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Stories of Accounting Change During Financial Reform of Public Enterprises

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ABSTRAK

Kertas ini membuat perbandingan secara analitikal mengenai lima enterpris awam yang berorientasikan komersil daripada pelbagai negara yang melalui proses perubahan perakaunan dan organisasi. Kelima-lima kes dipilih kerana penekanan ke atas pentingnya konteks dan ke atas proses bagaimana dan mengapa perakaunan berubah, diinterpretasi dan digunakan dalam spesifik organisasi. Perbandingan penemuan daripada kajian kes membolehkan pengajaran diperoleh serta persamaan dibincangkan. Perbandingan menunjukkan bahawa proses perubahan organisasi melalui perakaunan tidak akan sentiasa menjadi cara yang berpengaruh atau berkesan untuk mengubah gelagat atau cara berfikir yang telah diterima. Satu pengajaran penting ialah implementasi perubahan dalam perakaunan dikaitkan dengan pelbagai isu bukan teknikal seperti tekanan persekitaran, budaya atau cara pemikiran, kuasa dan kebolehpercayaan.

ABSTRACT

This paper analytically compares five commercially-oriented public enterprises from different countries which were subjected to the process of accounting and organisational changes in order to become profitable. The five case studies were selected for their attention to the importance of context, and to the process of how and why accounting evolved, interpreted and used within specific organisations. A comparison of the insights drawn from these case stories allows some possible lessons to be learnt and parallels to be drawn. The comparison reveals that the process of organisational change through accounting is complex and may not always evolve as an influential and effective means of altering behaviour and accepted ways of thinking. One vital lesson is that accounting change is implicated with various other non-technical issues such as environmental pressures, culture or ways of thinking, power and trust.

INTRODUCTION

Many recent empirical studies have recognised the implications of accounting in financially reforming public sector organisations (Gurd and Thorne 2003; Uddin and Hopper 2003; Nyland and Pettersen 2004). These studies raise empirical questions about how accounting change was implemented and used, and its consequences for organisational change. The aim of this paper is to compare five case studies that investigate the process of change in accounting so that possible lessons could be learnt and parallels drawn.

In reforming public sector organisations, the constitutive role of accounting in the creation of a new organisational reality and the language of profitability has been acknowledged (Dent 1991; Ogden 1995; Ogden and Anderson 1999; Hoque and Moll 2001). Hopwood (1990: 10) argued that accounting has the potential to create a new organisational reality that is related to economic understanding because 'they [accounting] enable economic knowledge and understandings to be operationalised and thereby to more readily permeate and shape organisational agendas, concerns and choices'. Nonetheless, accounting change may not always evolve as an influential means of altering the existing organisational routines and accepted ways of thinking in the public sector because organisations are composed of different intra-organisational groups with different goals, interpretations and political powers to implement and manage how change develops (Chua 1986; Pfeffer 1992; Hardy 1996).

The five case studies for discussion were selected for their attention to the importance of context, and to the process of how and why accounting evolved, was interpreted and used within specific organisations. The first case study by Abu Kasim (2004) is an in-depth case study of accounting change in a Malaysian public utility during the process of corporatisation; the second is a longitudinal study of cultural change in a public railway organisation by Dent (1991); the third is Ogden's (1995) paper on accounting change in the privatisation of the water industry in United Kingdom; the fourth is by Alam (1997) on the process of budgeting in two of Bangladesh's public enterprises; and finally, the case study by Vamosi (2000) on the transition process of a Hungarian company being subjected to new market pressures.

The findings from the five case studies were analysed for repeated and common issues, to explain their underpinning reasons and understand them in the context in which these findings were raised. These international case studies contribute to the insights of understanding the ways in which accounting is used and its consequences within different but in some ways similar social contexts, i.e., the public sector.

An interesting research puzzle is that why, in spite of the enactment of innovative arrangements in the accounting system, the new system may become detached from everyday social interactions and practices. In other words, accounting in practice may function in the unintended and unexpected ways and such diversity of practices is explained through the comparison of the insights from the different case stories.

This paper is structured into the following sections: literature review, case study method, five stories of accounting change, comparison of some of their insights, implications and conclusion.

LITERATURE REVIEW

Public sector reform exercises, such as commercialisation, corporatisation and privatisation, are underpinned by the policy of many governments (e.g. Malaysia, New Zealand and Australia) that private sector ownership and style of management are relatively superior for remedying the poor economic performance of public sector organisations (Muhd-Salleh and Osman-Rani 1991; Sulaiman 1993; Spicer *et al.* 1996; Potter 2002). It can be inferred that the ideology from the external environment shapes the purpose and the way in which accounting is reformed in the public sector.

The economic rationale, that is, the fiscal problems prevailing in the government sector, drives financial management reform (Humphrey *et al.* 1993; Sulaiman 1993). Financial stress provokes accounting change, and at the same time provides the opportunity for organisations to change by emphasising managerialism and efficiency (Hood 1995). The 'best commercial practices' for financial management reform in the public sector imply those drawn from the private sector. The wider social environment shapes the public sector's adoption of the new management and accounting systems by responding to the government mandate and the perception of 'best commercial practice'.

From the view of the governments, accounting change contributes positively to the economic welfare of public sector organisations due to its emphasis on efficiency, effectiveness and cost savings (Hopwood 1990; Hood 1995; Hoque and Moll 2001). The public sector managers are assumed to behave as rational agents who substantially use accounting information for enhancing organisational performance through effective use of resources. This means that the use of accounting for making decisions is taken for granted, and by introducing 'better' private sector techniques, the improved economic efficiency will be realised in a deterministic way.

Accounting information is assumed to be useful for allocating resources, motivating the performance of certain activities, and exercising influence and control; and through such use, enhancing financial accountability and the efficient allocation of resources. Accounting change, albeit the private sector way, is widely accepted as the method of strengthening financial accountability and controlling scarce resources within public sector organisations (Humphrey *et al.* 1993; Hood 1995; Olson *et al.* 2001).

Such a narrow perspective has failed to acknowledge that uneven implementation of the accounting technique can vary the effectiveness and consequences of accounting change between public sector organisations. The stories of accounting change, to be discussed later, attest to the uneven implementation of accounting in practice. Contrary to the expectations of reformers or the policy makers, the enactment of the innovative techniques in some situations will not necessarily lead to their desired instrumental use or positively impact on behaviour and ways of thinking.

CASE STUDY APPROACH

The case study approach in the empirical studies is an attempt to understand and explain the nature and organisational role of accounting as it is practised in a specific organisational context. This organisational context is crucial in providing a background for understanding how the accounting system is interpreted (Hopper and Powell 1985; Carruthers 1995) and enacted as an organisational routine (Hopwood 1990; Scapens 1994).

The consequences of accounting change are difficult to predict without understanding the process of change within the context in which it unfolds, and from the perspective of those directly involved with the process. Therefore, its actual role during organisational reform is difficult to determine in advance because the role of accounting might be shaped by the context, and this role in turn might shape that context.

Since accounting is implicated in social and organisational practices (Burchell *et al.* 1980), the traditional and technical approach, which ignores the context in which accounting operates, is not able to fully explain the actual role of accounting in a specific organisational setting. The case study method provides an appreciation of the social context in which accounting information is used and the natural setting in which the accounting practices emerge (Scapens 1990).

The broad and common concern of the five selected case studies was to empirically explain how the organisational members in public enterprise settings enacted, and used accounting. The way organisational members interpret and socially construct their day-to-day accounting practices explain why accounting is or is not used instrumentally for changing behaviour or ways of thinking.

It was an interesting puzzle that accounting became detached in certain settings and not in others; even though profitability is important for survival in all five cases. The findings from the five case studies were analysed for repeated and common issues, to explain their underpinning reasons and understand them in the context in which these findings were raised.

THE FIVE STORIES OF ACCOUNTING CHANGE

The first story by Abu Kasim (2004) is an in-depth case study of PSP, a disguised name for a Malaysian public utility company being subjected to the pressures of corporatisation. PSP was expected by the government to transform itself into a self-financing, efficient and profitable organisation to facilitate its future divestiture. Consequently, the need to transform PSP into a businesslike entity was not created by market forces, nor PSP's internal needs (as it was profitable), but rather by government policy. As profitability became increasingly important during corporatisation, attempts to enhance profitability were made through imposing new budgeting system and recruiting new accounting graduates. A new budgeting system was introduced in a deliberate attempt to emphasise cost control and accountability on the operations floor. In spite of these attempts, the finding reveals that accounting changes were enacted, but over time detached from operational concerns.

The preoccupation of the State accountant[1] in promoting cost-savings through mechanical compliance with accounting rules from the headquarters, and in attempting to improve financial visibility through a hierarchical form of accountability (Roberts 1991) overlooked the importance of making accounting information

[1] State Accountant refers to the position of the accountants at the state offices. State offices are the regional offices located in almost every state in the country.

accessible, understandable and relevant for the operations managers. As it was, the centralised budgeting system did not allow sufficient flexibility and empowerment of local decision-making. This constraint imposed by accounting failed to secure the trust of the operations managers to use accounting as a mechanism for enabling change. In short, the lack of change shaped by accounting practice could be attributed to the enactment and perception of accounting as a centre of calculation rather than discretion (Quattrone and Hopper 2001). Over time, the budgets evolved to become a source of conflict, implicated with issues of trust and power, and were not widely drawn upon or accepted by the operations managers.

The analysis showed that resistance, which led to the ritualistic use of the budgets by the operations managers, was due to the powerful embedded ways of thinking, the strategic deployment of power to maintain the existing power relations, the imperatives of the continuity of public service provision, and the lack of sufficient trust to cooperate in securing mutual benefits. Resistance enables the flexibility and autonomy of the operations managers to continue to concentrate on the provision of services. In this way, within PSP, the stability of the dominant public service 'ways of thinking' or 'institution' occurred simultaneously with the changes in the accounting system.

The second story of accounting change in Euro Rail, a disguised rail company, by Dent (1991) demonstrates a successful transformation from the public railway culture that stresses social service to a business culture that pursues profitability. The term 'culture' is comparable to the terms 'way of thinking' and 'institution' which were used in the case study of PSP. Dent conceptualises the reconstruction of the organisational culture as a process of 'uncoupling of activities from the railway culture and their recoupling to the business culture' (ibid: 724). Both Euro Rail and PSP faced changing environments, especially from the government's challenge that they have to become modern and businesslike through incorporating private sector management practices. The recruitment of accountants in PSP and the Business managers in Euro Rail symbolised an image of modernity that was important for securing legitimacy from the government.

How change was enacted and accomplished in both organisations was concerned with power and influence. A new culture can be a major source of power, particularly if it gains ascendancy to become dominant' (ibid: 708). In contrast to Euro Rail, the internal power struggles in PSP between the accountants and the operations managers did not lead to the dominance of accounting for influencing meanings. In Euro Rail, as well as in PSP, the incompatibility between the public service culture and the business culture created tensions between the pursuit of social services and profitability. However, such tensions were necessary in order to challenge the prevailing institutions, and subsequently to replace them with the new business ways of thinking. But in PSP, the challenge led to unintended consequences, namely the lack of trust and the ritualistic use of the budgets that undermined the role of the State accountants. The puzzle is why, given the same challenge facing both organisations, the meanings and significance attached to accounting change differed so fundamentally.

In Euro Rail, the competent Business managers, imported from outside, were the social agents who brought and instilled a new profit-oriented culture. They had broad business skills and experience and successfully introduced change through persuasion: 'It was all about relationships. We (Business managers) had to persuade everyone around us' (ibid: 717). To minimise resistance, change was introduced incrementally, and not in a threatening or difficult way. In PSP, the accountants were a new breed, just like the Business managers in Euro Rail, but being *new* graduates in accounting they lacked business experience and skills and tended to adopt the imposed rule rather mechanically.

In PSP, there were limited interactions, persuasion and relationship building over time. In contrast, the Business managers in Euro Rail built relations and secured support from the top management in their endeavour to gain influence and power. Furthermore, in PSP accounting tended to serve the hierarchical and statutory reporting requirements, rather than the needs of the operations managers. In PSP, the operations managers are powerful due to their senior positions and expertise in operations, and they have strong support from their superior, i.e. the State manager[2], in the pursuit of operational goals. They can easily mobilise their power to hinder the direct involvement of the State accountant in their affairs. In PSP's broader context, corporatisation had no intention to de-emphasise PSP's social obligations, since the public service obligations were actually strengthened through regulation. The strong enforcement of the regulatory body did not promote the 'uncoupling of activities' from the mandated social service concerns.

The study conducted by Ogden (1995) of the privatised water industry shares with the studies of PSP and Euro Rail the need for accounting change as a means of cultural transformation. In Ogden's work, privatisation exerted pressures on the Water Authorities to transform themselves into profit-making entities. In the transformation process, the role of accounting as an economic discourse was evident in the use of the language of efficiency and cost effectiveness to construct a new organisational reality. As a whole, the findings across the water industry show that accounting played a constitutive role in 'redefining organizational objectives, changing the meanings ascribed to organizational activities, and reshaping perceptions of what are critical issues' (ibid: 214). Internal resistance due to the incompatibility between the engineering demands and business priorities was only briefly noted, but initiatives such as delegated budgets, cost centres, new management information systems and reward systems successfully promoted financial accountability.

An interesting contrast between PSP and the United Kingdom Water Authorities is the greater emphasis placed on the economic rationale by the regulatory body for the United Kingdom water industry. The regulator set the price based on a standard formula, but the intention was not simply to stabilise the price, but also to promote "yardstick" competition (Ogden 1995: 197). Yardstick competition was intended to enable the regulator to promote cost competition between the different water companies through price control. The costs of the most efficient companies in the industry were incorporated into the pricing formula in computing and enforcing new prices. Accounting information was therefore drawn and acted upon by both the regulator and the companies to achieve cost savings. In the case of PSP, the government imposed a price freeze for the past ten-year period; and the regulator had to enforce those prices. This long duration and the lack of a systematic procedure for price revision reflect the government's predisposition to socio-political rather than cost and profitability issues. In spite of the corporatisation exercise, PSP was still treated as a public utility by the Malaysian government. The detachment of the budgeting system in PSP could be attributed, at least in part, to these socio-political demands of the regulator and the government.

Alam (1997) investigated the role of budgets by contrasting the budgetary process in two of Bangladesh's, commercially-oriented public enterprises involved in the processing of jute and sugar respectively. Although the study excluded internal organisational processes, the intertwined institutional and technical environments and the process of preparing budgets are comparable with the context of PSP. It was interesting to note that despite being subjected to similar institutional pressures, the sugar firm was able to deploy a more attached budget called the 'working budget' (ibid: 158). This budget was instrumentally involved with organisational activities because the 'budget estimates are always formulated at the lowest level where the activities are actually performed' (ibid: 158). In contrast, jute's budgeting process involved the imposition of often unrealistic production targets by the government for socio-economic purposes such as maintaining employment and avoiding labour unrest.

In Alam's case studies, the detachment of accounting in jute was due to the irrelevance of the government's imposed budget targets for the daily organisational activities. The imposed budget targets, either by the accountants in PSP or the institutional environment in jute, were prepared in isolation from the needs of the operations. However, imposition is an incomplete explanation for the detachment as was attested by PSP's intra-organisational budgeting process. For PSP, detachment also served the operations

[2] State manager heads the state or regional offices. He reports directly to the Chief Executive Officer at the headquarters.

managers' intentions of deliberately avoiding following rules that threatened to limit their flexibility and erode their power in local decision-making. It was also risky for them to trust and cooperate with the accountants by adhering to the budgeting rules.

In the final case study by Vamosi (2000), the story of BCW, which is a privatised Hungarian company, involved a deliberate attempt to use accounting for the transition from a government to a privately-owned company. BCW, with an established history of 125 years, became a privatised entity which was subjected to the new 'market disciplines', and was required to construct a new organisational identity. It now had to be 'in charge of securing its own survival' (ibid: 45) because the government relinquished its responsibilities concerning both ownership and management. Survival in the new market environment created the need for BCW's accounting system to be redefined and reconceptualised. In Vamosi's words, 'accounting practice is a target for change and an instrument in the process of generating a new constitution and institutionalization' (ibid: 28, emphasis in the original). There are parallels between BCW and PSP in terms of accommodating the new economic demands from the environment, and the pursuit of financial survival through accounting change.

As organisational change is a process that is ongoing, both PSP and BCW had to confront the 'cargoes-of-thoughts' (ibid: 27) or previously embedded ways of thinking carried over from the government era. The process of adapting to change was shaped and constrained by the institutions inherited from the past. An equally important observation in both PSP and BCW was the lack of the technically and professionally qualified organisational actors for understanding the rules and meanings of the new accounting system. Hence, the cognitive constraints in terms of the institutions and the low financial literacy limited the acceptance and the mobilisation of accounting for constructing the new reality. The lack of use of accounting led to continuity of the old reality. However, while BCW was unable to recruit qualified graduates, PSP recruited accountants from outside, but, as mentioned earlier, they lacked the wider essential business skills and experience to manage change.

COMPARING INSIGHTS OF THE CASE STUDIES

In summary, although all the organisations faced a strong influence from the environment, their comparison indicates some variety in the use of accounting information and its effects and effectiveness as a mechanism for infusing new meanings and values. Detachment of accounting, in terms of its lack of use and effect, was observed in some cases but not in others; the powerful role of accounting for attaining economic efficiency, assumed by the governments could not be generalised across all contexts.

The successful 'recoupling to the business culture' (Dent 1991: 724) resulted in promoting the use of accounting as the new organisational knowledge. Such use was possible through the strategy of persuasion and influence developed by the Business managers. The implementation of changes had the support of the top management, but was not perceived as an imposition that was drastically done, and directly came from the Business managers. Relative to the mechanistic and imposition method of exerting change in PSP, the way change was introduced and later enforced in Euro Rail led to the acceptance of the Business managers as effective and powerful change agents.

Privatisation of the United Kingdom water industry and corporatisation of PSP did not result in increased market competition. Instead these utilities are maintained as monopolies, but subjected to similar interference by the government through regulation. However, on one hand, in the United Kingdom water industry, the institutional environment enabled cost competitiveness through price regulation; PSP's environment exerted regulative and normative constraints through a price freeze on the other. Clearly, the objective of regulation differs in that the emphasis in PSP was more on the social aspect, while in the United Kingdom water industry, it was more on the economic aspect.

As mentioned above, the differing emphasis in regulation partially explains the detachment of accounting in PSP. The existence of both price stability and limited competition, results in less incentive for PSP to improve its cost-savings performance through the use of accounting information. Although both governments engage in regulation to curb the monopoly powers of the utility entities, the impact of the regulation in Malaysia appears to reinforce the intra-organisational conflict between public service and profitability goals. The Malaysian government interferes through the government regulatory body primarily to protect public interests than to maintain incentives for higher economic efficiency.

Similar to Alam's work, the government of Bangladesh through the Ministry interferes in the operations of jute through price fixing and enforcement, rather than economic purposes. The budgets became rituals because they were made to follow the requirements of the government rather than the daily operations. In PSP and jute, the non-economic aspects of interference by the governments contribute to explain the marginal use of the budgets for economic decision-making. The strong influences by the Bangladesh and Malaysian governments ensure that public enterprises continue to pursue multiple social and economic objectives. Ineffectiveness of accounting, in terms of its marginal role in operations, is due to the strong influence and role of institutional pressures. In BCW and PSP, financial survival drove accounting changes but the internal institutions – the established ways of thinking from the previous government entities - continued to exert influence and shaped the way in which accounting change became detached and not drawn upon for internal activities. While economic imperatives in the environment stimulate commercial and financial changes, organisations such as PSP, jute firm and BCW were still constrained by social responsibility, government interference, and old workforce. Consequently, these studies show that ceremonial enactment of accounting change can result in continuity or stability of the old ways of thinking.

In summary being entities in the public domain, new economic demands from the government are accommodated within all the case organisations. These public enterprises pursued financial survival through accounting and organisational changes. The results from accommodating the environmental pressures to change through accounting had an uneven impact, depending on how it was drawn upon by organisational members.

IMPLICATIONS

All the above stories share the need for accounting to change as a means of transforming themselves into profitable organisations. In some stories, accounting plays a marginal role in operations due to several reasons such as interference from the government, the established ways of thinking from previous government entities, social interactions which include trust and power issues. These issues question the potential of the new accounting system to create a new organisational reality (Hopwood 1990) with profitability as an important agenda. The findings imply that the process of accounting change and its effects and consequences cannot be rationalised on purely technical grounds, and in isolation from the context in which the information is produced and used.

Since the detachment of accounting system is a contingent and contextual phenomenon, the case study approach will continue to be useful for explaining the phenomenon in future and further studies. According to Keating (1995: 66), 'case study research is certainly one means for accounting researchers to develop an intimate, contextually sensitive knowledge of actual management accounting practices'.

For policy makers in the area of public sector reform, in particular in the Malaysian economy, the story of PSP should raise questions about the appropriateness of commercial accounting[3] for enhancing the economic efficiency of all public enterprises. Little consideration has been given to the 'unpredictable' impact of economic reform, contextual differences between organisations, and whether these differences matter when reforming each unique organisation. Policy makers can no longer take for granted that private sector accounting is an instrumental and sufficiently powerful means to achieve profit-oriented ways of thinking and behaving.

As shown in Dent's case study, managing change is about managing relationships and effective persuasion to reduce resistance from other organisational members. For accountants to manage change, they need to interact and secure the trust and confidence of other

[3] Commercial accounting is the term used in the corporatisation policy to indicate the private sector accounting.

members in the organisation. Technical skills without interpersonal skills will not be sufficient to secure other members' cooperation and commitment to use accounting information in the intended manner. Thus, an important implication is that learning outcomes in the teaching and learning of accounting should include both the technical and interpersonal skills.

CONCLUSION

The stories of accounting change provide some insights into the complexity due to the non-technical issues involved in implementing accounting change during financial reform. The lack of uniform effects from accounting practices supports the claim that accounting is not simply a technique but a social and organisational practice that can have a variety of possible but unpredictable effects on organisations. Its implementation was not narrowly and simply concerned with accounting techniques and rules that would inevitably be followed in the spirit of financial management reform.

As case study findings are context-specific, the idiosyncrasies of the findings hinder their possible generalisation to other contexts but are incorporated here in order to enhance understanding of the role of accounting during financial reform. Lack of generalisation in case studies is however compensated by the holistic and in-depth study of each specific organisation. Since financial management reform in the public sector is an international agenda, further research in terms of collaboration in various natural settings can further improve the comparisons and the search for explanations of the different or similar consequences from implementing accounting. These explanations are invaluable for improving and enhancing the effectiveness of the financial transformation of public enterprises.

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