Public sector reform
Implications for accounting, accountability and performance of state-owned entities – an Australian perspective

Zahirul Hoque and Jodie Moll
School of Accounting and Finance, Griffith University, Gold Coast, Queensland, Australia

Keywords Public sector reform, Public sector accounting, Australia

Abstract Faced by increased globalization, the dissatisfaction of Australian citizens, and a curtailing of spending, the Australian Government has embarked on a major reform agenda centered on new public management ideals to achieve greater economy, efficiency, and effectiveness. A major driver of reform in all levels of government has been the introduction of the national competition policy. Describes the recent developments in Australian public sector and discusses reform implications for accounting, accountability and performance in Queensland local governments. Suggests that accounting plays a significant role in promoting accountability, efficiency and effectiveness of public sector services.

Introduction
In recent years, the Australian Government has embarked on a wide range of financial and administrative reforms. These reforms have two broad themes: those which concentrate on the management control system (MCS) by improving the information provided by the accounting systems, clarifying roles and responsibilities and creating accountability; and those which account for stabilizing the economy by exposing the public sector to competition (Competitive Tendering and Contracting by Public Sector Agencies, 1996).

At the national level the two main objectives of the reform process are to: promote a culture of performance; and to make the public sector more responsive to the needs of Government by increasing the organizations’ accountability, promoting efficiency and effectiveness, introducing participative decision making and adopting a customer focus. At a broad level, the financial reform agenda includes such things as financial reporting, accrual accounting, full cost pricing, purchaser/provider agreements, and asset management. The administrative reform encompasses, but is not limited to, structural reforms, labor reforms, the review of information systems and accountability reforms. These reforms are centered on new public management (NPM) ideals (Hood, 1990a, 1990b, 1995a, 1995b).

The introduction of NPM in the public sector has seen a shift in focus from the adherence of formalized procedures to an emphasis on resource allocation and goal achievement (Aucoin, 1990). Briefly, NPM encompasses the following ideas:
- from management’s perspective, the public and private sector are not
dissimilar and therefore should be managed on the same basis;
- the shift in focus from process accountability to accountability for
results;
- the separation of commercial and non-commercial business activities;
- an emphasis on improved financial reporting, monitoring and
accountability;
- 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; and
- an emphasis on cost cutting and efficiency.

The purposes of this paper are twofold. First, it examines the recent
developments in the Australian public sector in general and, more specifically,
in the context of Queensland Local Government. Then, it assesses how these
reforms provide motivations for public sector entities to change their
accounting, accountability and performance systems. The paper concludes
with some suggestions for future research in the field.

**Reform of the Australian public sector and the national competition policy**

*Importance of the reform*

A range of social, economic and technological pressures are forcing
governments to become more effective, efficient and accountable for the use of
publicly generated funds. In particular, Rivlin (1996), Sansom (1997) and
Wensing (1997) claim that governments are pressured from increased
globalization, the dissatisfaction of citizens with the current management, and
a curtailing of budget spending. Mellors (1995, p. 1) contends that there are six
key forces driving the change in the public sector, including the following:

1. changing attitudes to the role of government in the economy;
2. the process of micro-economic reform;
3. changing community and business expectations;
4. resource constraints;
5. the impact of technology; and
6. demands for greater accountability.

It has been suggested that reform of the public sector will have the following
outcomes (Management Advisory Board, 1997, p. 2):
The national competition policy
The major catalyst for change of Australian public sector organizations has been the national competition policy (NCP). The Independent Committee of Inquiry (1993) claimed that Australia needed such a policy for three reasons. Firstly, Australia has become a single, integrated market because of advances in technology and transport. This means the economic significance of state boundaries is reduced and therefore firms are able to trade interstate. The second factor identified, which suggests that a NCP is essential to the economic wellbeing of the nation, is a review of the Trade Practice Act. The existing Act imposed restrictions on certain sectors of society reducing their ability to compete in the market. Finally, the Independent Committee of Inquiry claims that although various reforms have been implemented on an individual sector basis (i.e. at either the commonwealth level, the individual state level or the individual local government level), a broad reform of all tiers of government is necessary to promote nationally consistent approaches and reduce the costs of establishing industry-specific reforms (Independent Committee of Inquiry into a NCP, 1993). In short, the application the NCP prescribed that public sector entities should be operating according to the same commercial principles as the private sector, if they are to become more economic, efficient, and effective. Consequently, a series of the financial and administrative reforms have been introduced.

The increase in globalization sought the need for the Australian economy to increase competition to sustain improved living standards. In October 1992, a committee, headed by Professor Hilmer, was commissioned by Prime Minister, Paul Keating to undertake an independent inquiry into the need for a national policy aimed at “promoting and maintaining competitive forces to increase efficiency and community welfare, while recognizing other social goals” (Independent Committee of Inquiry into a NCP, 1993). In August 1993 the commission presented the proposals from its inquiry to Government (Queensland Government, 1996a). These proposals are what is now referred to as the NCP. NCP is built on the premise that increasing competition and leveling the playing field between the public and private sector will lead to an improved use of national resources. According to the Independent Committee of Inquiry, “Competition offers the promise of lower prices and improved choice
for consumers and greater efficiency, higher economic growth and increased employment opportunities for the economy as a whole” (Pascoe, 1994, p. 35). As suggested above, the impetus for introducing such a policy stems from the demand for improved use of resources and ultimately a higher standard of living (Queensland Government, 1995; 1996a). NCP seeks to do this by encouraging the structural reform of public monopolies, ensuring government business activities operate on a level playing field with the private sector, providing competition across state boundaries through the development of national markets, providing efficient pricing, controlling market abuse by government monopolies, applying the same anti-competitive rules to business activities regardless of ownership, facilitating access to essential infrastructure and abolishing legislative restrictions to competition (Independent Committee of Inquiry, 1993). These elements are illustrated in Figure 1.

In 1994, the Council of Australian Government (COAG) agreed to reforms set out in NCP. In 1995, along with Commonwealth, and other State and Territory governments, the Queensland Government accepted the three agreements of NCP: the Conduct Code Agreement, the Competition Principles Agreement (CPA) (Commonwealth of Australia, 1995) and the Agreement to Implement National Competition Policy and Related Reforms Revision (Queensland Government, 1996a). These agreements provide a framework for the implementation of NCP. Briefly, the conduct code agreement extends the

**Figure 1.**
NCP elements
competitive conduct provisions of Part IV of the Trade Practices Act (1974). Conversely, the CPA encompasses a new set of principles to address other forms of anti-competitive behavior. The five elements of the CPA are: third-party access, prices oversight, structural reform, competitive neutrality and a legislative review (Queensland Treasury Department, undated a). The agreement to Implement National Competition Policy and Related Reforms Revision is a timetable of the implementation of NCP and COAG agreements relevant to specific industries such as water, waste, electricity and roads revision (Queensland Government, 1996a). Although local governments did not participate in the acceptance of the agreements of NCP, Section 7 (1) of the CPA states that the principles of NCP will also apply to local government. The CPA further stipulates that the individual state and territory governments determine how NCP is to be applied at the local government level. Subsequently, in Queensland, the Local Government Act 1993 has been used to facilitate the implementation of NCP to local governments (refer to Section 543).

More specifically, Chapter 8 of the Local Government Act “National Competition Reform of Significant Business Activities” classifies the local government business activities into “type 1”, “type 2” and “type 3” activities for the purpose of applying the intergovernmental agreements (i.e. The Code of Competitive Conduct, The CPA and The Agreement to Implement National Competition Policy and related reforms revision). In accordance with the Local Government Act, water and sewerage activities are classified as a type 1 activity if they exceed the expenditure threshold of $28.1 million for 1997/1998. For other activities the minister set an expenditure threshold of $16.8 million for the 1997/98 financial year. Type 2 activity expenditure thresholds are $8.4 million for water and sewerage activities for the 1997/1998 financial year and $5.6 million for other activities during the same period (Local Government Act 1993). Type 3 activities are subject to the Voluntary Code of Competitive Conduct.

To date, eight local government activities in Queensland have been categorized as a type 1 business activity and 17 have been categorized as type 2 business activities (Section 545). Subsequently, NCP has been applied to those business activities where the introduction of increased competition results in improved socially beneficial outcomes. The elements of the NCP are now discussed below in turn.

Trade Practices Act 1974
In theory, the Trade Practices Act (TPA) sets out rules that promote competition, thereby reducing anti-competitive conduct. Prior to the introduction of NCP the majority of government businesses were not required to abide by the TPA and therefore operated with significant advantages to their private sector counterparts (e.g. tax exemption, department cross-subsidies). The NCP redressed these disparities through an agreement with the Commonwealth and State Governments which came into effect from July 21 1996 to extend the coverage of Part IV of the TPA to the unincorporated sector
and government entities (Fels, 1999; Queensland Treasury Department, undated b; McTaggart, 1996). The result of this that government entities cannot demonstrate any anti-competitive conduct such as price fixing, resale price fixing, third line forcing or primary boycotts in the provision of products or services (ACCC, 1996).

Third-party access
The aim of third-party access is to promote competition by providing business owners with access to significant infrastructure. More specifically, third-party access reduces the ability of the owners of significant infrastructure to control the market by preventing competitor access to their infrastructure. At present, third-party access has been applied at the Commonwealth and State Level of Government (Queensland Treasury Department, undated c). According to the Queensland Treasury Department, the purpose of third-party access to infrastructure is to ensure that competition is not reduced in industries which rely on monopolies in their production processes (McTaggart, 1996).

Prices oversight function
Similar to the other elements of NCP, the prices oversight function aims at removing the significant advantage governments may operate under. Specifically, the prices oversight functions’ purpose is to control government entities that are monopolies or near monopolies from over pricing their goods and services (Queensland Treasury Department, undated d).

Structural reform
According to the Department of Treasury (Queensland Treasury Department, undated e), structural reform refers to the restructuring of either individual businesses or the market in which the businesses operate. Most of the monopoly businesses in Australia are government owned. For instance, state and local governments often own gas and electricity businesses. The purpose of the structural reform is to introduce such markets to competition. In conjunction with amendments to the TPA, the structural reform requires a review of all government-owned monopolies. This means that monopolies are assessed to determine the benefits to be gained from commercialization, corporatisation or even privatization. The CPA specifies that each state or territory government is free to decide on its own agenda for the reform of public monopolies. The CPA requires that all governments, whether they are commonwealth, state or local, investigate the following issues arising from the possible structural reform of public monopolies. Firstly, business units are required to operate according to industry regulation so new competitors entering the market are not disadvantaged. In addition to this, a structural change to monopoly businesses requires those businesses to determine commercial objectives. Thirdly, the CPA requires governments to separate monopoly elements from competitive elements. The structural reform also requires the introduction of competitive neutrality. The fifth issue of concern is
the value of community service obligations. Finally, governments are required to determine the appropriate financial relationship between the owner of the public monopoly (whether it is government or private) and the public monopoly in terms of tax implications, the rate of return required, dividends and the appropriate capital structure (Queensland Treasury Department, undated e). In Queensland these issues are being addressed in conjunction with the corporatisation/commercialization process (Queensland Treasury Department, 1996a).

**Competitive neutrality**
The Queensland Treasury Department (undated c, p. 9) defined competitive neutrality as “the process of identifying and, where appropriate, removing any advantages (and disadvantages) that may accrue to a government business by virtue of its government ownership”. Possible advantages resulting from government ownership include: tax exemptions; regulatory advantages; explicit or implicit government guarantees on debts; immunity from bankruptcy; concessional interest rates on loans; and cross-subsidization. However, there are also disadvantages to operating as a government entity. These include limited markets, greater accountability obligations, reduced managerial autonomy, requirements to comply with government wages, employment and industrial relation policies and the fact that the government provides many goods and services to the community that could not realistically be provided by a private sector organisation without high costs to the consumer (Independent Committee of Inquiry into a National Competition Policy, 1993). The Independent Committee of Inquiry (1993, p. 297) stated that where these disparities exist, there is a “potential to reduce economic efficiency and community welfare by distorting the allocation of resources”. The aim of competitive neutrality therefore is to introduce measures to address the disparities resulting from government ownership (Queensland Government, 1996d).

Following the efficiency arguments in favor of competitive neutrality there are also three arguments, which suggest that introducing such an element could be to the detriment of the Australian economy. Firstly, the corporatisation of government monopolies could lead to service deterioration and price increases. In addition to this, adopting a commercial focus suggests that those business activities not providing an adequate rate of return on their assets should be abandoned. This would mean that some of the essential services provided by the government would cease to exist. Finally, with the adoption of full cost pricing, governments may conclude that services are costing more than they have been charging and therefore prices will increase and access to those products will decrease (Queensland Government, 1996c).

The CPA states that each of the governments which agreed to national competition should be free to set its own agenda for the implementation of competitive neutrality. The Queensland Government suggests several means through which competitive neutrality can be achieved: corporatisation;
commercialization; and full cost pricing (Queensland Government, 1996c; Queensland Treasury Department, undated f). Legislation passed in Queensland in 1996 required that 17 of the largest councils conduct a cost/benefit analysis of their significant business activities to determine if they would benefit from the reform of full cost pricing, commercialization or corporatisation. These councils were chosen based on the fact that they operated activities with a budget in excess of the type 1 and type 2 activity threshold set out in the Local Government Act 1993 (Queensland Government, 1995; Queensland Government 1996a). Full cost pricing, commercialization and corporatisation are further described below.

**Full cost pricing**

Full cost pricing, otherwise known as the full economic costs of operations, is the first step towards achieving commercialization (see Figure 2). Full cost pricing, according to Section 568 of the Local Government Act, “means that prices are charged for goods and services taking into account the full cost of providing goods and services”. It is adopted where activities would benefit from reform but not as a separate business unit. The main rationale for adopting full cost pricing is to enable governments to make the full cost of operations transparent, thereby enabling them to recover those costs. Full cost pricing requires costs such as office rentals, payroll, subsidies, depreciation and taxes to be accounted for.

**Commercialization**

Commercialization, according to the Commonwealth Department of Finance (1996), is the “introduction of a commercial financial framework into government entities leading to corporatisation and/or a process by which markets are established for selected public sector goods and services in order to increase competitive pressures on suppliers”. Specifically, the Local Government Act outlines the objectives of commercialization at a local government level to be an improved economic performance and also an increase in the local government’s ability to carry out its responsibilities for “good rule and government” (Section 572). This is to be achieved through the establishment of efficient and effective commercial business units and the introduction of a framework for the operation and accountability of those units.

Commercialized entities are recognizable as separate business units within government entities. In addition to providing goods on a full cost basis, commercialized business units are encouraged to adopt a commercial framework, or commercial principles similar to those of the private sector.

![Figure 2. Stages of competitive neutrality](image-url)
(Fellew and Kelaher, 1991). Fellew and Kelaher (1991) contend that the adoption of commercial management principles is fundamental to improved business management. The underpinning principles of commercialization as set out in the Local Government Act (see Section 576) are: clarity of objectives, management autonomy and authority, accountability for performance and competitive neutrality.

Several key areas are proving to be problematic in the commercialization process. These include full cost pricing, the treatment of community service obligations, and the elimination of disparities resulting from government ownership (Local Government Finance Standard, 1994). Specifically, local governments are faced with the problem of determining the extent to which competitive neutrality should be applied to their business units. This requires them to decide the appropriate business structure, information systems, and accountability systems of those commercialized units.

Dixon et al (1996) claim that the extent to which business units commercialize is dependent on five factors, including the recovery of costs, the extent to which market competition is restricted or unrestricted, the adoption of both commercial and non-commercial goals, the replacement of government funding with consumer charging and the retention of revenue.

The Queensland Government has identified three stages of commercialization: establishing a general business environment between clients and service providers, partial commercialization and full commercialization (Queensland Government, 1996c). In addition to NCP, the Queensland government has also embarked on a competitive tendering reform, which is also known as the purchaser/provider or specifier/provider reform. In short, purchaser/provider arrangements are “initiatives which distinguish between a public sector purchaser who decides what will be produced and a provider who may or may not be in the public sector, who delivers the agreed outputs and outcomes” (Commonwealth Department of Finance, 1996). This reform has been linked to the stages of commercialization (Queensland Government, 1996c).

The first stage of commercialization involves the identification of products to be provided, costs, prices and performance standards (Queensland Government, 1996c). The second stage is more complex. It involves the creation of formal trading relationships or intragovernmental relationships between departments. The second stage also involves the introduction of commercial pricing principles. The advantage of the purchaser/provider reform at this stage is that local governments are forced to specify desired outcomes and requirements on the provider (Competitive Tendering and Contracting by Public Sector Agencies, 1996).

Full commercialization of a business entity (stage 3) occurs when the purchasers are free to adopt a competitive tender process. This involves the local government paying an external or in-house provider a set fee for the delivery of service for a specified period of time. The rationale behind such an arrangement is that the competitive pressures generated through the tendering
process will lead to the best value for money (Harris, 1998). Johnstone (1999) suggests that such relationships are becoming more common as outsourcing has the potential to provide significant reductions in cost to the taxpayer. Some of the most common services contracted out by local government are auditing, catering, cleaning, information technology, security, fleet management, courier services, payroll and transport (Sciulli, 1996). Other advantages noted from a Competitive Tendering and Contracting Inquiry were outlined as increased flexibility in service delivery, greater output focus, innovation and cost savings (Kelaher, 1991a). More importantly, perhaps, is the fact that contracting out encourages local government to focus on strategic issues instead of the day-to-day-operations. There are, however, limitations to the contracting out process. Firstly, providers in the private sector may not be willing to comply with the same public sector accountability standards imposed on government departments. Additionally, considerable monitoring and contracting costs are borne by government in the contracting out process.

Issues such as a comparison of costs between in-house bids and outsourcing costs remain central to the purchaser/provider arrangement (Hazell, 1997). For example, an in-house bid consists of determining all of the costs of providing that service within the entity. This includes, for instance, wages, rent, and service delivery costs. Thus, in-house bids under the purchaser/provider arrangement are treated in the same manner as the external tender. It is important to note, however, that there are possible advantages to an in-house bid over its external counterparts. In particular, the purchaser is able to monitor complex activities (Harris, 1998). The disadvantages of such an arrangement also need to be considered before accepting in-house bids. In addition to the risks inherent with keeping the activity within the council, the local government is still responsible for the cost of failure to provide that activity. Therefore, services should only be contracted out when it results in a reduction in costs to the entity.

**Corporatisation**

Corporatised entities operate under an environment not unlike that of the private sector. This implies that the advantages or disadvantages realized with government ownership are eliminated. Corporatised entities operate under the same principles as commercialized entities. That is, they operate according to the following principles: clear and non-conflicting objectives, managerial responsibility, authority and autonomy, effective performance monitoring by the owner government, attained competitive neutrality and effective monopoly regulation (Independent Committee of Inquiry, 1993). The aim of these objectives is to increase the efficiency and effectiveness of business operations. Specifically, a corporatised entity obtains most of its funding via the public through principles such as user pays. Introducing commercial principles such as user pays and the separate legal entity concept means that corporatised entities are subject to whole range of corporate finance issues including the capital structure, the commercial rate of return, the dividend policy, and asset
Corporations Act (GOC Act) currently governs the corporatisation of
Queensland business activities (Queensland Government, 1996c).

The main difference between a corporatised entity and a commercialized
entity is that a corporatised entity is considered a separate legal entity, owned
by Council and supported by a corporate governance structure (Queensland
Government, 1996a). This means that the corporatised entity is under the
direction of its own board of directors.

**Legislative review**

The Queensland Department of Treasury claims the application of NCP will
not remove entirely the existing operating advantages of government
entities entering commercialization or corporatisation. The CPA specifies
that a legislative review is necessary to determine if the advantages
exercised by government entities are in the public interest, and to determine
if the objective of the legislation can only be achieved through the
restriction of competition. Furthermore, the agreement suggests that the
review of legislation will not only identify the nature of restrictions but also
consider alternative solutions to achieving the same result (Queensland
Government, undated g). In keeping with the reform, state governments
have begun a review of State legislation. At a local government level any
State legislation that encourages anti-competitive conduct that is also
applied at a local government level (i.e. Local Government Act) is to be
reviewed, along with the State NCP Legislative Review (Queensland
Government, 1996a). Additionally, local laws are to be reviewed by their
respective councils (Queensland Government, 1996a; Queensland Treasury
Department, undated h). The time frame set for local governments to have
reviewed their local laws is June 1999. In summary, the National
Competition Policy elements are set out in Table I.

**Government regulatory bodies**

This section briefly discusses the Australian government regulatory bodies,
which shape the activities of public sector entities.

**Australian competition and consumer commission**

The Australian Competition and Consumer Commission (ACCC) emerged from
a merger between the Trade Practices Commission and the Prices Surveillance
Authority on 6 November, 1995. The purpose of this body is to enforce the
provisions of Part IV and Part V of the TPA and the Prices Surveillance Act
1983 to all levels of government (ACCC, 1999).

**National competition council**

Recommended as part of NCP, the National Competition Council (NCC) was
established to advise governments on a variety of issues including pricing
matters, competitive neutrality matters, transition issues, the declaration of
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<th>Policy element</th>
<th>Purpose</th>
<th>Example</th>
<th>Supporting agreement/legislation</th>
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<tr>
<td>1. Extension of coverage of Trade Practices Act</td>
<td>To limit the anti-competitive conduct of business entities, regardless of their ownership</td>
<td>Coverage of part IV of the Trade Practice Act is extended to the unincorporated sector (including the professions), and state and local governments where they are carrying on a business</td>
<td>Conduct Code Agreement and Competition Policy Reform Act</td>
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<td>2. Third-party access</td>
<td>To provide a third party with access, at “fair” prices and conditions, to facilities that are essential for competition (i.e. a third party is someone other than the owner/supplier of the facilitate)</td>
<td>Access by a third party to facilities such as telecommunication cables, gas pipelines and railway tracks</td>
<td>Competition principles agreement and Competition Policy Reform Act</td>
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<td>3. Prices oversight of monopoly of near monopoly government businesses</td>
<td>To prevent the misuse of monopoly powers of Government business activities</td>
<td>Introduction of arrangements similar to the former Commonwealth Prices Surveillance Authority to state and local government business activities which exercise monopoly powers</td>
<td>Competition principles agreement and Competition Policy Reform Act</td>
</tr>
<tr>
<td>4. Structural reform</td>
<td>To reform the structure of Government-owned monopoly businesses to facilitate competition</td>
<td>Division of Queensland Electricity Commission into separate generation and transmission entities, to allow the potential for competition in electricity generation</td>
<td>Competition principles agreement</td>
</tr>
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<td>5. Competitive neutrality</td>
<td>To remove benefits (and costs) which accrue to government business activities as a result of their public ownership</td>
<td>Requirement for government business activities to pay taxes (or tax equivalents); and removal of regulations which provide special advantages for government business activities when competing with the private sector</td>
<td>Competition principles agreement</td>
</tr>
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Table I. The elements of the National Competition Policy
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<th>Policy element</th>
<th>Purpose</th>
<th>Example</th>
<th>Supporting agreement/ legislation</th>
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| 6. Legislative review  | To review (and justify) government business activities as a result of their public ownership                                                                                                         | (At a commonwealth level) deregulation of domestic aviation and telecommunications arrangements  
(At a state level) deregulation of various state-based agricultural statutory marketing arrangements  
State reviews of business regulations  
Restructuring and/or introducing further competition into the electricity, gas and water and road transport sectors | Competition principles agreement                                                                                                                     |
| 7. NCP-related reforms | To further reform key sectors of the economy which are already subject to Council of Australian Government Reforms                                                                                     |                                                                                                                                                                                                         | National Competition Policy and related reforms                                                                                                       |

**Table I.**

Source: McTaggart (1996)

access rights to facilities and regulatory restrictions on competition (Independent Committee of Inquiry into a National Competition Policy, 1993).

**Queensland Competition Authority**

The Queensland Competition Authority (QCA) was established on the 30 June 1997 in accordance with the Queensland Competition Authority Act 1997 (Queensland Competition Authority, 1999). The QCA is a regulatory body primarily established to perform the prices oversight function for both state and local governments. The QCA also regulates third-party access and the competitive neutrality of local governments (Queensland Government, 1996b; 1997).

At a local government level, the QCA’s specific roles relate to assessing the implementation of competition reforms to local government type 1 and type 2 business activities; assessing the implementation of the COAG water reforms, including a two-part tariff and full cost recovery; and assessing councils’ compliance with other competition policy reforms (Queensland Competition Authority, 1999). The Queensland Government has assigned $150 million as incentive payments for those local government bodies which comply with the competition policy requirements.
The Local Government Act

Like many of the other states, the Queensland Government reviewed the Local Government Act 1936 to overcome limitations and restrictions that were preventing it from governing effectively (Wensing, 1997). The Fitzgerald Inquiry originally recognized this need for change. Subsequently, a new Local Government Act was introduced in 1993. In essence, the purpose of the act is to reform government activities and to ensure that local governments remain accountable to the community (Wensing, 1997). Wensing (1997, p. 91) claims that the Local Government Act 1993 provides a “framework for wider micro-economic reforms on local government to improve its performance orientation, its accountability, and its relations with other spheres of government”. In addition to encompassing the National Competition Policy requirements, the Act also prescribed a boundary review of Local Councils. The result of this was the amalgamation of several councils (Wensing, 1997). Vince (1997) claims that the purpose of the amalgamation of councils is to create more efficient and effective organizations. Further to this, she suggests that amalgamations are used to redistribute resources and power and to provide the community with a wider range of community facilities.

Government reform and changes to the accounting standards

The Public Sector Accounting Standards Board (PSASB) recognized the need for uniform public sector standards to govern and drive the accounting changes. In recent years they have responded to this need by developing three specific standards for the public sector, namely AAS 27 “Financial reporting by local governments”, AAS 29 “Financial reporting by government departments” and AAS 31 “Financial reporting by governments”. A second driver of accounting change of local government has been the Local Government Finance Standard 1994 which sets out specific provisions to govern local government accounting procedures such as application of full cost pricing and the return on capital. Section 32(1) of the Local Government Finance Standard also reinforces AAS 27, by advising local governments to comply with the Australian Accounting Standards, the Statement of Accounting Concepts and the Statements of Accounting Practice.

AAS 27 “Financial Reporting by Local Governments” became operational as of December 1990. It was introduced to local governments by the PSASB for two reasons. Firstly, to improve the information provided for decision making through the preparation of general purpose financial reports including an operating statement, a statement of financial position, a statement of changes in equity, and a statement of cash flows. Secondly, to make local governments more accountable to the community through the disclosures of performance, financial position, financing and investing and compliance (Parker, 1998). This standard is in essence a replication of those applicable to the private sector. Due to the unique characteristics of public sector assets, many of the requirements of this standard are proving to be problematic and as such are highly
controversial. A key example of this is infrastructure. To date, managers have voiced their dissatisfaction with the requirements for valuing land under roads, dams and reservoirs and other public structures (for details on this issue, see Hope, 1999; Hoque, 1999; Rowles et al., 1998).

Similar to AAS 27, AAS 29 “Financial reporting by government departments” requires the preparation of general purpose finance reports by those departments which are considered reporting entities (Parker, 1998). The production of these statements also has a twofold effect; to make government departments accountable to external users; and to provide useful information for management decision-making purposes (Parker, 1998). AAS 29 became operational in December 1993.

Developed by members of the accounting profession and governments, AAS 31, “Financial reporting by governments”, operates on a much broader scale than AAS 27 and AAS 29, encompassing two tiers of government: commonwealth; and state and territory. Micallef (1997) asserts that the introduction of AAS 31 will put Australia at the forefront of public sector reporting worldwide. As reporting entities, the commonwealth, state and territory governments will be required to prepare accrual-based general purpose financial reports to discharge their accountability and to improve the decision-making ability of managers and other external users in the allocation of resources (AAS 31 para. 3.2). The number of external users of financial reports increases significantly at this level to include parliamentarians, the public, providers of finance, the media and other analysts (AAS 31 para. 3.2). Micallef (1997) claims that the introduction of AAS 31 will improve decision making through the increased harmonization of reporting reforms across all levels of government. Ultimately, this means that commonwealth and state bodies will be able to compare information between governments and across time. AAS 31 is applicable to those reporting periods ending on or after 30 June 1999.

Public sector reform implications for accounting
The introduction of NCP and other government reforms has had substantial implications for accounting. Traditional accounting in the public sector focused on inputs and the control of expenditure. The reform of the public sector has changed the traditional role of accounting to one that is focussed on accountability and the efficient allocation of resources. This implies that accounting should concentrate upon outputs, performance measurement, efficiency, cost saving, productivity and performance measurement (Broadbent and Guthrie, 1992; Guthrie, 1995). This in turn requires that new accounting technologies be employed such as planning program budgeting, accrual accounting, performance indicators and annual reporting mechanisms (Guthrie, 1995; Bishop, 1997). The following section describes the motivations for public sector entities to change their accounting systems.
Accrual accounting
The government has moved from cash-based accounting to accrual accounting in response to commercial principle adoption (Fellew and Kelaher, 1991). Briefly, cash accounting requires the record of inflows and outflows of cash. Conversely, accrual accounting requires revenue to be recognized in the period in which economic benefits can be measured reliably. Likewise, expenses are recognized when the consumption of goods is capable of reliable measurement (Hoggett and Edwards, 1996, p. 113). There are several reasons why the move to accrual accounting was inevitable. Firstly, accrual accounting offers the benefits of improved accountability and improved resource management (Funnell and Cooper, 1998; Ranby, 1997). This claim has been supported by evidence that suggests the cash system provides inadequate information for the full costing of operations (Management Advisory Board, 1997). Accrual accounting, on the other hand, is said to improve decision making by providing information on the full cost of operations and the resources used to deliver services to the public (Funnell and Cooper, 1998; Webster, 1998). This is increasingly important for those business units which are commercializing to enable them to recover the cost of products and services (Webster, 1998). Finally, accrual accounting gives governments the opportunity to minimize their costs through cost identification (Guthrie, 1999).

Limitations identified from the adoption of accrual accounting include the fact that it can lead to the misallocation of resources and an inadequate disclosure of the size of assets and liabilities. This reduces the organisation’s ability to account for the full cost of programs due to fluctuations in costs. More importantly, perhaps, is the fact that accrual accounting enables organizations to defer liabilities, such as long service leave, to future periods, therefore burdening future taxpayers with these costs. By contrast, the government can also charge the full costs of assets purchased during the year to the current taxpayers instead of allocating these costs over the useful life of that asset (Robson, 1988; Ryan, 1998).

The introduction of accrual accounting has many implications, including the preparation of accrual financial reports, the operation of government entities according to accrual management systems, the preparation of whole-government financial reporting and preparation of accrual based budgets (Guthrie, 1995; Pallot, 1994; Ryan, 1998).

Accrual financial reports
All three public sector standards AAS 27, AAS 29 and AAS 31 require general purpose financial statements to be prepared on an accrual accounting basis. In addition to this, local governments are also required to comply with the Local Government Finance Standard 1994 which specifies the use of accrual accounting to broaden the public accountability requirements (see Section 26). Local Government will benefit from the preparation of conventional accounting statements on an accrual basis through increased transparency and accountability for the use of resources, improved information for the
monitoring of financial performance, and the improved management of resources through the adoption of full cost pricing (see Paice, 1998).

The preparation of accrual financial statements means that organizations are required to include their assets on the face of the balance sheet. This means that entities need to take an inventory of their assets, asset values and use of those assets. This information will be a valuable source in asset acquisition, maintenance and replacement decisions, the measurement of the performance of assets, the provision of internal and external benchmarking information and also pricing decisions (Hope, 1999). Churchill (1992) suggests that the preparation of a balance sheet will enable the organisation to manage its asset base more effectively, increase the organization’s ability to evaluate the mix of debt/equity funding of assets, evaluate working capital management and allocate accountability for specific assets and liabilities. The downfall of including assets on the face of the balance sheet is that governments are struggling to value assets, especially heritage assets, infrastructure assets and community assets. There are many concerns as to whether such assets even meet the asset definition, recognition and measurement criteria set out in the standards (Boreham, 1994, 1995; Burrit et al., 1996; Carnegie and Wolnizer 1997a, 1997b; Coleman, 1996; Falk and Neilson, 1993; Hone, 1997; Micallef and Peirson, 1997; Tamlin, 1996; Walker 1995a, 1995b; Williams, 1996; Young, 1994). New valuation processes, such as the deprival value technique, have been suggested as a means for valuing such assets. The deprival value represents the value of the asset to the user. Assets assessed using the deprival value technique are valued using one of three valuation techniques: current market buying price, depreciated replacement/reproduction cost and current market selling price. The technique used depends on several questions. Firstly, does the asset contribute to meeting the organization’s goals? Secondly, would the asset be replaced if the organisation was deprived of that asset? Finally, in what manner would the asset be replaced (Addicott, 1997)?

Guthrie (1999) claims that the introduction of accrual accounting in the public sector requires a change in the existing information technologies and the culture of the organisation. This means that considerable amounts of money have to be invested into changing the MAS so that it can produce accrual reports, and either training or recruiting individuals to support the new accrual management accounting system.

Whole of government reporting
The Joint Committee of Public Accounts (1995, p. 194) defined whole-of-government reporting as “a form of general purpose financial reporting where the financial statements of the various entities controlled by the government are consolidated to show the financial activities and performance of the government as a whole”.

The purpose of producing whole-of-government financial statements is to provide the community with a much clearer picture of the government operations and their use of resources. Whole-of-government reporting involves
the preparation of the three conventional accounting statements: the balance sheet, the profit and loss statement and the statement of cash flows. The whole-of-government financial statements adopt a format similar to those of the private sector, in that revenues and expenses are a reflection of financial performance, assets and liabilities indicate the financial position and cash flows show how activities are financed (Boxall, 1998).

**Accrual budgeting**
Accrual budgeting refers to the preparation of budgets according to accrual concepts. To date, few governments in Australia have prepared budgets using accrual accounting (Guthrie, 1999). Guthrie (1999, p. 145) suggests that the primary reason for this is the inconsistencies between measuring the full cost of a program in inflated accrual terms when the cash allocated by governments is in smaller absolute dollar amounts. Recommendations have, however, been made by the National Commission of Audit (NCoA) for the Commonwealth Government to adopt full accrual principles including accrual budgeting. The NCoA suggests that commonwealth organizations should prepare operating budgets, a capital budget, a budget of cash flows and a budgeted statement of assets and liabilities. This recommendation was reinforced by the commonwealth budgeting, reporting and accounting scoping study (COBRA) in April 1997 and a timetable was set for its implementation (Funnell and Cooper, 1998). In 1998-1999 a trial accrual budget was to be tested on selected agencies. Over the 1999-2000 period it is expected the full accrual based outcomes and outputs framework will be adopted and 2001-2002 will complete the implementation of accrual budgeting. In Queensland, the Local Government Finance Standard 1994 requires the preparation of budgets on an accrual basis.

**Conclusions and future research**
This paper has elaborated how various external institutions in the form of State and Commonwealth agreements, the government legislation and the introduction of new business principles such as the NCP have changed the organizational culture of the Australian public sector. It has been discussed that the Australian public sector has implemented the textbook accounting systems required by the Australian Public Sector Accounting Standards. Public sector entities now are required to prepare an annual report to satisfy the requirements of the external institutions.

**Future research**
The discussion in this paper supports claims that there is a need for more research in the public sector (Broadbent and Guthrie, 1992; Broadbent, 1999). The administrative and financial reforms imposed on the public sector provide a key opportunity to study several issues. Firstly, future research may focus on the effects of the reform of the public sector at various levels of government: the commonwealth, the state and the local. For example, in a local government setting, has the reform resulted in a greater efficiency and effectiveness in the
use of publicly generated resources or is it merely a window dressing to increase the legitimacy of local government operations?

To date, much of the public sector accounting literature has had a technical focus. That is, it is concerned with accounting techniques employed by public sector entities. The contemporary accounting literature suggests that accounting is implicated in social and organizational practices. It has been claimed that accounting is more than a technical phenomenon, that it is shaped by inter-organizational forces (e.g. institutional, political and economic). Future research may investigate in depth the operation of management control systems at various settings to understand how accounting is implicated within a public sector context. Using a longitudinal field study approach, future studies may also investigate the changes occurring at various public sector entities. More specifically, the following issues can be investigated:

- What changes have occurred within the organization?
- Why have those changes occurred?
- Were the changes explicitly linked to the organization’s strategy?
- Who promoted the change?
- How was the accounting systems developed to support the strategic change?
- What were the roles of the accountants and other staff involved in the change process?
- What problems had to be resolved?
- Was there any resistance to the change? – if so, how did management manage the resistance?

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