Public sector management accounting

Sara Moggi

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University of Verona

Strategic Management Accounting

Some questions

- Should public sector entities be managed differently from private sector entities?

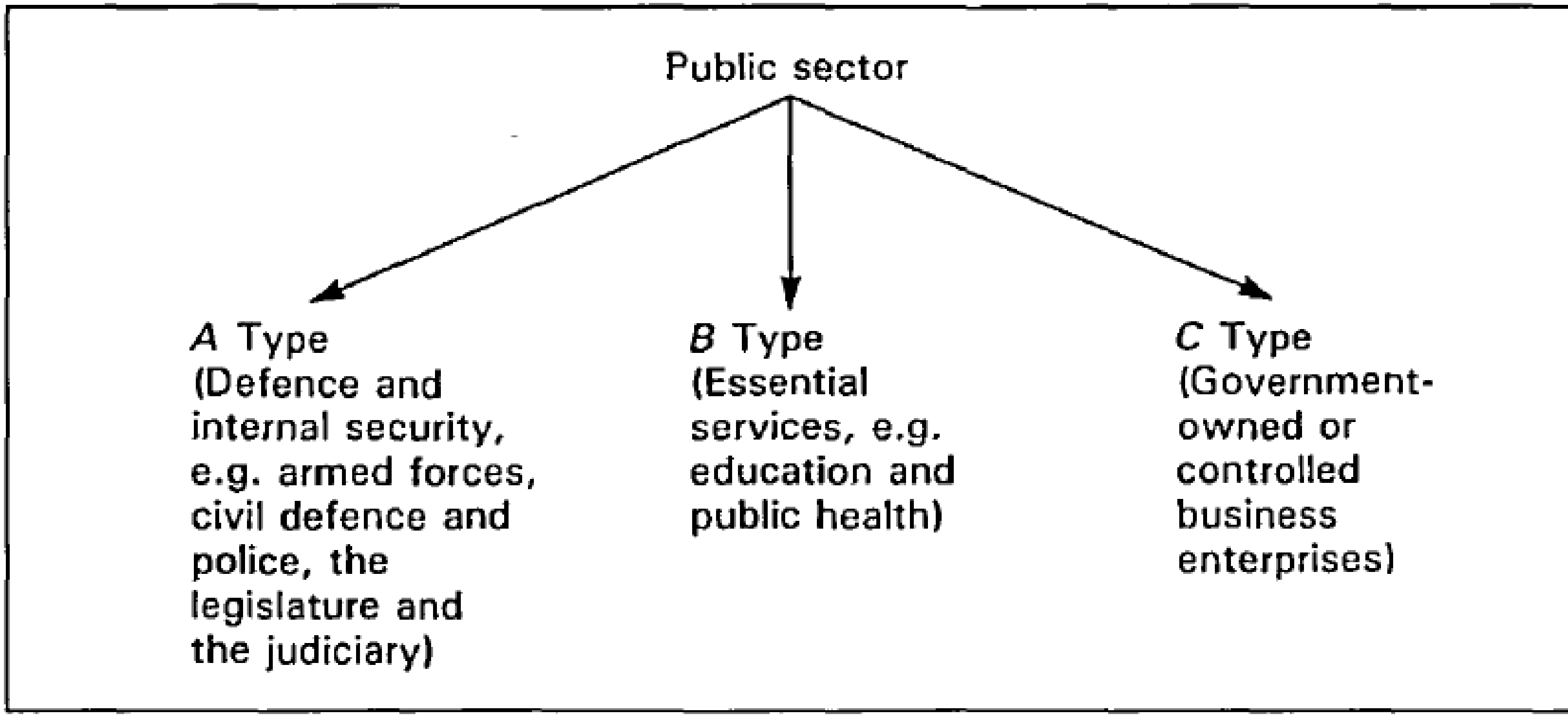
- How the government can change the public sector to be more effective, efficient and accountable?

The public sector

- The decision models used are often regulated by legislation and the decision makers are ministers, or directors appointed by ministers.

- Public sector enterprises sometimes serve as economic regulators of government — for instance in adjusting demand for goods, services or employment.

Public sector organizations



Souce: Khang Hong _ 1991

Public sector accountability

- the public sector is accountable to members of the public

- Where social and political considerations are dominant, temporary operating losses may sometimes be tolerated and may be subsidised by other sectors of the economy, and financed through taxes.

- The accounting and reporting systems of the public sector should, in my opinion, be modelled on commercial and industrial accounting systems, subject to modifications necessitated by their distinctive features

The rule of accountant in PS

The accountant in government is responsible;

- for ensuring that all government resources are conserved and optimally utilised;
- for producing and using accounting information;
- for planning and control by identifying, analysing, measuring, evaluating and verifying relevant economic data; for national income accounting and other social accounts and comparable statistics, as well as building econometric models useful for economic planning and project appraisals;
- for installing and improving the accounting and internal control systems of the government, making them sufficiently effective for executing the above mentioned responsibilities.

Public Management in public sector

- … is vigorously pursued, to analyse and evaluate public programmes and activities and to offer advice for improvements, including cost and time savings, in their implementation
- management accounting in the public sector attempts to attain the three objectives of the value-for-money criterion — namely economy, effectiveness and efficiency.
- **Economy** is concerned with obtaining and using quality and least-cost input factors to yield maximum results.
- **Effectiveness** refers to the degree to which the set of predetermined objectives is achieved, i.e. reaching the goals set.
- **Efficiency** is indicated by the productivity ratio of input/output.

Public Management in public sector

- Efficiency without effectiveness is purposeless. Effectiveness without efficiency is wasteful.
- An effectiveness measure must indicate the extent of attaining the company's objectives.
- Efficiency must be accompanied by effectiveness, that is corporate goals should be better achieved as a result of efficiency.
- It can be conceived therefore that measuring effectiveness is by no means easy, nor is it simple to appraise and report on the efficiency and effectiveness of managerial performance.

New Public Management (NPM)

- In last 20 years, many countries have embarked on a wide range of financial and administrative reforms

- The introduction of NPM in the public sector has seen a shift in focus from the adherence of formalised procedures to an emphasis on resource allocation and goal achievement

New Public Management (NPM) key - concepts

- From management's perspective, the public sector and private sector are not dissimilar and therefore should be managed on the same basis
- The refocus of process accountability to accountability for results
- The separation of commercial and noncommercial business activities
- An emphasis on improved financial reporting, monitoring and accountability

New Public Management (NPM) key – concepts (2)

- An increase in the contracting out of business activities using specific contracts for short-term work
- The mimicking of private sector management practices such as the introduction of corporate plans, mission statements and strategic plans
- A shift in preference from non-monetary incentives to monetary incentives (reward system)
- An emphasis on cost-cutting and efficiency

Pollitt & Boeckaert (2000) – the nature of public management reform

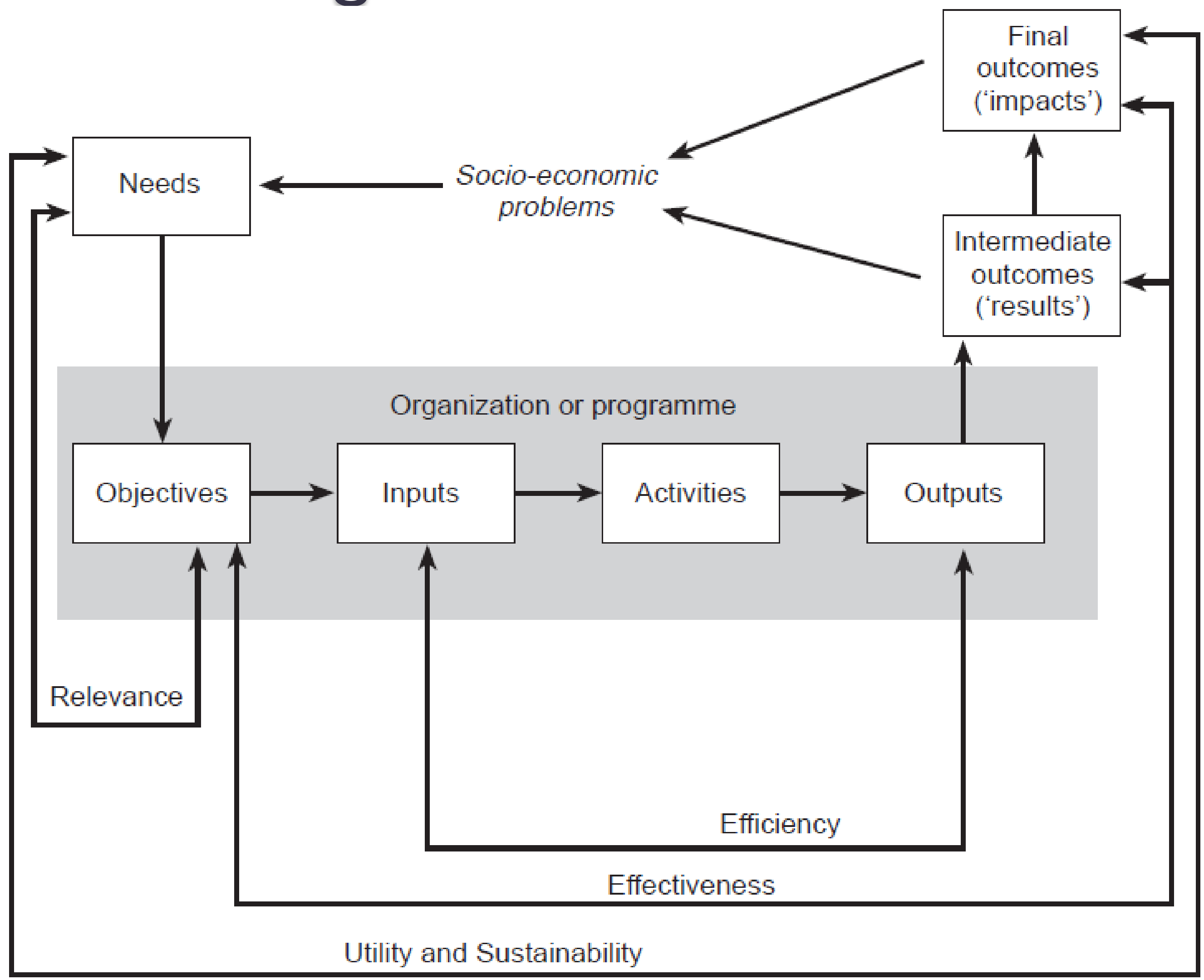
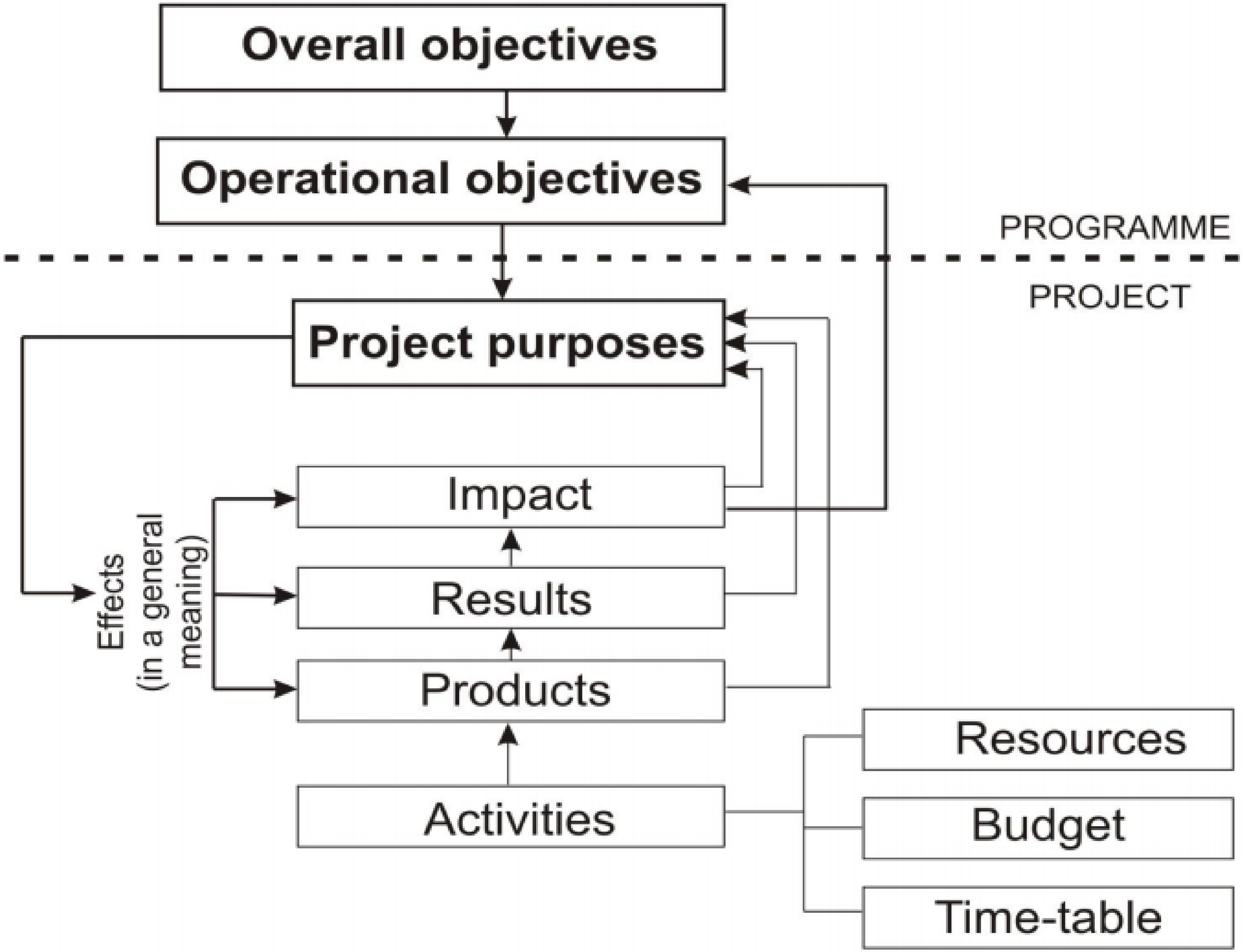


FIG. 1.1. The input/output model



Overall objectives
Operational objectives
PROGRAMME
PROJECT
Project purposes
Effects (in a general meaning)
Impact
Results
Products
Activities
Resources
Budget
Time-table

Forces driving the change in the public sector

- Changing community and business expectations
- Resource constraint
- Demands for greater accountability
- IT influence
- New attitudes to the role of government in the economy

Implications of public sector reform for accounting

- Traditional accounting in the public sector focused on inputs and outputs and the control of expenditure
- The reform of the public sector has changed the traditional role of accounting to the one that is focused on **accountability** and the **efficient** allocation of resources
- This implies that accounting should concentrate upon outputs, performance measurement, efficiency, cost saving and performance management
- **New accounting technologies** be employed such as planning-programming-budgeting, accrual accounting, performance indicators, annual reporting mechanism, balance scorecard, etc.

New accounting technologies: accrual accounting (1)

- Private sector accounting based on matching revenue and expense in order to measure profit
- This leads to using accrual accounting which recognizes both revenues and expenses when they occur: bottom line is profitability not cash situation
- What accrual has developed is an overall assessment of the *financial condition* of the organization

New accounting technologies: accrual accounting (2)

- Public sector focus on accountability for funds at hand has lead to using a cash basis as it is more easily understood and more sensitive to annual budgetary approvals of governing body
- Significant gaps in the cash approach has created a growing trend of governments and other parts of the public sector to adopt the accrual approach to both accounting and budgeting.

Cash Accounting vs Accrual Accounting

- Cash Accounting recognizes
  - revenues when cash is received and
  - expenses in the form of expenditures when bills are paid (focus on cash movement).
- Accrual Accounting recognizes
  - revenue when goods or services have been provided and
  - expenses when resources have been used (focus on when revenues are earned or resources are consumed).

Accrual accounting in PS

- Governmental funds have also used Modified Accrual Accounting.
  - Expenditures are recognized when resources are received.
  - Revenues are recognized when they are measurable and available within the accounting period or shortly afterwards (focus on financial resources).

Accrual accounting

- Cash accounting requires the recording of inflows and outflows of cash

- Accrual accounting requires revenue to be recognised in the period in which economic benefits can be measured reliably. Expenses are recognised when the consumption of goods is capable of reliable measurement.

Accrual accounting

- Accrual accounting is said to improve decisionmaking by providing information on the full cost of operations and the resources used to deliver services to the public.

- Accrual accounting gives governments the opportunity to minimise their costs through cost identification

Limitations of accrual accounting in the public sector

- Limitations identified from the adoption of accrual accounting include the fact that it can lead to the bad allocation of resources and an inadequate disclosure of the assets and liabilities
- This reduces the organisation’s ability to account for the full cost programs due to fluctuations in costs
- The introduction of accrual accounting in the public sector requires a change in the existing information techniques

Zero-based budgeting

- Zero-based budgeting is a technique whereby the total cost (base plus increment) of every item included in a proposed budget must be justified and approved
- It suggests that no base or minimum expenditure level should be acceptable for any activity
- Resources are not necessarily to be allocated in accordance wit the previous year's pattern
- This approach requires a reevaluation of all expenditures and all activity
- All activities start from a zero base

Advantages of Zero-based budgeting

- It allocates resources according to priorities, between the essential and the less essential
- It improves decision-making because budgetary allocation is related to objectives
- It makes managers plan ahead and defend their budgets
- It creares a greater feeling of ownership of those budgets

Issues on Zero-based budgeting

- It is a time consuming exercise
- It is impossible to appraise all activities each year
- It is imposed for legislative and political reasons
- It generates a mass of information that cannot be adequately assimilated by decision-makers

The change

- Some organizations being forced to change
- They face major challenge in managing change
- They need the capacity to adapt quickly.
- Large scale changes incur significant problems and challenges.
- Define patterns of behavior and relationships with others.
- Improve work procedures and job skills.

The change at an Organizational Level

- Rules
- Processes
- Organization structures or/and Manufacturing techniques
- Work process steps

Resistance to Change (the process)

- The change has been introduced
  - Few people are able to consider the need for change
  - Resistance could be strong and widespread
- Powers must be considered
  - Forces for and in contradiction of the change
  - Change have to be in depth understood.
  - The innovation link to the change tends to disappear.

Resistance to Change (the process)

- Direct Conflict
  - Between powers
  - You can have as consequence the life or the death of the innovation
- the resistance seen as persistent = balance of powers
- Resisters to change are as few and as alienated as were supporters in first phase

Key Factors driving the Success of Change

- Advocates of change.
- Degree of change.
- Time frame.
- Impact on culture.
- Evaluation of change.

Advocates of Change

- Person leading change often most important force for change.
- Practitioners may be brought in to assist.

Degree of Change

- Is change minor or major?
- The greater the change, the more difficult to implement.

Time Frame

- Greater chance of success if:
  - Change is gradual.
  - Longer time frame.
- Some organizations only chance for survival depends on:
  - Radical change.
  - Introduced quickly.

Impact on Culture

- The greater the impact on existing culture:
  - The greater the resistance and
  - The more difficult it is to implement change.

Evaluation on Change

- Standards of performance developed.
- Designed to measure:
  - Degree of change and
  - Impact on organization.

Organizational resistance (theory)

- Organisational resistance is emphasised by some societal and organizational theorists yet not by others
- Organisational theorists, organisational psychoanalysts and those concerned with organisational activist movements expect organisational resistance to occur in particular circumstances
- Where organisations are seen as a creation of a societally generated discursive lifeworld, as in the theoretical analysis of Habermas (1984, 1987), and are guided by steering media that are expressing these lifeworld values, then organisational resistance could be seen as unlikely.
- Habermas's model of society (cf. Habermas, 1984, 1987) is built on the premise that out of discourse over time we create views of our world, our social relationships and ourselves.

Steering media and lifeworld

- Systems, once created, have a potential to become separate and separable from the lifeworld in a complex society. Habermas suggests this causes the need for the creation of steering media.
- These (for example, money, power and law) ensure that systems continue to reflect lifeworld demands.
- Lifeworld = all the immediate experiences, activities, and contacts that make up the world of an individual or corporate life.
- Where this dynamic balance between lifeworld, steering media and organisations is disturbed by changes it may well lead to organizational resistance

Resistance to change according to Habermas

- Using this frame, resistance in organisational systems will be apparent in one of two situations.
- (1)The first is when the organisational system has moved away from expressing the societal lifeworld and resists those steering mechanisms perceived as legitimate (i.e. those emanating from a steering media which is following societal lifeworld requirements).
- (2) The second case is where the steering media has moved away from expressing the societal lifeworld but the systems remain in concert with that lifeworld. (ie: the introduction and rejection of one Tax).

Organizational resistance (Institutional theory)

- It highlights the importance of understanding the societal lifeworld and the organisational interpretive schemes in this respect.
- It allows for the recognition that the potential for the organisational interpretive schemes and the societal lifeworld to become disconnected and the ways this can lead to resistance to change.

Organizational resistance (Institutional theory) (2)

- Institutional theorydescribes the different processes of institutional steering in which organisational systems conform to external demands thanks to three pillars:
- (1) The regulative pillar, which provides a force for compliance through coercive isomorphism, reflects the role of law in societal steering that is highlighted by Habermas's approach.
- (2)The normative pillar reflects the taken for granted assumptions that, for Habermas, are the societal lifeworld and which we argue can also exist at an organisational lifeworld level as ``interpretive schemes''

Organizational resistance (Institutional theory) (3)

- (3) the cognitive pillar is an element that is not reflected explicitly in Habermas's structural scheme. In institutional theory it is the cognitive pillar that leads to mimetic isomorphism, where organisations copy each other in an attempt to gain legitimacy, particularly in situations of uncertainty.

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- Sara Moggi
- Sara.moggi@univr.it