 5 firms). Auditors have responsibilities for economy, efficiency and

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effectiveness audits (also called program audits), which could contribute to delay in reporting on financial statements.

In the US, audit requirements have been implemented piecemeal (at local, state, and national levels). The federal government started requiring "control audits" associated with federal grants at least since the 1950s. The idea and regulations for a single audit for state and local governments began in the 1970s. The Single Audit Act of 1984 mandated financial audits for all but the smallest local governments. There is usually no mandated period within which the auditors must report, although recommendations of three to six months after the end of the fiscal year are common. The auditors are, depending primarily on state law, either state (governmental) auditors or private sector (not necessarily Big 5) auditors.

The functions of the audit seem to be virtually identical in the two countries. However, there are important regulatory differences. In the US, most local governments choose their own auditors following an audit procurement process. Criteria may be audit- quality-based or low bid. In addition to federal regulations, which require additional procedures and reports beyond the standard financial audit, there is limited oversight of the audits by federal cognizant agencies.

In the UK since 1982, local governments do not choose their own auditors. Instead, they are chosen by a central government agency, the Audit Commission (for Local Authorities and the National Health Service in England and Wales). Also in the UK, there are two complications in producing the auditors' report. First, since 1996, the local government must by law formally approve the annual financial statements before the audit is conducted. This approval must take place no later than six months after the fiscal year-end. There is no overt parallel in the US and, although the US audit is similarly dependent on the underlying accounting, the clear separation in the UK could be a contributory factor to delay in publication of audited financial statements. Second, people in the UK (in effect any local electors) have statutory rights to inspect the accounts to be audited (over a period of fifteen working days), to question the auditor and to make objections to the accounts. Such objections can be immaterial to the financial statements as a whole, while being so difficult to resolve that the law allows auditors' reports to be issued even though the audit is only "substantially complete" (i.e., even though there are outstanding objections).

In summary, the audit purpose is similar across countries, but regulatory and other differences are noted. The objective of this paper is to test for similarities and differences in audit timing within the two countries for the same fiscal year and for local governments of similar sizes. The next section describes the development of our model. We then describe the research method and samples, followed by analysis of results. The final section offers interpretation and suggestions for further research on comparative government auditing and accounting.

3. MODEL DEVELOPMENT

The dependent variable of interest is audit timing (TIMING), the number of days from the end of the fiscal year to the date of the audit opinion on the financial statements. Auditors are expected to submit their audit reports as soon as possible after the end of the fiscal year. Regulators from both the US (GASB) and the UK (CIPFA) encourage publication of audited financial statements on a timely basis. Local governmental administrators can signal fiscal competence and stewardship to financial users with a "timely" (early) audit report. That is, complete financial records with no indication of GAAP or regulatory violations should result in a relatively quick audit. Thus, early TIMING can be considered "good news".

Auditor type is the independent variable of particular interest, but for different reasons in the two countries. In the UK, most audits are conducted by District Auditors. Since the advent of the Audit Commission, independent auditors have audited some 30% of local districts each year. It is expected that independent auditors have incentives to increase their percentage of local government audits and/or audit fees. One mechanism is to report audit findings on a timely basis. Assuming that independent auditors attempt to signal efficient audits, a negative sign is expected. In the US, most cities pick their own auditors, usually independent auditors. Only six governmental (state) auditors were used in the US sample. As stated by McLelland and Giroux (2000, p. 269): "State auditors may not be concerned with the effects of competition or with their reputations resulting in longer audit reporting lags." It is again expected that independent auditors will attempt to signal efficiency, a negative sign.

Client size should be associated with audit complexity. The log of population (LPOP) is used to capture complexity. Following Bamber et al. (1993) and McLelland and Giroux (2000), a positive sign is expected. The government's operating surplus or deficit (SD) is a signal of financial health and a surplus considered "good news". This would be associated with a negative sign. However, a deficit can be used "strategically". That is, surpluses in some years and deficits in others based on relative funding and spending requirements. An additional complication in the US is the mandate against deficit spending for many municipalities. No such mandate exists for UK local governments. Therefore, no sign is predicted.

The existence of a web page (WEBPG) is used as a surrogate for the use of advanced information technology. Organization productivity is directly related to information technology (Bhattacharya et al., 1997; Clement and Gotlieb, 1987). Governments with superior technology should have earlier audit timing and a negative sign predicted.

4. SAMPLE AND METHOD

This analysis looks at 260 UK local governments and 165 US cities, over 100,000 in population. For the UK, the data relate to all local governments over 100,000 in population (at June 1995), in England and Wales. For the US, a request was sent to all 209 US cities with population over 100,000 (fiscal year 1996) to send their comprehensive annual financial report (CAFR) and to complete a survey on audit characteristics. Complete data were received from 165 cities. The focus is on large, multi-function local governments, those most likely to benefit from signaling audit effectiveness. These two groups are roughly comparable in terms of size and functions.

Means and standard deviation were used to summarize descriptive results for all continuous variables. Frequency count was used for WEBPAGE, a dummy variable. A Pearson's correlation matrix was analyzed to consider variable relationships for both samples. OLS regression is used for empirical analysis.

5. RESULTS

Descriptive statistics are presented in Table 1. The time between the end of the fiscal year and the date of the audit opinion on the financial statements for UK local governments averaged 290.3 days; for US cities it averaged 124.7 days. It seems unlikely that UK local governments could be complex enough to explain the difference. On average, UK districts were slightly smaller than US cities. UK districts had an average actual operating deficit of almost £3.3 million. On the other hand, US cities recorded an average General Fund surplus of $11.3 million. Most US cities used independent auditors (96%), while only 30% of UK districts used independent auditors. The selection process of auditors varies significantly across the two countries. In most cases, US cities select the auditor based on a request for proposal. UK auditors are selected by the Audit Commission. Consequently, it is expected that auditor incentives are quite different in the two countries. Finally, relatively more US cities used web pages (as of 1997) than UK districts, 64.5% vs. 28.1%.

Correlation results are presented in Table 2, with UK results across the top and US results on the bottom. For US cities population, independent auditor and web page were significantly correlated with audit timing (negative for independent audit and web page). For UK local governments, only independent audit and web page were significant, both negative. Therefore, the direction of the significant variables was as expected. For UK local governments, significant correlations among independent variables included population and surplus-deficit, population and web page and surplus-deficit and web page. Only population and surplus-deficit was highly significant, suggesting that smaller local governments were more likely to run deficits. Only population and web page was significant for US cities, indicating that large cities (also true for the UK) were more likely to have web pages.

***Table 1:** Descriptive Statistics.Means/Frequencies (Standard Deviations/Percent)*

VARIABLE	UK	US
Audit Report Time (TIMING)	290.3 days	124.7 days
	(156.1)	(35.7)
Population (POP), in thousands	274.1	311.4
	(270.8)	(409.8)
Actual Surplus / Deficit (ASD)	£-3,355.3	$11,346*
	(5847.2)	(48,550)
Independent Auditor (INDAUD)	80	159
	(30.8%)	(96.3%)
Web Page (WEBPG)	73	107
	(28.1%)	(64.5%)
Sample Size (n)	260	165

Table 2: Pearson's Correlation Matrix (Prob.). With UK Local Governments Across the Top & US Cities Across the Bottom.

	TIMING	POP	ASD	INDAUD	WEBPG
TIMING	1.00	.006 (.924)	-.079 (.207)	-.193* (.002)	-.116** (.063)
POP	.203* (.009)	1.00	-.600* (.001)	.069 (.270)	.331* (.001)
ASD	.073 (.353)	-.002 (.979)	1.00	.021 (.739)	-.207* (.001)
INDAUD	-.218* (.005)	-.039 (.620)	.045 (.564)	1.00	.010 (.873)
WEBPG	-.141** (.069)	.242* (.002)	.028 (.719)	-.122 (.117)	1.00

N = 260 for UK; 165 for US
** Significant at .01*
*** Significant at .1*

OLS regression results are presented in Table 3 for both the UK and US samples. An analysis of correlations and variance inflation factors (VIFs) indicated that multicollinearity was not a problem (e.g., all VIFs were less than 2). However, there were seven extreme values with the UK model (also associated with non-normal residuals). Therefore, the extreme values were deleted and the regression rerun. This reduced the non-normality problems and this smaller sample was used for analysis.

Table 3: Regression Results for US and UK Audit Timing. Dependent Variable = Opinion Time (OPNTIME). Coefficient (t-value)

	Sign	**UK Model**	**US Model**
Independent Auditor (INDAUD)	-	-49.56 (-3.97)*	-37.80 (-3.26)*
Log of Population 1996 (LPOP)	+	14.00 (1.31)**	14.77 (3.84)*
Surplus / Deficit (SD)	?	0.0001 (0.09)	46.09 (1.50)**
Web Page (WEBPG)	-	-30.0 (-2.23)**	-20.29 (-3.49)*
Intercept		123.55	47.21
Adjusted R^2		6.3%	14.0%
F Value		5.21*	7.66
Sample Size (n)		253	165

Note: reduced sample for UK Local Governments
** Significant at .01*
*** Significant at .1*

The final UK sample had 253 observations. The model had an adjusted R^2 of 6.3% and had an F value of 5.21, significant at .0005. Three of the independent variables were significant, all in the predicted direction. As expected, independent auditors reported more quickly than District Auditors. Log of population was significant, indicating that larger districts took longer to audit, expected because of the greater complexity involved. Web page also was significant, suggesting that more sophisticated information technology was associated with shorter audits.

The US sample with 165 observations had an adjusted R^2 of 14.0% and an F value of 7.66, significant at .0001. All variables were significant in the expected direction. Surplus/deficit had a positive sign, indicating that surplus cities had a longer audit time. This was an unexpected result.

6. CONCLUSIONS

In summary, a single model was used to compare UK and US local governments for audit timing. Although incentives differ somewhat across the countries (especially auditor selection incentives), results are comparable based on OLS regression. Many limitation exist for this analysis, but it suggests that further comparative governmental analysis may be useful for economic and policy comparisons.

The primary purpose of this empirical study is to indicate the viability of comparative research, using similar models across countries. As demonstrated here, results are generally comparable. However, different regulatory environments suggest additional analysis of the audit environment, including the special dependence that UK auditors have on the local governments themselves to produce the financial statements before the audit can begin.

Further research is encouraged, especially in governmental audit characteristics. This study represents only a first step in comparing audit environments that have both interesting similarities and differences. Particularly important is the need to investigate the differences in auditor selection and other regulatory incentives.

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ELVIRA RODRÍGUEZ

SOME ISSUES ON THE CURRENT MEANING AND AIMS OF GOVERNMENTAL ACCOUNTING

The definition of accounting as an information system is generally accepted in any one of the areas it is involved with. However, the use of accounting information in public corporations has differed from that in private organisations for many years.
In this respect, the control of the activity reported is a striking differential characteristic. In public corporations, this element of control should, on the one hand, adhere to the lines set down by the annual Budgetary Law, and on the other, be rendered as in Anglo-Saxon accountability. These two dimensions of governmental activity have had a significant effect on the conception of its reporting systems, in other words, on the other informative facets or possibilities of its accounting systems.

Traditionally, Governmental Accounting consisted solely of budgetary accounting accompanied by cash control.

Recent years however, have seen an increase in the uses being made of Governmental Accounting, and hence, in its definition and development. In addition to budgetary information, information about assets and liabilities is also being obtained and the cash criterion has seen a move towards accrual basis to a greater or lesser extent. The need to achieve good management of public funds, not only from a legal point of view, but also from the perspective of efficacy and efficiency has acted as the main incentive in bringing about governmental accounting reform.

We must bear in mind that not only those responsible for public finances have an interest in knowing how the management of resources is being carried out, but also that those who generate these resources, citizens, have a right to know what is done with these funds.

Thus, accountability takes on a wider meaning and goes beyond the rendition to Parliament and external control bodies with the advent of the concept of transparency. In the case of governmental accounting, this concept must be understood not only as access to information, but also as the standardization of the information made available. In this case, standardization implies a move towards business accounting systems, which are much more advanced in this field than governmental accounting systems. Information must not only be available, but must also be understandable to those for whom it is intended, in this case, citizens.

On occasions, as technical managers, we may succumb to the temptation of designing systems which are only accessible to those in the know, and which require our assistance in their interpretation and utilisation. This could be a good short-term

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survival strategy, but it will not hold out in the long term. When, as in the case of governmental accounting, a system is a means for the achievement of certain objectives, and more so, objectives of a general interest, as technical managers, the specialists, we have a duty to define this system in the most user-friendly way possible.

In public administration, we are faced with a closed circle: the taxpayers provide their Governments with resources to administrate, redistribute and provide them with the services they demand. The sharing out of these resources is carried out by Parliament through budgetary legislation. Governments employ these resources, provide the services and inform Parliament, which then initiates a new cycle of resource allocation.

The reporting process is entrusted to the accounting system which must be capable of providing veracious information on various extremes; firstly, on the destination of these funds in order to verify whether they have been used as Parliament intended, and secondly, it must inform on whether the objectives which gave rise to the allocation of resources have been fulfilled.

It is irrefutable that, for the system to be able to gather this information, and for this information to be useful for the purposes of subsequent allocation, there must be a clear definition of which objectives are to be achieved and furthermore, we must be able to evaluate these objectives.

A democracy grants its citizens the right to know what is done with their taxes, and this right goes beyond parliamentary control. This requires both interpretations of the transparency previously mentioned to become the key principle by which governmental accounting fulfils its commitments.

In addition, the reporting system must be able to measure not only the efficacy of public managers, but also their efficiency; in other words, the administration of limited, scarce resources in order to achieve the optimum results at the lowest possible cost.

The securing of an accounting system oriented towards the measuring of costs and results in public administration presents certain peculiarities which explain, although do not justify, why so little has been done on this issue to present.

The main difficulty in establishing systems of cost measurement and control has been the existence of cultural barriers and corporate resistance. The availability of first-rate information on costs enables managers to maintain a clear vision of the production process, in which the principal management problems can be identified, thereby affording a greater capacity for controlling the activity within the organisation. There will always be resistance to the introduction of tools providing for this control by members of the organisation.

In order to overcome this reticence, important changes in attitude are required, since the development of systems enabling those managing an organisation to control the costs of their activities will be of very little use if those individuals are not convinced of the need for or the desirability of this control.

In this respect, public managers can be seen to be increasingly conscious of the need to include cost control as one of the elements on which their management is based, and we might thus expect to see cost accounting coming into use as a routine tool in public administration in the coming years.

The other major hurdle to the introduction of management accounting in public administration arises from the difficulty of measuring results in the public environment.

Within the field of private economic activity, the objective is to maximise profit. Indicators of the success of company management, such as profits, sales, turnover or company share prices can be deduced from accounting information.

In contrast, these references are not valid for public administration managers, whose aim is to provide the citizen with a range of services for the improvement of their standard of living, and for which market determination mechanisms are not appropriate.

If we want to control how Public Administrations are meeting the objectives entrusted to them, we must begin with the quantification of these objectives by means of indicators which can be periodically measured and which complement accounting information of a financial nature.

Both cost control and the monitoring of results are responsibilities, which first concern the immediate managers of services provided to the citizens by the administration. It is of no use to discuss a management accounting system, which is not established by and for the managers themselves. It is essential that those responsible for the various sectors be aware of this. This awareness is set within the framework of cultural change, which is gradually taking place in the organizational culture of the administration and in the attitude of public managers. This attitude is presently undergoing a transition from a bureaucratic management style in which the clinical observance of procedure guided their actions, towards a management style in which the procedure is considered to be a means for achieving certain results expressed in terms of service to the citizens.

The new financial culture recognizes that, if the quest for an improved management has led to a movement of de-concentration with the emergence of Public Bodies and other Public Sector entities, good economic-financial management requires those responsible for these bodies to be sufficiently flexible when it comes to managing the resources allocated to them to achieve their objectives. The other side to this flexibility is responsibility. Managers must be answerable for the management carried out. In the measurement and evaluation of management, the information provided by Governmental Accounting is essential. Precisely the new General Budgetary Law, currently being drafted, will be concerned with binomial autonomy for management-responsibility.

In this vein, it must be pointed out that many Governments have already taken on a vigorous process of the redefinition of the Public Sector which does not only focus on the politics of liberalisation and privatisation of public companies, but also on analysing and delimiting what should be financed with the taxpayer's money, with the aim of reducing the tax burden.

On this issue it is imperative that governmental accounting provide the right information to reveal inefficiencies which, when corrected, will reduce the costs of public services. It is not a case of reducing the services provided, but rather of finding out which ways of working enable the objectives set out to be achieved, which are unnecessary, and in the final analysis, which could be less costly to the citizens.

Finally, reference must be made to the duty of member states of the European Monetary Union to render accounts on the performance of our Public Administrations. This rendition is carried out according to the European System of Integrated Economic Accounts (ESA'95), for the confirmation of compliance with the Stability and Growth Pact.

Our accounting systems must provide the information necessary for the preparation of National Accounts, which in many cases follow criteria, which are not straightforwardly or automatically compatible with the criteria necessary to deal with the other objectives of governmental accounting.

The formulation of the national accounts in the Public Administration sector takes the information made available by governmental accounting as its principle information source.

This obligation, which came out of the recommendations of the Council of Santa Maria de Feira, with the aim of assuring stable and sustainable growth within the Union by means of a restructuring of governmental accounts, demonstrated the need for and importance of the availability of a tool to rigorously measure the execution of governmental finances, while giving new scope to the classic objective of control.

In summary, the evolution of Governmental Accounting in recent decades has led it to attempt to satisfy more ambitious objectives than merely that of control. The need has been established for the Public Sector to be consolidated as an efficient economic agent, able to attend to the ends it is justified by: the creation of the conditions necessary for the market to function, the promotion of the fairest redistribution of taxes and wealth, social progress, the consolidation of Social Welfare, and the contribution to economic growth and full employment.

In order to accomplish this, Governmental Accounting has taken on new challenges, as information is needed to evaluate public management efficiency, both in each separate entity of the administration, seen individually, and as a set of public administrations, taken as a whole to achieve budgetary equilibrium and stability.