

ECONOMIC MANAGEMENT AND ITS EVALUATION IN THE PUBLIC SECTOR

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Abstract

Management in the terms of the public sector is characterized by shifting from rather administrative methods to business-like ones in last decades. This process is usually connected with terms like new public management, new public sector performance management or value-for money management. Effective management then requires among others an existence of adequate economic data and permanent utilization of suitable evaluation techniques and tools. This paper analyses methodologies used for preparing budget and financial statements by selected developed countries. In fact, there are two main methodologies, i.e. the cash basis and the accrual one or their modifications. Further the paper observes whether the public sector data are used in the process of performance evaluation in selected developed countries. The last part of the paper then briefly summarises the current state of methodologies used for preparing budget and accounting data in the Czech public sector and it presents a brief output of a survey undertaken among managers of the Ministry of Defence of the Czech Republic concerning utilization of financial statements in the process of economic management.

Key words: public sector, management, accrual basis, performance, evaluation

JEL Code: H 11, H 72, H 83

Introduction

Management in the public sector can be understood diversely. Flynn (2007) for example points out a difference between the terms administration and management in the context of the public sector. He describes administration as involving the orderly arrangement of resources to follow previously defined procedures and rules. On the other hand management should involve discretion in managing of sources to achieve a set of objectives. Flynn suggests that both activities may be useful within the public sector management process, and also many public sector managers are engaged in both. Management requires thinking and acting adequately to find the best ways of achieving objectives and goals. Managers dispose

of formal authority and carry out a set of activities including planning, budgeting, projecting, marketing, personnel management, performance measurement, and others.

Traditionally administration and fiscal control of the public sector activities predominated over a managerial view of them. The situation has started to change systematically in last two decades of the 20th century as to developed countries. Majority of them started to search for effective tools that would enable to improve transparency of the public sector data, control expanding indebtedness of the public sector, and generally, improve performance of the public sector activities (Vodáková, 2012a). Among others this effort was supported by some international or supranational organizations, such as Organisation for Economic Co-operation and Development (OECD), International Federation of Accountants (IFAC), European Union (EU), and others.

The aim of this article is to analyse the state of methodologies used for preparing budgeting and accounting data in the public sector of selected countries and to find out whether these data are used in the process of evaluation of the public sector activities, especially on the state administration level. The second part of the paper is devoted to synthesis of current findings concerning the Czech public sector. As a basic scientific methods description, analysis, comparison, and synthesis were used in the paper.

1 Public sector management

Contemporary changes in management of the public sector are characterized by shifting from traditional rather administrative methods to business-like ones which are usually connected with terms like new public management, new public sector performance management, or value for money management (Box, 1999). The core of these changes consists in an effort to improve information capability of the public sector data and use them effectively in the process of performance evaluation because permanent evaluation is considered as an indispensable factor of successful management process nevertheless it is carried out in business or in the terms of the public sector.

1.1 Qualitative changes of the public sector data

Because of poor information capability of the public sector data in relation to economic management vast changes in both accounting and budgeting methodologies were needed. The core of changes lied in transformation from traditional cash basis to accrual one. While under the cash basis transactions and events are recorded only if they are simultaneously connected

with cash inflows and outflows, under the accrual basis they are recorded in accounting at the moment they occur, and not necessarily at the moment they are connected with cash flows (IFAC, 2012). This enables besides others evidence of such important inputs for economic evaluation process like expenses and revenue that either were not recorded at all or their evidence was not complete and accrued in the public sector in past.

Based on various international studies it can be concluded that around the turn of the 20th and 21st century majority of developed countries had been in the process of implementation of the accrual basis into the public sector accounting or they at least announced an intention to implement it in the near future. Though there are some limitations and doubts as to problematic implementation (Lapsley, Mussari, Paulsson, 2009), different degrees of implementation and legal compliance (Pina, Torres, Yetano, 2009) or problematic evaluation of certain public sector assets (Carnegie, West, 2003) it seems that generally information capability and transparency of accounting data increases thanks to the accrual basis implementation and revealing these statements to the public.

However in budgeting a situation seems rather different. Noticeably less number of developed countries intends to implement accrual basis into budgeting though it may serve to better management and performance (Salinas, 2002). Reasons may be different, but as the most frequent are introduced a dislike for budget legislation changes, their complicated throughput, and a fear of fiscal indiscipline failure or political reasons. In table 1 a brief review of used reporting bases by selected developed countries according to the state in 2007 and 2008 is introduced.

As it implies from the table accrual basis in both budgeting and accounting was according to database of OECD used for preparing budget and financial statements by 7 countries in 2007, i.e. Australia, Canada, Iceland, Italy, New Zealand, Switzerland, and the United Kingdom. In the case of Denmark only 8 % of entities have prepared budget and financial statements under accrual basis and the rest used cash basis. In the case of Finland, 40 % of entities have prepared budget statements under accrual basis while 100 % of entities have still prepared financial statements under cash basis in 2007.

The United States and France used accrual basis for preparing financial statements and cash basis for preparing budget statements in 2007 while all other selected countries (including the Czech Republic) used cash basis for preparing budget and accounting statements. Majority of countries (14, i.e. 63.6 % for budget and 13, i.e. 59.1 % for accounting) further stated that related legislation and technical standards for budgeting and accounting are issued by the Ministry of Finance or the Central Budget authority. Only one

country (4.5 %) claimed that technical standards are issued by an independent standard board and 1 country (4.5 %) in the case of budget and 2 countries (9.1 %) in the case of accounting stated that technical standards are determined by a private sector standard body. The rest of countries used other alternatives for standards setting.

Tab. 1: Reporting basis used for presentation of financial and budget statements

Country	Budget statements		Financial statements	
	Cash based	Accrual based	Cash based	Accrual based
Australia		x		x
Austria	x		x	
Belgium	x		x	
Canada		x		x
Czech Republic	x		x	
Denmark ¹	x		x	
Finland ²	x		x	
France	x			x
Germany	x		x	
Iceland		x		x
Ireland	x		x	
Italy		x		x
Netherlands	x		x	
New Zealand		x		x
Norway	x		x	
Portugal	x		x	
Slovak Republic	x		x	
Spain	x		x	
Sweden	x			x
Switzerland		x		x
United Kingdom		x		x
United States	x			x

Source: OECD, online <http://webnet.oecd.org/budgeting/Budgeting.aspx>

1.2 Performance evaluation systems

Despite the fact that the public sector entities are not primarily profit oriented and thus they generate negligible income while rendering services to the public there still exist evaluation techniques, financial and non-financial performance information that could serve as effective tools of economic management. Some of them such as financial analysis, controlling or benchmarking were used only by businesses formerly but at present their utilization seems to

¹ Budget: 92 % of entities prepare budget statements under cash and 8 % under accrual basis. Accounting: 92 % of entities prepare financial statements under cash and 8 % under accrual basis.

² Budget: 60 % of entities prepare budget statements under cash and 40 % under accrual basis. Accounting: 100 % of entities prepare financial statements under cash basis.

be beneficial at all levels of the public sector too though of course some modification of measures would be needed.

Usage of managerial evaluation tools and techniques generating information about the governmental performance was traced by OECD. In table 2 a brief review of types of performance information produced to assess governmental performance is introduced. As it implies from the table only Belgium and the Czech Republic have declared they produced no performance information for assessing the governmental non-financial performance in 2007³. All other selected countries used for performance evaluation either performance targets, performance measures, evaluation reports (i.e. programme, sectoral, efficiency, or cost effectiveness reviews), benchmarking or others managerial tools.

Tab. 2: Types of produced performance information

Country	None	Performance targets	Performance measures	Evaluation reports	Benchmarking	Others
Australia		x	x	x	x	
Austria		x	x	x		
Belgium	x					
Canada		x	x	x	x	
Czech Republic	x					
Denmark		x	x	x	x	
Finland		x	x	x	x	x
France		x	x	x		
Germany			x	x	x	
Iceland			x	x		
Ireland		x	x	x		
Italy		x	x	x		
Netherlands		x	x	x	x	
New Zealand		x	x	x		
Norway		x	x	x	x	
Portugal						x
Slovak Republic				x		
Spain			x	x		
Sweden		x	x	x	x	
Switzerland		x	x	x		
United Kingdom		x	x	x		
United States		x	x	x		x

Source: OECD, online <http://webnet.oecd.org/budgeting/Budgeting.aspx>

8 countries (Australia, Canada, Denmark, Finland, Netherlands, Norway, Sweden, and the United States) used 4 or more types of information, mostly evaluation of performance

³ Portugal produced other kind of performance information than that given in the table, Slovak Republic used evaluation reports only.

targets, measures, evaluation reports, and benchmarking. Only one country (Finland) used more than 4 types of information. 8 countries mentioned in the table used evaluation of 3 types of information, i.e. performance targets, performance measures, and some kind of reports (monitoring specific programmes, sectors, efficiency, or cost effectiveness of governmental activities) at the same time. Benchmarking as a managerial tool was used by 8 countries, i.e. (Australia, Canada, Denmark, Finland, Germany, Netherlands, Norway, and Sweden) in 2007.

The question is whether acquired performance information is further used within the management process and whether it serves to improve allocative efficiency too. From this point of view 18 countries (81.8 %) of total 22 countries selected indicated they use evaluation reports during budget discussions between the central budget authority and ministries. But at the same time 4 countries (18.2 %) of them estimated that these reports are not taken into account in the process of budget negotiations at all and further 5 countries (22.7 %) think they are taken into account up to 20 % of cases. Only 4 countries (18.2 %) think evaluation reports influence budget negotiations in the portion of 81 – 100 % of cases. As to comparison of performance information against targets the situation is slightly worse. In this case 7 countries (31.8 %) claimed this comparison has no effect on budget negotiations and 4 countries (18.2 %) admitted this comparison influenced budget negotiations up to 20 % maximally.

Also answers to the question whether failure to performance targets leads to any negative consequences such as program elimination, more intense monitoring, limitation of budget size or personal responsibility may be debatable. For example 10 countries (45.5 %) claimed that the program was almost never eliminated and 3 countries (13.6 %) thought the program was rarely eliminated if performance targets were not met. The rest (9 countries, 40.9 %) did not answer this question. 11 countries (50.0 %) further claimed that failure to performance targets led almost never to negative consequence for head of entity or ministry, 1 country (4.5 %) thought it led to negative consequences only rarely while 9 countries (40.9 %) did not answer this question at all.

Answers to the question whether not meeting performance targets means any negative consequences for future career opportunity of head of entity or ministry seems very similar. 9 countries (40.9 %) suggest there are almost never negative consequences in this case while 3 countries (13.6 %) announce negative consequences for future career rarely. 9 countries (40.9 %) did not answer again.

2 Recent development in the Czech public sector

Similarly to other developed countries also the Czech Republic was forced to solve growing long-term budget requirements and weak control over the public finance at the beginning of 21st century. For that reason a public finance reform was initiated by the Resolution of the Government of the Czech Republic No. 624 in June 2003. The real reform activity then had been launched in 2004 within the budgetary outlook 2003 – 2006 and it supposed changes in budget and accounting methodology with the aim to improve the quality of the public sector data and increase their transparency. Further the reform was directed at social system (pensions including), tax system, and public control.

2.1 Changes in the public sector reporting

An intention to reform accounting of the Czech public sector was announced for the first time in Resolution of the Government of the Czech Republic No. 561 from May 2007. In this resolution the Government defined main principles and tasks in order to launch financial reporting under the accrual basis till 2010. Financial reporting before the reform showed vast diversity of accounting legislation and outputs across the whole public sector. Mutual comparison not only between the public sector and businesses but also among particular public sector entities was limited. Besides, the Czech methodology differed from that recommended by the European Union.

On the base of an analysis of legislation, accounting outputs, and systematic research conducted in the terms of the Ministry of Defence from 2009 it can be stated following conclusions. First financial statements prepared under accrual basis were presented to external users in 2011 for the period of 2010. In comparison with the former state the structure of financial statements and their content enlarges. Statements are supplemented by formerly missing accrual elements such as depreciation of long-term assets, impairment items, or contingent items, also important changes in evaluation techniques were carried out (Vodáková, 2012a). Thanks to these changes information capability of accounting data definitely increases, they harmonize and standardize which enables better mutual comparison and orientation of external users. Accounting the fact that financial statements are obligatory revealed to the public (also via internet) transparency of accounting data increases. On the other hand there is no evidence about an intention to implement accrual basis to budget reporting at present which may be debatable because some authors point out that full

advantages of the accrual concept can be derived only in the case of its implementation to both budgeting and accounting.

2.2 Public sector management

Main principles of the public sector management and control are introduced in Act No. 320/2001 Coll. on financial control in public administration. This act defines terms like financial control in the public sector and 3E Concept, i.e. Economy, Effectiveness, Efficiency that should be obeyed within the process of the public sector management. The question is if these legislative specifications are measured and evaluated in practice. For that reason a survey via anonymous questionnaire was undertaken among economic managers of the Ministry of Defence of the Czech Republic in 2012 (Vodáková, 2012b). The survey showed following results.

Though managers have financial statements prepared under the accrual basis at disposal anytime 67 % of them stated they use these statements only occasionally for the purpose of economic management. In an open-ended question they added they still used more frequently statements of budget expenditures. As to managerial tools (performance information, benchmarking and others) they stated they had at disposal financial report (based of financial analysis of financial statements) which was prepared once a year only. Unfortunately, 58 % of respondents declared they never used this report for managerial purposes while 25 % of respondents used it only rarely. In an open-ended question managers have brought following reasons of that state: a lack of concrete performance targets and measures, inconvenient related legislation, complicated managerial structure, insufficient space for economic decision-making, a lack of incentives, and too centralised system of management. These findings that may be common to the whole Czech state administration correspond with former assumptions and partly also with results of foreign studies.

Conclusion

This paper deals with economic management in the public sector, especially at the state administration level and its evaluation. In its first part an analysis of methodologies used for preparing budget and financial statements by selected countries was carried out. In 2007 the cash basis was noticeably prevailing methodology in budget and slightly prevailing methodology in accounting reporting. While implementation of the accrual basis into accounting is received relatively positively, in the case of budget reporting a certain dislike to

adoption of the accrual basis arises. Further the paper analyses whether budget and accounting data are used in a performance evaluation process. It was found that vast majority of selected countries use any form of performance evaluation of the public sector activities. Unfortunately, this utilization seems rather formal and does not lead to consequent financial, control, or personal impacts mostly.

The situation in the Czech state administration seems similar; the accrual basis was implemented into accounting to 2010 while budget reports are still prepared under the cash basis and there is no evidence about any change at present. Though managers have reformed financial statements as disposal from 2011 they use them rather formally in the process of economic management and they still monitor budget expenditures more frequently.

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