

## **Malaysian Governmental Accounting: National Context and User Orientation**

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*Recent years have seen changes in governmental accounting from a cash-based accounting system to an accrual-based accounting system. According to Lüder, development in governmental accounting system is influenced by its environment. Lüder hypothesized that specific contextual variables and primary user orientation of governmental accounting and reporting could determine the design of the governmental accounting systems. These variables could indicate whether or not a particular governmental accounting system is favourable towards change. Assessment of the national context and development of the Malaysian governmental accounting shows support for Lüder's hypothesis.*

**Field of Research: Government accounting, national context, user orientation**

### **1. Introduction**

Developments in governmental activities in recent years have raised concerns over whether the cash basis of accounting is sufficient for governmental accounting and reporting. Accrual accounting, previously thought to be only suitable in the private sector, has been seen to be an alternative for better reporting of government activities. Although there is a continuing debate over the use of cash versus accrual accounting, accrual accounting has been adopted in the governments of several countries including Australia, New Zealand and the United Kingdom.

According to Lüder (1989, 1992), differences in governmental accounting systems can be explained by looking at the environment in which the systems operate. The environment includes factors such as economic condition, political, administrative and culture. In his contingency model, Lüder asserted that governmental accounting innovation can occur given appropriate stimuli and conducive environmental factors (Lüder, 1992; 1994; 2001). It should be noted that the contingency model assumes that the benefits of accrual accounting are significant for the public sector whilst this is still not clear and has not been supported by extensive research. Criticisms on Lüder's contingency model and on the claimed benefits of accrual accounting in the public sector have been put forward by several authors including Nobes (1988), Chan et al. (1996), Monsen and Näsi (1997), Mellett (1997) and Robinson (1998).

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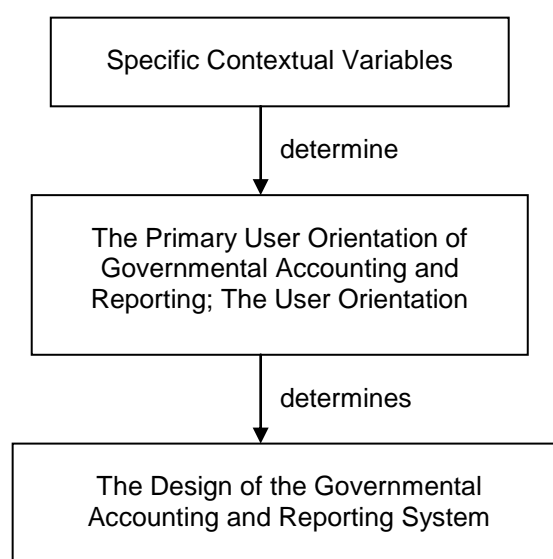
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This paper aims to assess the Malaysian governmental accounting system using Lüder's classification of national context and user orientation. The assessment will identify the national contexts influencing governmental accounting in Malaysia, determine user orientation of governmental accounting and reporting, and evaluate whether or not the Malaysian governmental accounting system is favourable or not to changes. In addition to providing support for the hypothesis in Lüder's classification analysis, the assessment could also identify factors to be considered in further development of the Malaysian governmental accounting.

## 2. Review of Lüder's Classification of National Context and User Orientation

A study by Lüder (1989) can be seen as an attempt to provide classification criteria for governmental accounting. The study identified two classification criteria: internal criteria, which characterised governmental accounting and reporting systems; and external criteria which characterised the national context and user orientation of governmental accounting. The study was based on a hypothesis that "specific contextual variables determine the primary user orientation of governmental accounting and reporting; the user orientation determines the design of the governmental accounting and reporting system" (Lüder, 1989, p. 5).

Lüder conducted a study of six industrialised Western countries (Canada, Denmark, France, Sweden, United Kingdom and the United States), in an attempt to classify accounting and financial reporting practices; identify the distinct patterns; and explain the reasons for the differences between patterns. Lüder classified the government accounting systems of the countries under his study based on the relationship between the "primary user orientation of governmental accounting and financial reporting" and "perceived underlying contextual variables". The hypothesis of Lüder's study is shown in Figure 1.



Source: Lüder (1989, p. 5)

Figure 1 Basic Hypothesis of Lüder's Classification Analysis

The study asserts, “there exists a relationship between those two variables (national context and user orientation) in the sense that a specific national context is favourable (or not favourable) to a specific user orientation of governmental accounting” (Lüder, 1989, p. 6). However, Lüder emphasised that the existence of a specific national context will not necessarily cause a country to have a specific user orientation to which it is most favourable. Hence, the relationships that might exist between national context and user orientation are more complex and do not lend themselves to the framing of simplistic causal relationship.

## 2.1 Contextual Variables of National Context

The perceived underlying contextual variables describe the national context, which is characterised by three contextual variables: (1) distribution of political power, (2) legal tradition and (3) professional influence.

***Distribution of political power*** is measured by the relative strength of the citizenry, the legislature and the executive in controlling governmental financial resources. Thus, a country may have political entities with a relatively strong citizenry, or with a relatively strong legislature or with a relatively strong executive (Lüder, 1989, p.7).

***Legal tradition*** is based on either common law or civil law. The characteristics of the legal tradition that could influence governmental accounting are as shown in Table 1:

Table 1: Characteristics of Legal Tradition

Legal Tradition	Characteristics		
	Statute of law	Degree of codification for governmental accounting	Flexibility and intra-national uniformity of governmental accounting
Common law	Limited and general	Only general provisions of governmental accounting	Less unified and more flexible than the civil law
Civil law	Comprehensive and detailed	Principles and procedures of governmental accounting stipulated in detail by codified law	Governmental accounting systems are unified but less flexible

Lüder (1989, p. 8) suggested that innovations in governmental accounting and reporting are more likely to occur in common law countries due to the following:

- The lower uniformity of governmental accounting in common law countries produces a pressure for change to achieve a higher degree of uniformity.
- Common law has a higher built-in-flexibility, thus the legal system will not be an obstacle for changes.

**Professional influence** is reflected by a direct or indirect influence of the private sector accounting profession on governmental accounting. Professional influence was described in terms of educational background, roles of professional bodies as advisors on governmental accounting and involvement of private sector audit firms in governmental auditing. The influence was described by Lüder (1989, p. 9) as follows:

<b>Educational background of government accountants</b>	In countries where government accounting personnel has little knowledge of private sector accounting, governmental accounting tends to develop relatively independent of private-sector accounting.
<b>Advisory bodies</b>	Existence of professional bodies with advisory responsibilities on governmental accounting ensures inclusion of private-sector accounting experts.
<b>Auditing work</b>	When more auditing work is done by private sector auditing firms, governmental accounting is more likely to apply private sector accounting standards.

## 2.2 User Orientation

The primary users of governmental accounting and financial reporting are the legislature, public and management. User orientations affect the purpose of accounting and reporting for the government. The relationships between user orientation and the purpose of accounting and reporting are as follows:

<b>Legislature orientation</b>	Government accounting system responds exclusively or at least primarily to the control and information needs of the legislature. The focus of accounting and reporting is to demonstrate compliance with spending authorities.
<b>Public orientation</b>	In addition to the legislature orientation, public orientation is seen as a second and important purpose. Accounting is also a mean to provide the public with a reliable picture of the overall financial situation of government.
<b>Management orientation</b>	In addition to the legislature orientation, management orientation is seen as a second and important purpose. Accounting is also considered as a mean to manage government operations. The focus of accounting and reporting is on encouraging and demonstrating effective and efficient resource management.

## 2.3 The Classification Scheme

Based on the relationship between the contextual variables, Lüder came up with a classification scheme consisting of sixteen different classes of national contexts,

which differently favour the respective user orientations of governmental accounting. The scheme is shown in Table 2 below:

Table 2: Classification Scheme of National Contexts

Degree of Legal Codification	Professional Influence	Distribution of Political Power			
		Strong Citizenry 1	Strong Legislature 2	Strong Executive 3	None of these 4
High (Civil law)	Strong 1				
	Weak 2				
Low (Common law)	Strong 3				
	Weak 4			Malaysia	

Some hypotheses concerning the relationship between the type of national context and the user orientation are as follows:

Line 3      Types of national contexts are supposed to be most favourable to major changes of governmental accounting

Line 2      Types of national contexts are supposed to be least favourable to major changes of governmental accounting

Column 1    Types of national contexts are supposed to be most favourable to a public-oriented governmental accounting systems

Column 3    Types of national contexts are supposed to be most favourable to a management-oriented governmental accounting systems

*Source:* Lüder (1989, p. 11)

The results of the classification, however, must be interpreted with caution for the following reasons: First, the assignment of a specific country to a specific contextual variable depends on personal judgement and can be questioned by others. Second, the categories of national contexts are broad, making it possible to assign two countries to the same national context even though they are in fact different (Lüder, 1989, p. 13).

Lüder further acknowledged that the existence of a favourable national context does not imply “the government accounting system adapts quasi automatically to the user orientation” (1989, p. 12). An ‘incentive’ or ‘stimulus’ is required to initiate a major change in governmental accounting practices, which include financial crisis, technological innovations, and personal commitment of an authoritative government official. Thus, Lüder concluded that although the existence of a national context may be a sufficient condition, it certainly is not a necessary condition, for adapting the accounting system favourable to a particular user orientation. Accordingly, given a strong stimulus and ability to overcome implementation barriers, “it is also possible to enforce a government accounting system if the national context is unfavourable to it” (Lüder, 1989, p. 12).

### **3. Methodology**

Archival research was used to trace and document the development of governmental accounting. The archival research involves going through documents such as government publications, Acts and regulations, annual reports, government circulars, seminar and training manuals from government departments in Malaysia and other forms of record relevant to the issues of study. Most of these documents were obtained from the Accountant General's Department in Malaysia. Analysis of the archival research data focused on the qualitative aspect. The analysis provides the context for understanding the development of governmental accounting, i.e., insight into the stages and key influences or forces that have impact upon accounting.

### **4. Discussion**

According to Lüder's hypotheses on the relationship between the type of national context and the user orientation, Malaysia is expected to have a contextual situation most favourable to management oriented governmental accounting system. The classification of Malaysia is similar to the federal government of the USA and the UK.

#### **4.1 Contextual Variables and National Context in Malaysia**

##### **4.1.1 Distribution of Political Power**

Malaysia has a strong executive. The executive in Malaysia has a strong control over the financial resources. The cabinet or executive always represents the parliamentary majority and is in control.

##### **4.1.2 Legal Tradition**

The legal system in Malaysia is based on common law, being inherited from the British. Procedures and practices of accounting and reporting are governed by a set of rules. Among the regulations governing the accounting procedures for the government are Federal Constitutions (Revised 1972), Financial Procedures Act, 1957 (Revised 1972) and Audit Act 1957 (Revised 1972). These Acts provide limited and general provisions on financial, budgeting, accounting and auditing aspects of the government.

The Federal Constitution, for example, sets out the rules regarding financial provisions. Specific requirements concerning the control and management of public finance as well as the financial and accounting procedures are provided by the Financial Procedure Act 1957. Further guidelines and requirements concerning accounting procedures are issued by the Treasury through instructions and circulars. Thus, it can be seen that legal tradition in Malaysia has a higher built-in-flexibility as in other common law and does not pose as obstacle for change.

##### **4.1.3 Professional Influence**

The Malaysian accounting profession's influence on governmental accounting is weak and almost non-existent. There has been no significant contribution or significant interest expressed by either the Malaysian Institute of Accountants (MIA)

or the Malaysian Association of Certified Public Accountants (MACPA) (Coombs and Tayib, 1997). The Malaysian Accounting Standards Board (MASB), has not shown any attempt to be involved in the standard setting for the government. In addition, the Malaysian Institute of Public Sector Accounting (IPSAM) whose members are public sector accountants, with the potential to “provide a lead to the federal government in the development of public sector accounting and reporting standards ... is not particularly active and its establishment has not been widely trumpeted” (Coombs and Tayib, 1997, p. 14). In addition, audit works for the federal and state governments are the sole responsibility of the National Audit Department.

#### 4.2 User Orientation

Based on the above discussions, Malaysia can be placed on line 4, column 3 of Lüder’s classification scheme (refer to Table 2). Governmental accounting system in Malaysia is expected to emphasise management accounting and the effective and efficient use of resources. This assessment is consistent with the development of governmental accounting practices in Malaysia, in which the government has been emphasising management oriented accounting and budgeting systems. Nevertheless, it should be noted that in Malaysian government, the budgeting system has seen major reforms compared to the financial accounting system.

The traditional line-item budgeting system was replaced by the programme, performance budgeting system (PPBS) in 1969. Subsequently, in the 1980s, as a result of problems associated with PPBS, particularly on the implementation of the performance measurement and programme evaluation, a Modified Budgeting System (MBS) was devised. MBS was premised on the PPBS, with the main objective to increase the efficiency in the financial management of government, specifically, to increase accountability among controlling officers and programme and activities’ managers. Principles and objectives of MBS are (Xavier, 1998, p. 101):

- To improve and modernise the process of resource allocation on the basis of performance.
- Line management empowerment through the devolution of authority over the management of resources to as low a level of management as practicable.
- To introduce a results-oriented and cost effective management.

In 1992, the government introduced the Micro Accounting System (MAS), which is similar to Activity Based Costing, to enhance the efficiency in financial management. The *Manual for Micro Accounting System* was introduced through the issuance of Development Administrative Circular No. 3 of 1992. The system was done manually in the early stage but was computerised in 1995. MAS was designed to achieve the following objectives:

- Facilitate the collection, processing and preparation of the cost information.
- Prepare information on cost efficiently and in a more flexible manner.
- Produce reliable cost information.
- Contribute to the optimisation of the use of resources.

The Manual of MAS indicates that “[MAS] is another step towards strengthening management accounting at the department level. Its implementation would further improve the strategic planning process and engender the optimal utilisation of resources. In general, the implementation of [MAS] would further enhance

accountability in the Public Service". Effective financial management is stressed in both the *Malaysia Seventh Plan* and the *Malaysia Eighth Plan*. In the *Seventh Plan*, it was stated that "effective financial management will be given further emphasis to ensure greater accountability in the management of public funds and improve financial discipline at every level of Governments" (Economic Planning Unit, 1991).

It can be seen from the above that the Malaysian government has been very proactive in bringing about improvements in governmental budgeting and financial management and although the reforms of recent years do not specifically include resource budgeting they do provide evidence that the Malaysian Government would be very interested in supporting resource budgeting and accounting if this was seen as a means of enhancing the effectiveness of MAS and overall financial management. Furthermore, the situation in Malaysia is consistent with 'managerialism-driven' innovation process described by Lüder (1994, p. 10) as follows:

The managerialism-driven approach is mainly stimulated by fiscal stress and in the first place aimed at contributing to more efficient and effective public sector management. This approach therefore is primarily concerned with reforming governmental internal (managerial) accounting, but improvements in financial accounting and reporting sometimes is [*sic*] a by-product of the innovation process.

## 5. Summary and Conclusion

In order to assess future development of governmental accounting and reporting, Lüder's classification scheme is used. The scheme looks at the relationship between the contextual variables and user orientations of governmental accounting and reporting to determine the possibility of innovation in governmental accounting. Based on the analysis, it is found that the national context for the Malaysian governmental accounting and reporting favours a management oriented governmental accounting system. This is categorised by a low degree of legal codification, strong executive and weak professional influence.

Although Malaysia does not have the contextual variables to be most favourable to major changes in the governmental accounting system, Lüder's framework suggested that the accounting system could change given enough stimulus and influence from the accounting professions. The influence of accounting professions in the development of governmental accounting towards accrual-based has been seen in countries such as the USA and UK. These countries were classified in the same category as Malaysia, both have already adopted accrual accounting for their government accounting and reporting. Hence, there is a possibility for Malaysian governmental accounting to further develop towards accrual accounting.

In order for Malaysia to be most favourable to major changes in governmental accounting, Lüder's classification scheme suggests that there is a need for a strong influence from the professional bodies, preferably with advisory responsibilities and accountants with knowledge of private sector accounting. But, further research is needed to assess the acceptance of major changes in the accounting system among the government accountants and whether or not the benefits outweigh the costs of changing the current accounting system.



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