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On Managerial Accounting Practices in South African Public Departments

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ABSTRACT The availability and adequacy of accurate cost information is required for sound financial decisions in any organisation, but the level of its usage differ from one organisation to another either private or public according to the relevance attached to it. In particular, this study examines the determinants of implementing cost and management accounting systems in two South African public departments based on two determinants: (a) to satisfy regulations, and (b) to provide legitimacy. Furthermore, this study presents the outcome of studies conducted in a water agency and a hospital in South Africa. Participants were selected based on their relevance to managerial accounting practices in these organisations. Evidence suggests that those departments that claims to have a management accounting system in place did so only to satisfy regulations and to legitimatise their activities before external stakeholders such as the auditor-general's office as having control on their operations.

INTRODUCTION

The pressure on governments to deal with shrinking budgets and dwindling financial resources have raised concerns for public department managers to efficiently and effectively utilize available financial resources, increase transparency, expand constituent services, and improve performance. The increasing level of competition for the few available resources among government agencies has intensified this challenge for public department managers to have detailed understanding of the required financial resources needed and consumed in relation to the goals, mission, and outputs of the department (OECD 1995; Jung 2013). This understanding is required for public department managers to make decisions that enable effective utilization of limited financial resources to improve performance and transparency. Due to the limitation in government financial resources, performance measurement issues are receiving increasing attention as these organisations attempt to implement new measurement techniques that better support their objectives (Cavalluzzo and Ittner 2004). While many performance measurement initiatives stem from the private sector, recent efforts by governments worldwide to improve public departments' performance have placed emphasis on increasing accountability and improving decision-making (Ittner and Larcker 1998). Essentially, governments are compelled to cut costs by taken steps to reduce costs and improve services through regulations like the Public Finance Management Act (PFMA) (No.1 of 1999 as amended by Act 29 of 1999) in South Africa for instance (National Treasury South Africa 1999).

In response to this challenge, a range of management accounting techniques has emerged (Chenhall and Langfield-Smith 1998). Accounting literature identifies some critical attributes of a costing system design to include the level of detail provided, the ability to separate costs according to behaviour, the frequency with which cost information is reported, and the extent to which variances are calculated (Pizzini 2006). Pavlatos and Paggios (2009) warn that if management accounting practices is to remain relevant, it needs to adapt to meet the changing needs of managers. Particularly, there have been increasing emphasis on delegated budgets and accountability, cost accounting and cost management initiatives, and value-for-money audits as a means to increase the efficiency and effectiveness of public department operations (Broadbent and Guthrie 1992; Humphrey et al. 1993). In contrast, descriptive studies find that public departments' management accounting systems are implemented to satisfy government mandates and regulations like the PFMA and are rarely used for internal decision-making purposes (Uddin and Tsamenyi 2005). Instead many of these public departments' cost and management accounting systems are merely implemented to satisfy regulations and provide legitimacy for their activities to be seen by external stakeholders as having control on their operations (Geiger and Ittner 1996).

While research on management accounting practices have largely focused on accounting systems of large manufacturing organisations in developed countries (Waweru et al. 2004; Pavlatos and Paggios 2009); a number of government cost accounting issues have not yet been dealt with comprehensively in existing literature. Drawing on both institutional and contingency theories of management accounting practices, this study examines the determinants of implementing cost and management accounting systems in the South African public departments based on two determinants: (a) to satisfy regulations, and (b) to provide legitimacy. In addition, this study reports on two case studies about what influences of managerial accounting practices in government departments in South Africa.

Institutional and Contingency Theories of Management Accounting

Proponents of normative institutional theory argue that it extends beyond the focus of contingency theory on an organisation's task environment (Covaleski et al. 1996). Other proponents indicate that because individuals are led to make conceptual changes to public sector accounting systems and financial reports, the system of institutions provides the framework with which accounting systems are shaped (Luder 1992). While supporters of contingency theory contend that a one-size-fits-all approach is undesirable; they suggest that the approach will be more effective if it takes into consideration the potential diversity of governance mechanisms which deal with important contingencies (Aguilera et al. 2008). Conversely, public departments should consider that management accounting is not only a homogeneous set of calculative practices that is highly contingent and situational specific, but as a dynamic and organisational embedded social phenomenon utilising instruments that are not stable and fixed but oftentimes complex, temporary and fragile (Vaivio 2008). Due to conflicting interests among public departments' officials to fully implement management accounting systems in South Africa which may lead to inefficiency and sub-optimality in the use of the few available financial resources, this study considers both the institutional and contingency argument to support the need for public departments to embrace the use of managerial accounting information for improved public service delivery.

The Changing Information Needs of Government Managers

There have been increasing emphasis on delegated budgets and accountability, cost accounting and cost management initiatives, and value-for-money audits as a means to increase the efficiency and effectiveness of public department operations (Broadbent and Guthrie 1992; Humphrey et al. 1993). In contrast, these initiatives have yet to yield desired improvements envisaged for an efficient and cost-effective public service. Moreover, there are few skilled accountants within public departments to make the adoption and implementation of private sector-styled managerial accounting techniques thrive to yield improved cost decisions in government service delivery (Hyndman and Connolly 2011). Moreover, Kober et al. (2010) argue that the increasing public sector managerial autonomy in decision-making necessitated the generation of financial information other than cash by public accountants to assist public sector managers improve their financial decisions.

Incidentally, critical attributes of a costing system design includes the level of detail provided, the ability to separate costs according to behaviour, the frequency with which cost information is reported, and the extent to which variances are calculated (Pizzini 2006). Nevertheless, Verbeeten (2011) found that while cost management information is used by some public departments' financial managers; it is hardly used by political managers thereby debunking the claims that cost management information has become important in managing public sector orgnizations. This assertion remains true, inasmuch as protagonists in politics, government and public administration assume the possibility of political managers to pursue one's self-interest presupposes a discretionary margin in public decision-making (Luder 1992). With regards to this, Cavalluzzo and Ittner (2004) argue that the extent of performance measurement and accountability in public service are positively associated with greater use of performance related information provided by its managerial accounting systems for various purposes. Similarly, Pizzini (2006) found that managers' evaluations of the relevance and usefulness of cost data are positively correlated with the extent to which its managerial accounting systems can provide greater cost detail, better classify costs according to behaviour, and report cost information more frequently. Conversely, Mucciarone and Neilson (2011) observe that one institutional factor that can influence the development and use of management accounting principles in a public service department is the extent that its bureaucrats have the requisite knowledge and experience to support its implementation.

The Influence of Costing Information in Government Business

Government managerial accounting systems are implemented to satisfy government mandates and are rarely used for internal decision-making purposes (Uddin and Tsamenyi 2005). Instead many of these public departments' cost and management accounting systems are merely implemented to satisfy regulations and provide legitimacy for their activities to be seen by external stakeholders as having control on their operations (Geiger and Ittner 1996).

Implementing Managerial Accounting to Satisfy Regulations

While private sector accounting served as a benchmark for evaluating public sector accounting; many of these public departments' cost and management accounting systems are merely implemented to satisfy regulations so that they can be seen by external stakeholders as having control on their operations and activities (Geiger and Ittner 1996). In order words, public sector management accounting most often refers to budgeting and control in relation to expression of public policy and political preferences, or more of an instrument of fiscal policy on revenue and spending to achieve macroeconomic objectives (Chan 2003). In other words, Jackson and Lapsley (2003) confirm that public service departments' main reason for adopting new managerial practice is to comply with regulations and statues. They argue that instead many public service finance or accounting departments reports that they are adopting new managerial accounting procedures to cope with the pressure from government to reduce costs and utilise resources more efficiently because they are faced with increasing pressures and demands for information to justify future financial resource allocation to their departments.

Implementing Managerial Accounting to Provide Legitimacy

Many of these public departments' cost and management accounting systems are merely implemented to provide legitimacy for their activities to be seen by external stakeholders as having control on their operations (Geiger and Ittner 1996). With regards to this, Verbeeten (2011) indicates in a study in The Netherlands that while the design and use of cost management accounting systems differs across public departments; information from cost management systems is used to legitimise the organization's activities to external stakeholders rather than to manage public sector finances. Similarly, Geiger and Ittner (1996) maintain that other public departments are compelled to implement a management accounting system in order to meet the legal requirements for revolving funds from the government. Eventually, when managerial accounting change takes place because of forced regulation or legislation, it is not difficult to precisely determine that such public departments are under presssure to improve their efficiency, their budgetary process and flow of information to the public and other interested parties (Jackson and Lapsley 2003). Consequently, public service departments need to increase their ability to supply detail costs of their services with greater measurement and accounatbility through effective cost accounting system design to enable them manage their services successfully (Cavalluzzo and Ittner 2004; Pizzini 2006).

METHOD

The study method consists primarily of in-depth interviews with accounting officers of two public service departments in South Africa. Otherwise, where appropriate, relevant senior members of the accounting staffs were interviewed using open-ended questionnaire. Deciding on the appropriate choice of public departments proved a bit difficult because of the lack of willingness to participate in research by most public department officials in South Africa and non-response to survey questionnaires made the choice of exploratory qualitative study approach the best available option. At any rate, a qualitative approach is preferred in this circumstance since the study is particularly focused on examining the determinants of implementing cost and management accounting systems in the two South African public departments, and to suggest potential social, economic and environmental benefits of adopting management accounting practice in public departments. A multiple case study approach was adopted based on a constructive paradigm that allows for a close collaboration between the researcher and the participant, while enabling participants to tell their stories from different angle (Crabtree and Miller 1999). The approach was to gain a better understanding of managers' actions; because they are able to describe current reality as they tell their stories (Lather 1992). The multiple case approaches were to report the outcome of studies conducted at Lepelle Northern Water (LNW) and Mokopane District Hospital in South Africa. Participants were selected based on the relevance of their duties to managerial accounting practices. The in-depth-interview method was used to collect data through a series of open-ended questions from accountants and managers in the two organisations (Qu and Dumay 2011). While this study may have suffered some inherent limitations such as subjectivity and generalisation due to the case study approach (Yin 2010); the findings obtained from these case studies can be adopted in other situations since each case may likely involve a number of commonalities. Although, generalizability is a controversial issue in case study research (Yin 2010); attempts were made to overcome this limitation by asking open-ended questions which is unlikely to overcome the limitation completely.

The Lepelle Northern Water

The Lepelle Northern Water (LNW) was established and regulated under Water Services Act No.108 of 1997 and Public Finance Management Act of No1 of 1999 of South Africa. Its primary mandated is to provide bulk water to Water Services Authorities (municipalities) and industries. The organization has the ability to raise capital in the open financial market to fund expansion projects. However, the department has to contend with issues of non-remittance of water revenue by municipalities for bulk water services rendered to them. Other contending issues are replacement, rehabilitation and refurbishment of water services infrastructures due to the effects and consequences of aging and climate change. The LNW consists of 306 employees with 26 in the finance department who are responsible for Financial and Management Accounting and Supply Chain Management. The Management Board of LNW is the accounting authority tasked with the responsibility to ensure LNW resources are managed in an effective, efficient and sustainable manner. The Chief Executive participates in the development and oversees the implementation of strategic plan for the organization and reports directly to the Board.

The Mokopane Hospital

At the Mokopane District Hospital, two senior accounting officers were interviewed. The Mokopane Hospital is a regional hospital in the Waterberg District of Limpopo which offers both primary and secondary services and a little bit of tertiary services. All of the district clinics in the Waterberg District most often refer their patients to the Mokopane District Hospital for secondary and tertiary services. The Mokopane Hospital has three categories of patients: the non- paying patients, the paying patients, and the private patients. An established management accounting information systems is likely to assist managers improve their financial decision making.

RESULTS AND DISCUSSION

While the objective of the study is to examine the determinants of implementing cost and management accounting systems in two South African public departments; there were challenges in persuading the accounting managers to participate in the research. However, the researcher convinced them that their responses and identities will be treated with discreet. Moreover, they were assured that the findings will be useful to improve their decision making especially in relation to financial resources management as well as contribute to improving their departments' service delivery. Results from these interviews were analysed using deductive reasoning. However, the lack of a separate cost accounting system within these two government departments is evident. Essentially, the shortage of skilled management accountants can be attributed for the lack of oriented use of performance measures for distortions in costing-related information within the public sector. Furthermore, current costs of producing a kilolitre of water had almost equalled water tariffs and the realisation that the water agency may longer be self-sufficient. Consequently, managers were oblivious of the usefulness of cost accounting information in decision-making while there is no reference to the use of cost accounting information during budget preparation.

The Lepelle Northern Water (LNW)

Findings indicate that LNW do not have a separate management accounting system in place contrary to the suggestion of Pavlatos and Paggios (2009). The existing financial management system is a finance department with no clearly defined cost and management accounting function to assist management to integrate the processes of financial management and accounting for accurate determination of product costs for an effective internal control system. According to one of the senior accounting officials interviewed:

'We do not have a separate cost accounting section; the cost per litre of water is agreed and fixed at the beginning of each financial year with the municipalities.'

Although, financial reports are produced timeously, this does not influence the costing decisions of the department. This is a consequence of the non-availability of a management accounting system. Moreover, finance staffs have been trained to adhere to a system where only monthly and variance reports are prepared for comparison with budget (Jackson and Lapsley 2003). On the contrary, there is no existing management accounting system to assist managers to adequately calculate unit product cost or monitor their budget (which is based on the incremental budgeting system) whether they are adhering to established standard. While officials have responsibilities to determine budget in terms of cost centres and communicate to end users; there are no measures to ensure compliance to established management accounting system to assist decision makers on input-output costs for pricing strategies (Verbeeten 2011). Furthermore, current costs of producing a kilolitre of water had almost equalled water tariffs and there is a realisation that the water agency may longer be self-sufficient because of its product costing system. Some of the accounting managers interviewed does not fully understand the usefulness of cost accounting information in day-to-day financial decision-making. There is absolutely no reference to cost accounting information during budget preparation because of the lack of qualified cost accountants in this public department (Hyndman and Connolly 2011). Consequently, there is no relevance of a management accounting system to assist the organization to monitor variances between planned and actual cost (Jackson and Lapsley 2003).

The Mokopane District Hospital

Within the Mokopane District Hospital, management accounting principles is not particularly used and not relevant in their day-to-day financial decision-making due to lack of competent officials with sound managerial accounting skill (Mucciarone and Neilson 2011). Although, the hospital has an established accounting information system in place but there is no separate management accounting system because officials follow the financial reporting rules set by the Provincial government and which are influenced by political interference (Vaivio 2008; Jackson and Lapsley 2003). While some of the services rendered at regional hospitals are paid for; the lack of an established management accounting system and improperly patient records makes it difficult to collect outstanding patient bills. For instance, files that were opened for pregnant women during ante-natal period are not updated even after delivery, a situation that results in such services not been paid for. The lack of updated patients record is more prevalent in most of the districts' rural clinics where collection of payment for services are inefficient with no internal cost control mechanism to monitor the collection process because of the unavailability of cost accounting related information to make necessary decision for improvements. The lack of an effective management accounting systems make patients visit the hospital with no intention to pay because they are fully aware that they would not be turned back if they do not pay, this relates to the findings of

Pizzini (2006). This problem is compounded due to the lack of a good verification mechanism to determine the employment status of patients. This loophole encouraged patients go to the police station to give false affidavits which claims that they are unemployed to avoid payment. Although, the hospital keeps changing the outpatient department's (OPD) data capturing software; the information process at these OPD departments left little to be desired on revenue collection of outstanding patient fess. Another major deficiency is that the hospital internet and intranet facilities are disconnected most of the time with the loss of patients' record often attributed to sabotage. Also, the cost of service to paying patients at the hospital has not been properly accounted for or documented. Consequently, the unavailability of a separate management accounting information system has placed limitations on the management's ability to make improved decisions. The lack of articulated cost information through effective management accounting systems has also left employees with low morale and demotivated since financial information are prepared only to satisfy legislation and prove their legitimacy (Uddin and Tsamenyi 2005).

CONCLUSION

A critical analysis of the two case departments reveals that the implementation of managerial accounting practices is influenced by the choice to satisfy regulations and provide legitimacy but not necessarily to provide the desired level of cost detail required to analyse reported cost information for improved decision making. However, the inability by public departments in South Africa to attract skilled manpower with the necessary analytical competences in managerial accounting have contributed to a large extent to the non-application of management accounting practices in public service delivery. A significant implication of these findings is that public projects have been evaluated and implemented using inappropriate cost analysis which often leads to over-spending of public funds. In consequence, mass protests and civil disobedience have continued to trail public departments inability to provide improved service delivery. In conclusion, for public departments to improve its service delivery, adequate cost detail and analysis of projects through well established management accounting practices similarly to that in the private sector is encouraged.

RECOMMENDATIONS

This study suggests that public service departments, especially those that are required to be self-financing by fully recovering their service costs through collection of revenues such as the Lepelle Northern Water, should not only endeavour to implement elaborate managerial accounting systems that is better than public departments like the Mokopane District Hospital that is funded by appropriate budgets and reimbursement of expenses by the national government, but should make an extensive use of managerial accounting system for diverse internal control purposes to include pricing and management control. Indeed policy makers and public department officials should endeavour to establish and implement private-sector styled management accounting systems in projects planning, cost control, financial decision making, and project evaluation and monitoring for better service delivery. The study recommends the establishment of a functional cost accounting system to assist managers in cost control and decision-making process. The study recommends the implementation of management accounting practices in selected public departments through pilot studies to demonstrate its potential to influence and improve public spending and financial performance.

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