



**THE NEW PUBLIC MANAGEMENT
A PERSPECTIVE FOR
FINANCE PRACTITIONERS**

December 2006

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FEE commissioned Eugenio Caperchione from the CIGAR network (Comparative International Governmental Accounting Research) to prepare this paper. Professor Caperchione has prepared this paper based on theoretical research and on his analysis of the survey data. FEE is very grateful for the efforts of Professor Caperchione, and in particular that this paper shows the benefit of working closely with colleagues from the CIGAR network.

CONTENTS

Introduction	4
Scope and purpose of this paper	4
Structure of the paper	5
1. Theoretical framework	6
What are the origins of NPM?	6
Is NPM a theory or a toolkit?	6
What are the main characteristics of NPM?	7
Is NPM applicable to all countries?	9
2. Financial implications of New Public Management	10
2.1 The Accounting Profession	10
2.2 The Auditing Profession	14
3. Field Research: A deeper insight.....	19
Introduction	19
Methodology.....	19
Disclaimer.....	21
3.1 An analysis of the implementation of the characteristics of NPM across the survey group.....	21
3.2 Commentary on the key themes and common messages arising from the survey.....	23
4. Identified best practice and suggestions for reformers.....	28
Identified best practice.....	28
Suggestions for countries intending to implement NPM style reforms.....	29
Annex A – Questionnaire on New Public Management	31
Annex B – Respondents to Questionnaire on New Public Management	32
Quoted References	33
Suggested Further Readings.....	36
Internet References.....	41

INTRODUCTION

In the last fifteen to twenty years a reform movement known as New Public Management (NPM) has developed and been widely discussed by both academics and practitioners.

NPM is a powerful set of reforms which can be very influential on public administrations. It advocates change in a number of areas, and incorporates different dimensions: culture, goal and performance, organisation, markets and outcomes.

The reforms have at their heart the budgeting, accounting and reporting structures as well as auditing systems. Whilst these aspects are only part of a more comprehensive set of reforms, they are a key aspect as stated by Guthrie et al. (1999: 211) “without financial management reforms, new public management would be a far less significant programme”.

In other words, NPM (and every international variation or national adaptation) attributes high relevance to its accounting and auditing components. At the same time, accounting and auditing are growing in relevance, so that “the concept of the accounting practitioner is no longer restricted to professionally qualified public accountants” (ib.). Therefore, “financial management as such stands as a language through which new public sector people increasingly have to converse – in a sense, the technical lifeblood of NPM organisational structures” (ib.).

Inspired by these theories, a number of EU countries have developed and adopted new ways of working, which, in many cases, have changed how central and local governments serve their communities and have often resulted in improved performance. The changes have also affected the day to day work of public servants and it is likely that more reforms will take place. Accountability structures, accounting rules, reporting schemes, auditing systems, to mention just a few areas, have seen significant changes. These changes have meant that finance professionals have had to re-examine and modify their traditional ways of assessing achievement and auditors have had to approach their work in quite different ways. They have also had to interact with many new stakeholders.

Given the pace of change FEE decided the time was right to examine the ways in which NPM style reforms have affected the way in which public administrations in Europe are run, and to examine the implications for accounting and auditing in particular.

Scope and purpose of this paper

This paper’s main objective is to provide an insight for public sector finance practitioners and auditors to the implications of NPM particularly with regard to the financial aspects of the reforms. It will not provide a detailed analysis of how NPM has developed, nor will it include an evaluation of the impact on the behaviour of public administrations and civil servants.

Instead, the paper will look at a number of NPM-inspired reforms which have been introduced and consider in overall terms how these have affected and are affecting the way public administrations are run and managed, with particular focus on the financial aspects of NPM. This consideration will be based on the results of a survey conducted by FEE of its European constituents.

Structure of the paper

The paper is divided into four Chapters:

Chapter 1 sets out the theoretical framework underpinning NPM and discusses the main characteristics of NPM reforms. This examination includes a review of relevant literature.

Chapter 2 looks at accounting and auditing practices in the context of NPM.

Chapter 3 offers an insight into NPM reforms adopted by some European Countries at various levels of government, based on the results of the survey conducted by the FEE. In particular it considers:

- To what extent NPM style reforms have been introduced in individual countries;
- How the characteristics of NPM reforms have been applied across the survey group; and
- What common features or key messages can be highlighted.

Whilst the analysis is of necessity limited to those European countries which responded to the FEE survey, we hope, nevertheless, that the results will be of interest to other countries both in Europe and elsewhere, where NPM-inspired reforms have been put in place.

Finally, **Chapter 4** highlights some best practice identified from the FEE survey and makes some suggestions for practitioners who intend to introduce some of the aspects of NPM.

The questionnaire used to gather data for the survey is included as an Annex along with the list of European countries who responded. There is also a bibliography at the end of the document which includes some suggested further reading on the topic.

1. THEORETICAL FRAMEWORK

The label New Public Management (or New Public *Financial* Management, see Guthrie et al., 1999) has become very popular to describe a range of management theories. However this does not necessarily mean that either academics or practitioners agree upon a specific definition of what NPM actually is.

In order to do this, following issues need to be considered:

- What are the origins of NPM?
- What is the fundamental nature of NPM? Is it mainly a theory or more a toolkit?
- What precisely is NPM? Can we identify its main characteristics?
- Is NPM universally applicable?

What are the origins of NPM?

In considering this question it is necessary to look at both academic discussion and practical implementation.

On the academic front a number of academics, and especially Hood (1991), are often considered as NPM debate initiators. However, some would argue that it is questionable whether NPM is really new. Page (2005: 713) supports for instance the claim that “NPM represents an evolution and renewal of historical trends in public administration”. Gruening (2001: 18-19) similarly suggests that “many of the theoretical origins and influences on NPM are not new”, but he also believes that “the mix of reforms that make up NPM is certainly new”. This group of academics thus often refer to ‘Public Management’ rather than ‘New Public Management’.

At least of equivalent relevance is the actual implementation of reforms. Starting in the late Seventies and continuing throughout the Eighties NPM inspired reforms have led to many changes in a number of public bodies in the UK, Australia and New Zealand. According to Barzelay (2001: 159-160) the latter case was especially remarkable, since a single three-year parliamentary mandate was sufficient to change policies in a wide range of distinct areas: expenditure planning, financial management, organisation, civil service and labour relations. These reforms have given a life and a dimension to the term ‘New Public Management’.

Is NPM a theory or a toolkit?

According to Gruening (2001: 19) “New Public Management is not a new paradigm for the behavioural-administrative sciences”. Interesting to consider, NPM is confirmation of the fact that “it is surely possible to mix practical solutions that are offered by scientists with competing perspectives” (Gruening, 2001: 21).

A somehow similar thought is expressed by Wegener (see Jones, 2004: 162), when he affirms that “NPM is nothing more than a set of almost every management tool found to be suitable for the public sector”.

In effect, NPM theory is so loose (Hood, 1991: 3) – or, at least, it leaves so much freedom for interpretation, that actual NPM-inspired reforms can hardly be defined as homogeneous. Every NPM reform picks up some of the possible tools out of the toolbox and uses them to improve the overall

performance of selected public administrations. National political and civic cultures, legislative system, size of jurisdiction, history of previous reforms are all variables which lead to a specific design of reforms in every country and for every tier of government. The NPM imprimatur does play a role, but it does not automatically lead to standardised solutions: “there is no NPM that has been used as a single concept in any country” (Wegener, op. cit.).

From this we can say that the label NPM applies to a diverse collection of reforms, some of which may have existed for some time. NPM can therefore be seen as a loose theory under which a great number of public sector innovations have been grouped – and marketed. Indeed some authors speak about “NPM-inspired” reforms: indicating that NPM is often seen as a source of inspiration, rather than a well defined theory or a catalogue of possible solutions.

NPM can therefore be said to be a loose collection of ideas which encompass many techniques and innovations, rather than a well defined and specific theory. It is thus more of a toolkit to be used as required than a management theory.

What are the main characteristics of NPM?

One way of defining the main characteristics of NPM is to pursue the analogy of a toolkit, and to identify the various tools available and understand what links them, and thus to give us a better idea of the real nature of NPM.

One of the possible ways to do that is to identify some dimensions of change, which can eventually be subdivided into more specific items.

Hood (1991), taking into account a number of different scholars’ studies, refers thus to seven dimensions:

1. **Unbundling of the public sector into functional departments** organised by product or service. This should make each unit more manageable;
2. **More contract-based competitive provision**, with internal markets and term contracts. Competition here is seen as key to lowering costs and improving standards, while the contracts can serve to clearly set performance measures;
3. Stress on **private-sector style of management practice**;
4. Introduction of **discipline and parsimony in resource use**, by stressing the need to find less costly ways to deliver public services.

With the use of these first four dimensions, public administrations are called upon to reduce the differences between themselves and the private sector as far as internal organisation and accountability methods are concerned.

Dimensions 5 to 7, on the other hand, are about “the issue of how far managerial and professional discretion should be fenced in by explicit standards and rules” (Hood, 1995: 95):

5. The need for **more visible “hands-on” top management**, so to increase the discretionary power of those who can actively control public bodies;

6. Setting of **explicit and measurable** (or at least checkable) **standards of performance**, which tend to replace the traditional confidence in professional standards and expertise;
7. Higher relevance of **output measures and output control**, especially in the sense of linking pay to job performance.

An alternative approach, as cited by Steiner (2000: 173) suggests that a comprehensive NPM approach generally incorporates following dimensions: culture, goal and performance, organisation, market, outcome. For each of those a number of possible reform tools are then mentioned.

Gruening (2001: 2) on the other hand uses a rather different approach: he simply distinguishes a long list of undisputed characteristics of NPM, which most observers identify (see Box 1) from a shorter list of debatable attributes, when observers are not unanimous (see Box 2).

Box 1 – Undisputed characteristics of NPM, according to Gruening (2001: 2)

Budget cuts	Vouchers
Accountability for performance	Performance auditing
Privatisation	One-stop shops and case management
Decentralisation	Strategic planning and management
Separation of provision and production	Competition
Changes in management style	Contracting out
Flexibility	Improved accounting
Use of incentives in personnel management	User charges
Separation of politics and administration	Improved financial management
Information technology	Performance measurement

Box 2 – Debatable characteristics of NPM, according to Gruening (2001: 2)

Legal, budget and spending constraints

Rationalization of jurisdiction

Policy analysis and evaluation

Improved regulation

Rationalization of streamlining of administrative structures

Democratization and citizen participation

Under NPM there are some common characteristics of reforms:

- Public bodies tend to concentrate on strategies (or at least they should: Pallot, 1999) much more than on the direct provision of services;
- There is extensive use of so called internal or external markets with internal prices, compulsory competitive tendering, outsourcing, agencies, and the use of functional departments all the with the aim of reducing costs, without decreasing service quality;
- The autonomy of management increases, as the many-times repeated phrase “ let the managers manage” illustrates;
- Businesses (but also charities and other institutions) tend to be seen as possible partners in service delivery (public-private partnerships);
- Public administrations tend to look for new ways to deliver their services which are improvements over traditional models;
- Accountability, transparency, information to citizens and other stakeholders and participation all acquire an increased relevance. The legitimacy of public entities is not taken for granted, it must be continuously researched and reinforced;
- New budgeting, accounting and reporting structures, as well as a new auditing system have replaced older ones;
- Performance measurement becomes a routine component of managerial practices.

Is NPM applicable to all countries?

Commentators on NPM have disagreed as to whether the reforms have universal validity. Some believe that NPM could be used as the basis for reforms in any public administration, whereas others argue that it is more readily applicable to countries which operate under systems of common law and would not be as applicable to those operating under Roman law. This has been suggested in view of the fact many of the countries leading the way on NPM inspired reforms to date have been those which apply common law. However, there are exceptions, for example the very important experiences of public administration renewal in Tilburg City in the Netherlands, which benefited from its participation to Cities of tomorrow, an international network for better government (van der Poel, 2001). Roman law countries may find that most aspects of NPM do not fit with the way that public administrations are run, and therefore fewer benefits would be observed from introducing them.

It is therefore a matter of choice for countries as to the benefits of introducing such reforms. This paper examines how NPM has been implemented in countries which have chosen to do so, and makes suggestions as to how such reforms could be applied in other administrations. However, this paper does not lose sight of the fact that implementation of NPM may not be the best way forward for all.

2. FINANCIAL IMPLICATIONS OF NEW PUBLIC MANAGEMENT

This chapter will look at the impact on the accounting and auditing professions following the introduction of NPM style reforms. It is structured as follows:

- The impact on the accounting profession, together with a discussion on the characteristics of reform of the various components of accounting and reporting; and
- The impact on the auditing profession, with discussion on how this will affect the work of auditors.

2.1 *The Accounting Profession*

The characteristics of accounting under NPM

There are various elements common to all accounting systems in a particular country, or of a specific level of government in that country. Under NPM style reforms they display the following characteristics:

- *Basis of accounting*, where administrations have moved to an accruals basis;
- *Budgeting*, comprising the plans for actions and the financing of those actions;
- *Book-keeping*, the rules and practices concerned with keeping an accurate record of the monies that are spent and received;
- *Financial reporting* concerning the reporting of financial information on the basis of which decisions are taken. This concerns both internal management accounts and published financial statements;
- *Performance reporting*, related to the collection and dissemination of information about the performance of a public body both in terms of the quality and quantity of goods and services delivered and the economy, efficiency and effectiveness of the delivery mechanism.

Cash versus accruals accounting

Once a public body adopts NPM, accounting systems will generally need to be modified in order to be able to support the new management regime. This can often mean that cash accounting systems, previously perfectly adequate for the needs of the organisation, become less so in the new NPM environment and that new systems of accrual based accounting must be introduced. This is largely due to the much more extensive information needs under NPM, particularly for decision making purposes which traditional cash accounting systems cannot satisfy. For instance NPM generally focuses on reducing costs and for that it needs detailed costing information, for instance by service or by project. Cash accounting cannot provide such information.

Another problem with traditional cash accounting is its inability to provide forward looking information, particularly for the medium to long term. Such information is crucial for assessing future sustainability. Everybody in the field can remember the impression given by the Financial Statements

of the Government of New Zealand for the year ended 30 June 1992 which revealed how long-term liabilities, so far kept out of financial reports, had made government net worth negative. This is important information for those, under a new regime of fiscal responsibility and discipline, to discharge their responsibilities.

There is no doubt that the shift to accrual accounting systems requires long implementation times and considerable investment both in terms of IT systems, data capture and staff training.

Budgeting

The first steps taken to introduce systems of accruals accounting, although successful, often were not fully effective because they did not change the financial culture of organisations and the attitudes of both politicians and managers towards the use of resources. In large part this was because budgets continued to be cash based. Without accrual based budgets, there remained the overriding imperative that all appropriated cash resources had to be utilised. This naturally reduced the importance of meeting accrual-based targets (Wildavsky, 1984; Jones-Pendlebury, 1992: 155).

Some countries that have adopted accruals accounting have also made the move to accruals based budgets. This ensures that the NPM concept of delegation of responsibility throughout public bodies applies to budgeting as well as accounting. In the long term this could be the solution for all public administrations adopting the accruals basis.

A clear theoretical foundation for accrual budgeting is presented by Lüder (1998), which was subsequently used for pilot projects in German local governments (Budäus et al., 2004).

Practical examples include the UK's adoption of Resource Accounting and Budgeting (Likiermann, 2002 and 2003) and the example of some Australian territories (Carlin, 2006). Other examples include the Netherlands VBTB where the basis of budgeting was changed to make budgets more readable and more focused on well defined items and objectives (Ministerie van Financiën, 2004). Something similar was introduced in the Italian legislation for Central Government (Caperchione-Mussari, 2002: 307-312), and later on for Regions.

Book keeping

Double entry book keeping generally must underpin a system of accrual accounting. However, with the aim of keeping it simple, some countries (e.g. Italy) allow public bodies to produce accrual-based reports without double-entry book-keeping (Caperchione, 2003: 120; Anessi Pessina-Steccolini, 2005). This has, however, led to problems where the financial statements cannot be supported by the books of account.

Financial reporting

At the very beginning of the reform process, attention was focussed on changing financial reporting to an accrual basis.

It is interesting to see that nearly twenty years ago Lüder (1987) advocated the use of commercial accounting for German public administrations, offered theoretical reasons to justify this change of perspective – and subsequently discussed technical solutions to the overriding number of problems the

transition would have raised. New Zealand was also in the vanguard in both central and local government and other countries followed, albeit some covering only a part of the public sector and others not requiring the production of the full portfolio of primary statements.

Accounting reforms have also involved the adoption of accounting standards. The need for a body of accounting standards has emerged, in order to reduce the subjectivity and discretionary power of accountants and to limit the possibility of adopting window dressing policies (see Percy, 2001: 354). The existence and use of standards also facilitates comparisons between different organisations and countries as well as between different time periods for the same organisation.

The private sector in many countries now uses International Financial Reporting Standards (IFRS) and many public administrations follow standards closely based on those, albeit with some variations to cover public sector specific situations. Many in the public sector believe that the future for public sector accounting lies in convergence between public and private sector standards, except where there are explicit public sector reasons for divergence. However, there are others who think that this may not be the best solution.

Standards for the public sector may be the responsibility of government or the accountancy profession and can be mandatory or simply recommended. The setting of Standards is usually a consultative process.

In 1986 the International Federation of Accountants (IFAC) established a Public Sector Committee. Since 1996, it has taken forward a Standards Program directed at developing International Public Sector Accounting Standards (IPSASs) for financial reporting by public sector entities at the local, state and national government level. In 2004, the Committee was reconstituted as the International Public Sector Accounting Standards Board (IPSASB) when its mandate was changed to focus more firmly on standard-setting. The Board's brief is to converge its standards with IFRS and to only produce public sector specific standards where there are particular situations not covered by IFRS. A number of countries and international organisations have adopted these standards, or developed standards based on IPSAS, although many have not.

For example, the European Commission has published its first accruals based financial statements for 2005, using a modified version of the accruals IPSAS as the basis of preparation. More information can be found in the Commission publication 'Modernising the EU accounts: Enhanced management information and greater transparency' available from the Commission publications office.

FEE has also conducted a survey into the level of implementation of accrual accounting across European countries. This will be available from the FEE website (www.fee.be) towards the end of 2006.

Performance reporting

Being held accountable for performance, as we saw in Chapter 1, is an essential part of the NPM movement and so performance measurement plays a key part in the new system.

Notwithstanding some resistance (Jones, 1994), most academics believe information on performance must be gathered and disseminated both internally for the information and use of managers, and externally, so that citizens and other stakeholders can understand the activities of public bodies (Buschor-Schedler, 1994).

The growing awareness of this need leads to a situation in which the production of information on performance cannot be considered optional any longer. The GASB, for instance, by applying the concept of accountability, deems the co-existence of output and outcome measures to be indispensable for the general purpose external financial reporting (GASB, 1994; see also GAO, 1998).

According to Johnsen and Lapsley (2005: 261) “performance measurement represents the greatest challenge and has the potential for the most significant impact (*a reinvention*)”.

Many countries have introduced performance measures, for example the UK (HM Treasury, 1999; Accounts Commission, 2000; The Comptroller and Auditor General, 2001).

In many cases, output and outcome measures are produced autonomously by the relevant administration, without any audit checks. However, there is an increasing trend for commonly accepted sets of measures to be adopted and for reported performance to be audited and often certified.

The impact on the accounting profession

As far as budgeting, accounting and financial reporting are concerned, it is quite clear that they have changed dramatically during recent years. The innovations in accounting are no doubt amongst the most impressive reforms the public sector has ever experienced, since they concern both the underpinning conceptual framework and the actual tools adopted. Key reforms are:

- The introduction of accrual-based financial reporting, which is in many cases associated with accrual-based budgeting;
- The measurement and evaluation of output and outcome, which are far more frequently compared with related targets;
- A new disclosure and communication policy, aiming at informing stakeholders both on plans and results; and
- The adoption of accounting standards.

These new processes require public sector accountants to perform a more complex set of tasks in order to provide managers with the management information that they need to work in these new environments. For example it is possible to monitor a specific service unit, by measuring its production costs, the financial sources, its output and outcome, and to compare it across over time or with other units. This can significantly enhance the accountability of public institutions, but it also requires public sector accountants to change from their traditional methods and to adopt new behaviours in line with the required practices.

It is also apparent that most countries are moving in the direction of a growing homogeneity of business and governmental accounting systems. The progressive narrowing of differences between the accounting policies used by public entities and those typical of business entities makes it easier for employees to move from the private to the public sector and vice versa, thus changing the labour market of the finance profession. Training paths are also destined to change, as they should allow people to be able to work both in the public and private sectors. This is especially true in Roman law countries, where public sector accounting traditionally used to be a judicial discipline: people currently occupying finance positions with legal backgrounds will need to become more familiar with commercial accounting practices as reforms take effect.

The role of the public sector finance manager is also increasing in importance. Public institutions have objectives to provide citizens with services or goods. As cost effectiveness and efficiency become more important to the public sector and the citizens, accountants must be able to help them to understand the economic consequences of plans. This is needed to improve decision making and ultimately the service that is provided.

2.2 The Auditing Profession

The characteristics of auditing under NPM

As with accounting, there are a number of common elements involved in auditing under NPM. These can be characterised as follows:

- *Internal auditing*, which should aim to provide independent, objective assurance and consulting services designed to add value and improve an organisation's operations and helps and organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance;
- *External auditing*, which concerns the independent examination of, and provides an opinion on, the results of public bodies together with assessment of performance;
- *Audit committees*, which are concerned with risk management in an organisation, the effectiveness of internal controls, and the supervision of the preparation of accounts and the significant accounting judgements made. They are also responsible for dealing with the internal and external auditor of an organisation; and
- *Auditing standards*, under which many auditors of public administrations must work.

Internal audit

In an organisation management is required to implement effective internal control systems and governance processes. Internal audit exists to review those arrangements and provide assurance to management on the effectiveness of those systems. Indeed in an NPM style environment, the role of internal audit is likely to be significantly enhanced. This is particularly true in the area of corporate governance, where the internal auditor has a role in reviewing the statements on internal control that management have prepared.

The Sharman Report (2001: main recommendation # 3), an important source of suggestions for the improvement of accountability in the UK Central Government, proposes that "all central government bodies should have access to well-resourced and independent internal audit, reporting to an audit committee, with its programme and performance against plan reviewed by the committee".

In expanding its role in an NPM environment, internal audit has had to ensure that its personnel have the necessary skills and that the audit methodology is appropriate.

Key changes for internal audit are thus as follows:

- Work on governance will be much more significant. Here internal audit's job is generally "... to point out weaknesses in the management arrangements in governance structure of the organisation that is being audited and point to improved methods for management to consider in the development of best value" (Percy, 2001: 359-360). Examination of governance issues will generally include looking at risk management issues;
- Work on risk management is likely to become central to the work of internal audit, both in terms of examining management's risk arrangements but also in conducting its own work in a risk based way;
- Work on internal controls is likely to be much more wide ranging, looking at non financial as well as financial controls;
- The internal auditor's relationship with the audit committee will assume a new importance in an NPM environment;
- In an NPM environment an auditor would expect to spend perhaps less time checking sample items of expenditure and more time looking more widely at the robustness of the financial control environment;
- Internal auditors may become involved in strategic planning, helping to inform the process by providing information on key controls, risks etc.;
- Internal audit may become more involved in looking at performance measurement issues, alongside external audit.

From the foregoing it is clear that internal auditors in the public sector play a significant role in the environment of NPM, particularly in the areas of risk management and governance processes.

As in the private sector, the professional qualifications and the independence of the internal auditor are very important. With respect to the latter, it will be crucial that the head of internal audit has reporting lines which are independent of operational management.

External audit

The introduction of NPM-inspired reforms (see § 1) changes the environment in which external audit operates, and introduces a number of challenges for all those wanting "to make the most of audit" (Sharman Report, 2001: 3). In rising to those challenges auditors have often had to broaden their skills, and change their approach and methodology.

The Sharman Report (2001: main recommendation # 4) refers to external audit. The traditional watchdog perspective remains in place, but "to make the most of the work, auditors should seek to combine this role with that of advisor in ways which do not compromise independence". It agrees with the position that "external audit should be based firmly on the principles of the Public Audit Forum, which emphasise the independence of public sector auditors –from the organisation being examined; the wide scope of public audit; and the ability of auditors to make the results of their work public" (ib.).

In both the public and private sectors external audit is "an examination of records or accounts to check their accuracy ... characterized by the attest function" (Granof, 1998: 609). However, in addition to

this, there is a widespread practice in the public sector that audit includes the requirement for auditors to “make, and report upon, their own independent evaluations as to whether auditees have complied with appropriate laws, regulations, and terms of grants” (Granof, ib.). Specific requirements exist in certain Member States for such compliance audit, and professional guidance is available. Public sector external auditors often also assess “whether the auditees have achieved their objectives and carried out their missions efficiently and effectively” (Granof, ib.).

According to Percy (2001: 360) “the quality auditor is therefore not just a person who reports on presentation of information but who reports on the regularity and probity of the organisation and one who acts as a *catalyst to change for improvement*” (emphasis added).

Key changes for external audit are as follows:

- The change from the cash to the accruals basis in budgeting, accounting and financial reporting has meant that auditors have not only had to understand new frameworks but have also had to be in a position to evaluate the many value judgements which are fundamental to accruals accounting. Furthermore, they are often called upon to give advice to their clients on such matters of judgement at an early stage;
- Increasingly, auditors are also examining matters of economy, efficiency and effectiveness. In other words, they are perceived as being able to “study areas of service delivery and publish studies which promote the best ideas and methods of achieving best value whilst, at the same time, identifying savings and resources which can result” (Percy, 2001: 357);
- Another important role for the external auditor is in the area of performance measurement in the public sector where they are often now involved in the assessment of the systems used to collect and present the data;
- Governance processes are also a key aspect of NPM-inspired reforms, and external auditors are called to express their view about it. In so doing they will often rely on the work of internal audit as mentioned above. As is the case for internal audit, examination of governance issues will generally include looking at risk management issues;
- Reporting to the audit committee is important to the external auditor in an NPM environment;
- In undertaking their work, external auditors cannot neglect the issues relating to their client’s strategic plans and the way in which those plans are implemented. These issues acquire a new significance under NPM because they form the backdrop for the organisation’s operations and the auditor cannot make assessments of the public sector organisation’s efficiency and effectiveness without knowledge of them;
- Accountability takes on a new importance under NPM and auditors need to consider this when assessing an organisation’s financial reporting regime;
- Traditionally, external auditors expressed opinions on financial statements. Recently, there have been calls to also involve external auditors to provide assurance on the internal controls of an organisation. Another aspect of NPM is that public sector organisations should look for innovative approaches to the delivery of public services. It has been said that it is “important that auditors recognise the danger of being perceived as discouraging well managed risk taking, and ensure that their work lives up to the spirit of statements made on attitudes to innovation”

(Sharman Report, 2001, Main recommendation # 17). (See also HM Government, 2002, Executive summary, # 8).

From the foregoing it is clear that external auditors in the public sector play a significant role in the environment of NPM.

Audit Committees

The Sharman Report (2001) also suggests (ib., main recommendation # 2) that an *audit committee* be constituted in every department. Committees should be chaired by a non-executive director and consist if possible solely of independents. They should:

- Consider whether all risks faced by the department, not just financial risks, have been properly assessed;
- Review the effectiveness of internal controls in the organisation;
- Supervise the accounts preparation process, and review draft accounts and the significant accounting judgements made within them;
- Deal with and communicate about all aspects of the work performed by internal and external auditors;
- Approve and review internal audit's work programme and receive internal audit reports;
- Challenge both external and internal auditors about their assumptions and methodologies.

These suggestions, although conceived primarily for central government, can also quite easily apply to other tiers of government, as well as for other countries.

Auditing standards

In the NPM environment, Auditing Standards take on a new importance for external auditors. Many auditors now follow International Standards on Auditing produced by the International Auditing and Assurance Board (IAASB) although some rely on national standards (for instance those produced by the Consiglio Nazionale dei Dottori Commercialisti jointly with Consiglio Nazionale dei Ragionieri in Italy). Further public sector specific guidance is produced by INTOSAI - International Organization of Supreme Audit Institutions.

For internal auditors examples are the ECIIA - European Confederation of Institutes of Internal Auditing and the IIA – Institute of Internal Auditors which has developed internal audit standards and maintains the so-called *Professional Practices Framework*, consisting of three categories of guidance: the Code of Ethics and Standards, Practice Advisories, and Development and Practice Aids.

The impact on the auditors of public sector organisations

The members of the auditing profession are constantly updating their professional knowledge and skills in order to meet the challenges of the changing environment. The implementation of NPM style

reforms in the public sector requires the auditor to respond to a number of key challenges. These include:

- The move from traditional cash based financial statements to accruals based financial statements and the adoption of Public Sector Accounting Standards. This presents a big challenge to public sector auditors as it requires the learning of an additional set of skills to audit the more complex statements being produced;
- The attention being paid to cost control in the public sector gives the auditor a role in providing independent advice arising from the audit on how the public sector can control costs without reducing the effectiveness of the service;
- Auditors may be required to monitor performance measures and the systems used to report against those performance measures;
- Auditors may be asked to evaluate the adequacy of governance structures or internal controls; and
- Attention may be made to the assessment and management of risks.

Another challenge is to ensure that the reporting lines followed by the external auditors of public sector bodies are sufficiently independent to ensure and maintain transparency and accountability. Independence for the auditor must be achieved by methods most appropriate to the individual country, but in the UK for example the auditor is accountable to Parliament rather than the bodies that they audit. It can also increase the scope of the audits that they are being required to perform. One way that this is happening is in the greater use of an internal audit service in the public sector, and by the introduction of audit committees to whom the external auditors provide reports.

In general as well as providing an opinion on the financial statements, the role of the auditor is expanding and becoming more important. Through their recommendations to management the auditor can be a catalyst for change. Thus, the auditor can demonstrate that the audit adds value to the public sector.

3. FIELD RESEARCH: A DEEPER INSIGHT

Introduction

The theory behind NPM reforms has been discussed in the previous chapters. To investigate the impact of NPM inspired reforms on European public administrations, and in particular public sector finance managers and auditors, FEE has commissioned both literature and field research.

The field research consisted of a survey of European countries. The objective was to gain an insight into the pace of change of NPM reforms, and gain an understanding of the different ways in which such reforms have been implemented. The survey also considered where such reforms have not been implemented.

The literature research consisted of a review of relevant books, journal articles, conference proceedings and grey literature in the field of NPM. The result of this research has informed Chapters 1 and 2 of this paper.

Field research results will be presented in the following manner:

- An analysis of how the characteristics of NPM reforms have been implemented across the survey group (see 3.1); and
- A discussion of the central themes, key differences and challenges experienced by countries who have implemented NPM style reforms (see 3.2).

We will then identify in Chapter 4 whether there are any areas of best or innovative practice which would be useful to share with a wider audience.

Methodology

The survey questionnaire was sent to countries that are represented on the FEE Public Sector Committee, via the individual representatives. The questionnaire was designed to prompt the survey countries to detail how the characteristics of NPM apply to their own circumstances, and to discuss how they have implemented the reforms related to NPM. The questionnaire is attached at Annex A. The list of the survey countries who responded is attached at Annex B.

Our survey allowed us to examine how the characteristics of NPM as described in Chapter 2 have been implemented.

Characteristics of New Public Management

- A. Unbundling of the public sector into functional departments
- B. More contract based competitive provision
- C. Private sector style management practices
- D. Better resource management
- E. More visible top management
- F. Explicit and measurable performance measures
- G. Relevance of output measures and output control

The questions asked in the FEE survey were linked to these seven characteristics. Below is a list of the areas which were examined as part of the survey with a description of how they map onto the theoretical characteristics of NPM:

1. Are there formally defined policies, objectives and performance measures for public sector bodies? (link to characteristics A, B and F)
2. What are the lines of accountability for those bodies? (link to A and E)
3. What systems are in place to ensure sound corporate governance and financial management? (link to B, C and D)
4. What links are in place between budgets, policies and outcomes? (link to D, F and G)
5. What checks are in place on reported public sector performance? (link to F and G)
6. What use is made of audit committees? (link to C, D and E)
7. What use is made of an internal audit service and what is the nature and scope of their role? (link to C, D, E and G)
8. In what ways are public bodies subject to external audit? (link to C, F and G)
9. To what extent are non-audit inspection bodies used? (link to C, D, F and G)
10. The extent to which public services are decentralised and / or delivered in partnership with the private sector? (link to A, B and C)

Disclaimer

The general impression from the survey and literature research is that many European countries have introduced reforms aligned to the principles of NPM. However, they have done so at different speeds, and followed different implementation paths. The results will be discussed in more detail below, but they should be considered in the light of the following cautions:

- The survey findings were provided on a voluntary basis, and as such the results must be treated with care. Specifically, the respondents would have emphasised particular aspects of that country's situation considered most relevant or up to date. When using such subjective data to compare between countries, care must be taken when drawing conclusions; and
- Describing a country's reform is not an easy task. From the survey responses it is sometimes difficult to distinguish between intentions, proposals, laws requiring change and actual implementation of those changes.

Despite these reservations it has nevertheless been possible to summarise the positions in each country as indicated by the survey response and the literature, and to comment on how the results compare across the group.

3.1 An analysis of the implementation of the characteristics of NPM across the survey group

- On **formally defined policies, objectives and performance measures for public sector bodies** we found that all survey countries had formally set policies and objectives. However, the use of performance measures to measure progress in meeting those objectives was patchier. In general, Roman law countries are much less likely to make use of formally defined performance measures than Northern and Western European countries. We also noted variations between the tiers of governments, for example in Belgium the central and regional bodies operate to one year planning cycles with no performance measures, whereas some local public bodies operate to longer timeframes and define key performance indicators in order to track progress.
- On the **lines of accountability** there was a consistent message. Public sector bodies in the survey countries are accountable to the government. In addition there is a state audit institution which examines the activities of those bodies, although differences were observed in the scope of those examinations. For example, whilst a generalisation, in Eastern and Southern countries the audit body tends to examine compliance with legal requirements whereas Northern and Western bodies take a much more traditionally financial audit based approach to their work.
- On the **systems in place to ensure sound corporate governance and financial management** there was a varied response. Some of the countries surveyed have well defined corporate governance codes and an emphasis on internal controls. Other countries are in the process of implementing systems, and some do not have formal processes in place, nor are they required to report on systems. For example, in the United Kingdom public bodies are required to prepare a Statement on Internal Control to accompany the financial statements, and the external auditor is required to review the Statement for consistency and accuracy. In Denmark and Germany there are no formal public corporate governance requirements, but moves are being made to introduce such requirements in order to increase accountability. In Hungary there are no formal reporting requirements for internal controls, but the country response indicates that they recognise that

standardisation of financial systems is an important way to increase accountability for public funds.

- On the **links between budgets, policies and outcomes** there was generally a negative response. Many countries are still focused on inputs rather than moving to outputs and outcomes (for example inputs in Cyprus are raised incrementally rather than oriented towards objectives). However, there is evidence of a gradual move away from the traditional focus on inputs. For example in healthcare in some countries the trend is towards financing hospitals based on levels of service.
- On the **checks in place on reported public sector performance** the responses generally followed those on whether performance measures are used. Where performance indicators are in place and well defined, there is generally some kind of check performed as to the suitability of the indicator and the information used to report against it. Performance audit is also evident in some countries, notably in Germany where performance audit is undertaken to look at the resources utilised in pursuing policy objectives.
- Our survey also asked about the **use of audit committees in public bodies**. The responses showed that it is not common practice for audit committees to be in place. In some countries (for example Spain) some of the larger public bodies have committees, and in others (e.g. Belgium) there are such committees but they are restricted in scope to a review of the internal audit service. In the United Kingdom, however, it is considered good governance for all public sector bodies to have an audit committee which is staffed by non-executives and whose role includes an examination of internal controls and risk management in the body.
- On the **use of an internal audit service by public bodies** we found that most countries have such a service but that there are wide variations in the scope and nature of the work undertaken, and in the reporting lines followed. Some countries have a formal internal audit service where members must be professionally qualified (usually in accounting, economics and / or law), the head of internal audit reports directly to the top person in the public body and there are mechanisms in place to ensure the independence of the internal auditors. Another common experience is that internal auditors are appointed centrally by the government and are controlled through a central committee. The survey also highlighted some differences in the use of internal audit at the various levels of government. For example in Sweden there is a formal internal audit service at a state level, but at municipal level there is much less distinction between internal and external auditors.
- Looking at how **external audit** is achieved, there was a very consistent message. The central government or state bodies are audited by that country's Supreme Audit Institution. The SAI also generally reports to the political level. There is also an increasing focus on the SAI going beyond its traditional audit perspective and examining performance and technical issues. Below the national level it is also common for the audits of public bodies to receive an external audit, and that often the audit is performed by private accountancy firms or public accountants.
- On the **use of non-audit inspection bodies** there was a mixed response. It is common for tax inspectors to be used to a great extent in the countries who responded. Some countries also use specific inspection bodies to look at issues such as compliance with labour law (e.g. the Czech Republic) or with green or social issues (e.g. Belgium). Others were silent regarding the use of any such bodies (e.g. Spain). From the responses more generally it is apparent that there is a desire for an increased use of non-audit inspection bodies to ensure compliance with new laws

and regulations. For example in Sweden there are inspection bodies at a state level to control regulatory functions.

- The **decentralisation of public services** provided an interesting mix of responses. One common feature is that all countries have tiers of government with a varying degree of autonomy for the more localised provision of public services. There is a growing tendency to contract out public services to the private sector, particularly amongst Northern and Western European countries. The number of services delivered by private finance initiative and by public private partnerships is increasing and this trend looks likely to continue. In some cases (e.g. the UK and Germany) there is increasing use of internal markets to create competition, and therefore efficiencies, in the delivery of public services.

3.2 Commentary on the key themes and common messages arising from the survey

Having gathered and analysed the responses, along with the literature research, it is possible to draw some conclusions from the results. These conclusions concern five areas:

1. To what extent have the characteristics of NPM been introduced as part of a comprehensive set of reforms?
2. Can the characteristics of NPM be implemented in practice, or are there barriers to implementation?
3. Are NPM-inspired reforms characterised by central themes or leading ideas?
4. Is accounting and auditing really changing? What impact might there be on the work of public sector finance managers and auditors?
5. What are the similarities and differences in the way that the characteristics of New Public Management have been introduced in the survey countries?

These areas will be considered in turn. Areas of best practice and suggestions for finance practitioners can also be highlighted and are considered in Chapter 4.

Has there been a comprehensive set of reforms?

The nature of reform in the survey countries is different. Some of the countries surveyed have introduced a comprehensive set of reforms for public administrations whereas others have not. Whilst the level of reform varies from country to country in terms of both the pace of change and also the decision as to whether such change is necessary, it is possible to draw two broad conclusions from the results of the survey:

- Countries from Northern and Western Europe have implemented many more of the characteristics of New Public Management than those in Southern and Eastern Europe. For example, in the North and West it is becoming common practice for performance indicators to be used to demonstrate to the citizen the effectiveness of the public administrations. In the South and East there is much less emphasis on performance indicators and more on legal reporting.

- Secondly there are indications that reforms are being implemented at a faster rate at local level than at national level. For example, Swiss cantons (Schedler, 2003: 338) and German municipalities (Reichard, 2003: 361) are two examples of front runners in the field of implementing the characteristics of New Public Management. Whilst both countries have also implemented such reforms at a national level it seems that those at local level are more embedded.

The response received from England and Wales highlighted that a number of NPM style reforms have been implemented. This can be usefully highlighted as a case study.

England and Wales: A case study

A number of the characteristics of New Public Management have been implemented in England and Wales over the last twenty-five years. These characteristics show how such reforms can be implemented in a coherent way across government and across all levels of the public administration. In England and Wales we now see the following elements:

- A strong emphasis on defined policy objectives, prioritisation and the extensive use of performance indicators. In the local authority sector there have been requirements for published performance indicators for over ten years. Health bodies have also been required to produce performance information for a number of years;
- Performance information and targets have been extensively used to monitor progress against the achievement of central government policy objectives;
- The introduction of local public service agreements, which were first announced in the UK Government's 2000 Comprehensive Spending Review. The agreements allow local authorities, which in the UK are responsible for services such as education, social services and housing, to access extra money, freedoms and flexibilities by committing themselves to meeting a range of national and local targets;
- There is considerable emphasis on sound corporate governance and a related stress on the importance of risk management in control environments. The public sector is expected to have in place systems of internal control and to regularly review and remedy defects in those systems. Most parts of the UK public sector are required to publish statements of internal control in Annual Reports or alongside financial statements. These are subject to audit by the relevant external audit body;
- There is a growing emphasis on ensuring that budget allocations are linked to policy objectives and are based on expected outcomes, not outputs;
- There is an emphasis on inspection and validation of performance and published material;
- The reform of the public services has sought to break down the rigid divisions between private and public sectors and create a model of service provision where both sectors can work together in partnership to achieve the policy outcomes.

Barriers to the implementation of the characteristics of NPM

Where the pace of reform has been brisk, the countries have indicated that implementation of those reforms is not an easy task. Again, we have found that this has two aspects:

- Where reforms have been implemented the actual working of those reforms in practice has presented difficulties. For example, England and Wales have implemented resource budgeting across government, but their response notes that “public service agreements and local service agreements are quasi-contractual mechanisms for ensuring links between budgets, objectives and outcomes. The complexity of outcomes, dependent upon the actions of a number of different agencies – and possibly attributable to none, makes outcome based budgeting problematic”;
- In those countries that have a strong tradition on the rule of law and a commonly accepted recognition of values like equality, legality and reliability, the appetite for NPM style reforms can be low. Supporters of New Public Management reforms can be considered as “hesitant reformers” and seem path-dependent (Reichard, 2003: 361).

In all cases, the commonality is that the introduction of any reforms must be accompanied by a change in behaviour in those who are to implement them. Regardless of the appetite for change, the introduction of change requires a new way of thinking and working, and this is a challenge for those administrations.

What central themes or common practice have been identified?

There are a number of common threads to the implementation of NPM style reforms. These correspond well to the theoretical characteristics discussed earlier in this report and can be found across the survey countries where such reforms are advanced. Where common threads are identified this may also help to overcome obstacles and ensure greater coherence in any reform set.

The identified common themes are as follows:

- **Transparency:** Many of the countries who responded quoted this aspect as a key principle in any set of reforms. This is embodied by the situation in Sweden who responded “Since the end of the 18th century, there is a law to guarantee that every report, decision document, literally all documents existing within an agency or a ministry will be fully open to the public at large at their own convenience. The principle will serve as a guarantee that the governing of a public body is done properly. Within the public sector at large, having this principle of total openness to anyone interested, it has been said that no other governing principle is necessary”;
- **An emphasis on financial management and corporate governance:** This is linked to the principle of transparency. The Netherlands introduced in 2000 the ‘Government Governance’ framework and commented that “Transparency and coherence are central themes: the transparency of relations between organisations and the transparency within organisations are essential to achieve good governance. It must be clear who is responsible and for which processes”. Government Governance in the Netherlands serves to introduce a coherent approach to four elements: management, control, supervision or oversight and accountability. The Norwegian way towards sound governance and financial management has also a quite clear reference point, at least for Central Government: “the Office of the Auditor General undertakes controls testing in order to form an opinion about whether the minister concerned has performed his tasks as the administrator of the national interests in keeping with the decisions and intentions of the Storting”;

- **The role of managers:** The key point of such reforms is to ‘let the managers manage’ and be assessed on performance, rather than operate under constraints. A good example is the response from the Netherlands, where managers are put at the heart of the reform process. The Dutch view is that “Management has a responsibility in creating sound financial management, including effectiveness and efficiency. They have to receive proper management information about the quality of the management control system. The control function has to provide basic quality guarantees in the processes. The introduction of VBTB has given rise to more explicit responsibilities and duties for management”;
- **Performance reporting:** This is also a common element whereby the public administrations are required to report on how effectively they have met their objectives over the period. For example, the response from Denmark shows that they believe effective management of the public sector includes “contract management, performance audits and reporting on the achievement of goals”;
- **Decentralisation:** This is about finding the most appropriate way to deliver the services, defining those services as products and setting objectives around the delivery of those products. This may include the involvement of the private sector in the delivery of services if this is considered to be a more efficient way of delivering them. This was seen back in 1993 in Germany where KGSt, a municipality-funded non-profit institution, formulated its NPM variant under the label “Neues Steuerungsmodell” (New Steering Model). This model was derived from the international new public management discourse and, more specifically, on the new public management-guided modernisation concept worked out and put in practice in the Dutch town of Tilburg. Amongst others the Neues Steuerungsmodell introduced intra-organisational decentralisation and autonomy of resource management and responsibility. The idea was to conceive the tasks of public administration as products and to define them in terms of objectives to be achieved (outputs) and of the resources and costs involved (inputs). This idea was then transformed by the implementation of *Kosten-Leistungs-Rechnungen* (cost-achievement accounting) and controlling systems. Over ten years later these principles remain in Germany. In 2004 the Land Nordrhein-Westfalen passed a law requiring local governments to convert their accounting to the accrual basis by December 31st, 2008 and to set product-oriented goals considering the revenue and the consumption and to define indicators as basis for the budget process, the execution and the controlling of the effectiveness.

Is accounting and auditing changing?

Most countries across the survey group have undergone, or are undergoing, reforms of their budgeting, accounting and reporting systems. However, the pace of change and the details of those changes are not homogenous across the different countries. This can be demonstrated by highlighting a few examples:

- In the UK Central Government, Resource Accounting and Budgeting (RAB) was introduced in 2001. It consists of a system of planning, controlling and reporting on public spending for government: on one side it is the basis of public expenditure planning and control, and at the same time it is the application of accruals accounting for reporting on the expenditure of central government and a framework for analysing expenditure by departmental aim and objectives, relating these to outputs where possible (see Likiermann, 2003, for details);
- Germany has started reforms at the local level, with pilot projects in various Länder (Lüder, 2005): most projects are characterised by the introduction of both accrual budgeting and accrual

reporting. The Länder are currently passing specific bills, in order to make those changes mandatory. At the same time, some Länder (Nordrhein-Westfalen, Hessen, Niedersachsen) have started a transition of their own accounting system;

- In Denmark accruals-based budgeting systems have been tested in pilot institutions. The current system is expected to be transformed by 2007-08;
- Italy has reformed local government accounting as well, and has introduced a mandatory external audit for all municipalities. The budgeting and accounting remains cash based;
- Significant reforms have also been proposed in the Netherlands (Ministerie van Financiën, 2002) to improve the information value and the accessibility of departmental documents on budget and budget accountability. The main features of this new system are a central role of policy objectives, concrete operational priorities and performance indicators, coherence between budget and accounting documents, careful formulation of policy objectives which need to be made tangible as performance data (indicators) and other instruments to measure efficiency such as policy evaluations, which contribute to the measurability of performance and effectiveness.

Public sector finance managers and auditors are therefore operating in a changing environment. With change comes the need for training and re-education in the principles involved. The move, for example, from cash based budgeting and accounting to accruals based budgeting and accounting requires a new set of skills both for those preparing the information and those validating it.

What similarities and differences exist in the reforms?

The similarities shown by the reforms are characterised by the common elements described above. However, these need to be considered in context: every country, notwithstanding its adoption of reforms, remains characterised by its history and tradition, its culture, and its constitutional and administrative systems. A fundamental diversity in Europe is that some countries can be described as operating under civil law, others under common law. It is not possible for all countries to therefore take the same approach to any reforms, particularly those that demonstrate the characteristics of NPM. For example, in the Czech Republic external inspection has been introduced to look at compliance with labour law. We can therefore conclude, as per Schedler-Proeller (2000: 5), that there is not one model of New Public Management, but there are as many national variants as there are nations.

In addition, just as there are variants between nations, the survey also highlighted differences between the different tiers of governments within those nations. For example, the Swedish Constitution guarantees that local governments are autonomous from their central government. As a consequence, although central government monitors local governments through its inspection bodies, the decision-making process itself is autonomous. Sweden has thus the need to design its reforms taking into account this aspect, while many other countries, with a tradition of a higher influence of the central government, will quite clearly act differently.

4. IDENTIFIED BEST PRACTICE AND SUGGESTIONS FOR REFORMERS

Identified best practice

The questionnaire survey highlighted a number of countries where reforms have been implemented in a positive way. Whilst this report recognises and has highlighted that any reforms must be placed in the context of the culture and constitution of the countries, the following examples could be considered as principles which could be modified and applied to all countries considering implementing similar practices.

Most of the identified best practice therefore comes from Northern and Western European countries as these are the countries that, by and large, have chosen to implement reforms displaying the characteristics of NPM.

The Netherlands – Emphasis placed on management controls

- Emphasis placed on the autonomy of the managers and the abilities of the staff.
- Management controls are seen as a way of safeguarding the quality of the processes. The risks of the business operations have to be outlined systematically and measures have to be taken to remove, reduce or at least control the risks.
- The requirement to produce a “control statement” requires a ministry to have a management control system that satisfies the most important requirements.
- The awareness that budgeting and accounting in an integrated way on policies, business processes and resources creates new information needs of managers and that consequently the role and attitude of the financial, control and audit functions are significantly enhanced.
- The content and presentation of a ministry’s budget and accounts have been amended so that performance, budgets and accounts are presented in relation to each other.

The Netherlands – Effective use of performance indicators

- Public sector bodies are required to formulate key objectives. These objectives have to be “smart” i.e. they must be specific, measurable, accurate, realistic and time-related.
- Relevant performance indicators to report against the key objectives have to be defined in advance of the period being reported on.
- The ministry audit department has to give an opinion on the reliability of financial information with a level of confidence of 95 per cent and a tolerance of 1 per cent. In most cases, however, it is not possible to use the same percentages for non-financial information. Defining the appropriate level of reliability is necessary to prevent an expectation gap being formed. Ideally, management should indicate the quality of non-financial information. The reliability of the performance indicators may be validated in special assurance assignments requested by the minister or management.

- The audit of the annual report does not lead to an opinion on the reliability of the non-financial information. In 2006 and beyond the annual report contains a statement in which possible inadequacies in the gathering and reporting of non-financial information included in the annual report are reported to parliament. The audit department is responsible for reviewing this process and the statement included in the annual report. Any audit outcomes from this review are included in the auditor's report to the minister.

Sweden – Use of benchmarking performance

- Since the early Nineties the appropriations contain instructions on certain objectives and important issues for public sector bodies. The agencies have also been greatly encouraged to define and describe their own key performance indicators and to report on them and on their development in their yearly financial statement, within the performance report part of the document.
- There also exists, from the ESV (Financial Accounting Agency), a benchmarking activity which is done every year at a state, regional and local level. This examines the agencies' abilities to fulfil their obligations regarding the financial statements. This can then highlight issues and enable improvements to be made.

United Kingdom – Linking performance to operations

- In the UK, for high performing public sector bodies, meeting targets may result in more freedoms being offered. For example, a reduction in centrally imposed regulations from Government, or greater freedom to borrow or spend centrally provided funds more flexibly.
- Performance against targets is used both as a punitive measure and as an incentive for the individual public sector bodies.
- For example, if targets are not met there may be closer supervision by sponsoring government bodies, or the threat of non-renewal of senior staff contracts.

Suggestions for countries intending to implement NPM style reforms

There are a number of recommendations to be made. However, these are not intended to be prescriptive and countries should interpret the recommendations in light of their own circumstances. The aim of the recommendations is to provide a set of principles to follow rather than to prescribe a way of working which may not be appropriate to the individual circumstances of a country intending to implement them.

The recommendations which follow are therefore insights based on the experiences of the countries who responded to the survey, together with findings from the theoretical research.

1. **The use of performance indicators.** Those countries who have implemented performance measures, and who report against them, are able to better demonstrate the value added by the public sector to the citizens who fund it. Performance indicators can be both more relevant to daily life, and can be more understandable to the citizen than the information contained in financial statements. They can provide the link between the taxing of the citizen and the outcomes that the citizen receives. Performance indicators show the achievement of the public sector against objectives, whilst financial statements can show only the costs involved.
2. **Checks on performance measures and benchmarking.** Where performance indicators are used it is important that the information used to report against them is reliable, relevant and accurate. Implementing checks on the systems used to collect the data and report against the targets is another key way that the public sector can demonstrate to the citizen its principles of transparency and consistency. In addition, comparing performance by using bench marking can be used as a useful tool to identify areas for improvement and recognise good performance, as well as providing useful information for citizens.
3. **Budgeting for outcomes, not inputs.** As part of accounting and budgeting reforms, countries can now link their budgets to their objectives and outcomes, rather than basing budgets on historical need. In this way, resources can be targeted at areas where they are needed. Budgets could also be prepared on an accruals basis to ensure that better decision making is taken by those using the resources.
4. **Implementation of audit committees.** Audit committees can be a useful tool to secure an effective check on the procedures and systems operated by managers in the public sector. Where used well, the audit committee can examine the procedures for risk management and implementation of internal controls in the organisation. By including non-executives the committee can also bring external expertise to bear on the running of the organisation.
5. **Use of internal audit.** Most of the survey countries had an internal audit service. However, to get the best from internal audit there are opportunities for the audit committee to be the body which oversees their work. The audit committee can also have input into the implementation, by public sector managers, of the internal audit recommendations.
6. **Training for finance staff.** As reforms for budgeting and accounting take hold, there will be an increased complexity of work for public sector finance workers. Public sector bodies should ensure that finance staff working in the changing environment are equipped in terms of the necessary skills to perform these tasks to the best of their abilities.

ANNEX A – QUESTIONNAIRE ON NEW PUBLIC MANAGEMENT

1. How is effective management and supervision of public bodies achieved in your country? What are the lines of accountability for central, regional, and local government bodies?
2. To what extent have formally defined policy objectives, operational priorities, and performance indicators been introduced for public bodies in your country?
3. What mechanisms are in place to ensure sound financial management of public bodies in your country? What is the role of management information in this process?
4. What are the systems for achieving sound corporate governance of public bodies in your country?
5. How close are the links between budget allocations, policy, and outcomes in your country? How does this affect the budgetary process?
6. What checks are made on the reliability of performance indicators and reported outcomes?
7. Have audit committees been introduced for public bodies in your country? What is the scope of their activity?
8. Do government bodies in your country have an internal audit service? To whom do the internal auditors typically report? What qualifications are required of internal auditors?
9. How is the external audit function exercised in government bodies in your country? How is auditor independence assured? To who are audit reports addressed? How are audit findings followed up?
10. Are there inspection bodies, as distinct from auditors, for specific public services? How are they appointed, and to whom do they report?
11. To what extent is the private sector involved in the provision of public services in your country?
12. How far is service provision decentralised in your country? How are common standards maintained in a decentralised environment?

ANNEX B – RESPONDENTS TO QUESTIONNAIRE ON NEW PUBLIC MANAGEMENT

Countries who responded to the questionnaire were as follows (in alphabetical order):

- Belgium
- Cyprus
- Czech Republic
- Denmark
- Germany
- Hungary
- Italy
- Lithuania
- The Netherlands
- Norway
- Poland
- Spain
- Sweden
- Switzerland
- United Kingdom (Scotland)
- United Kingdom (England and Wales).

This represented sixteen responses from fifteen countries.

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