

## Accrual Accounting: Change And Managing Change

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### Abstract

The Malaysian government has decided to adopt accrual accounting to enhance financial accountability and to have a better asset-liability management. Based on experiences of other countries such as Australia and New Zealand, the change process has to be properly managed to ensure successful implementation of the new accounting system. Employees' commitment to change has been identified as a critical factor in organisational change. Commitment to change model as proposed by Herscovitch and Meyer consists of three components: affective (want to change), normative (ought to change) and continuance (have to change). Hence it is very important for public sector organisations to identify and manage organisational and individual factors influencing commitment to change. The literature has identified factors including organisational support (ICT and human resource), top management support or leadership, communication channel and flow, attitude towards change, employee participation or involvement, are pivotal to successful implementation of accrual accounting. Thus, a study will be conducted to investigate whether the Malaysian government is ready to embrace the change or otherwise.

Keywords: accrual accounting; governmental accounting; managing change; commitment to change; organisational readiness.

### 1.0 Introduction

Public sector transformation has been identified as one of the eight strategic reform initiatives (SRIs) under the New Economic Model (NEM) for Malaysia. Accrual accounting has been identified as one of the policy measures for Public Sector Transformation with the main focus to facilitate asset-liability management in public sector. Under the current modified cash-based accounting system, very limited information on assets and liabilities are recorded in the financial reports, thus give rise to concerns related to risk associated with inattention to asset-liability management. In addition, accrual accounting is argued to provide a better picture of government financial position as under accrual accounting, government assets and liabilities will be disclosed in financial reports. Good asset-liability management is critical for public finance sustainability as many of the assets or liabilities are long term in nature and of very significant amount. Accrual-based reporting is argued to reflect full cost service provision and enhance performance measurement and accountability (Saleh and Pendlebury, 2006).

However, it should be noted that benefits of accrual-based reporting are yielded only to the extent that people make use of the information. There are costs associated with the change in accounting system for the public sector. Difficulties in changing the system include resistance from accounting staff, compiling records, asset measurement, determining the valuation basis and dealing with the complexity of the public sector organisation in general. Huge resources are necessary to implement the new system, including the cost of training and employing people with the right qualifications.

Countries that have fully applied accrual accounting include Australia, New Zealand and United Kingdom. The rate of full adoption between these countries differ as each country has to deal with issues such as required changes in the rules and legislation as well as acceptance of the policy makers and implementers. Relative to Australia and New Zealand, the United Kingdom took more than 10 years to fully adopt accrual accounting. In the UK, accrual accounting has been implemented successfully at various levels of their government organisations. The success was not an easy achievement but a sum of hard work a huge budget – proper management, guidance, frequent and consistent communication and support from the top have been proven as among the factors contributing towards this success (Abu Hasan, 2012). Developing countries including South Africa, India and Jamaica have started the process to adopt accrual accounting while others such as Argentina, Albania and Pakistan have expressed intention to adopt accrual accounting but are still taking the ‘wait and see’ approach.

The objective of this paper is to give an overview of factors influencing change. This paper is organised as follows. The first section presents an overview of the development of accrual accounting adoption by the Malaysian government. This is followed by a discussion on managing change. Section 2.3 continues with a discussion on commitment to change and section 2.4 provides factors influencing commitment to change.

## 2.1 Moving Towards Accrual Accounting

Cash basis has been used to account for financial transactions of the federal government since Malaysia gained its independence. Subsequently, modified cash based accounting was adopted in 1974 to cater for the need to have full cost information under the programme and performance budgeting system. However, as size and activities of the government expanded, and economic resources became limited, there was concern about financial accountability as well as efficiency and effectiveness of government service provisions. Information provided by the cash based accounting was not sufficient to assess financial performance of the government. This led to the consideration for adoption of accrual accounting which is argued to provide better financial reporting, reflect financial position and full cost of service provision (Saleh and Pendlebury, 2006).

Efforts to adopt accrual accounting for the Malaysian federal government started in the 1990s. A group of personnel from the Accountant General's Department (AGD) visited the Australian government to learn from its experience in implementing accrual accounting. However, after the visit, the idea to adopt accrual accounting was not pushed forward. Later in the early 2000, as part of business reengineering process and information technology strategic plan, once

again the need to adopt accrual accounting was deliberated. The AGD put forward an accrual accounting migration conceptual plan to be implemented in 2008 (AGD Circular, Issue No. 1, 2003). Although the AGD obtained a system known as Government Financial Management Accounting System (GFMAS) that can cater for accrual accounting, the new basis of accounting was not being implemented. According to Saleh (2002), accounting change is difficult to occur because the structural variables, the societal (professional accounting bodies), political (support from politicians) and administrative (Treasury and AGD), were not favorable to accounting innovation. In addition, lack of qualified professional staff was also found to be a barrier to implementation.

In an analysis of the stimuli for change in the Malaysian governmental accounting, Saleh (2002, p. 208) concludes that "in order for Malaysia to be most favourable to major changes in governmental accounting, there is a need for a strong influence from the professional bodies, preferably with advisory responsibilities and accountants with knowledge of private sector accounting". The decision to adopt accrual accounting in 2010 came about after involvement of professional stakeholders in government strategic plan, whereby, in 2009, the government appointed economist, business leaders and corporate adviser to be members of the National Advisory Economic Council (NEAC) to advise the government on a new national economic model. One of the issues highlighted in the NEM report is the need to have a good asset-liability management which will enhance government accountability and critical for public finance sustainability. The current cash based accounting does not capture information on assets and liabilities thus, it was decided that the government should adopt accrual accounting. Consequently, migration to accrual accounting is stipulated as one of the policy measures to stimulate reforms in the public sector (NEAC, 2010). Thus, the Malaysian government finally decided to embrace change in the accounting system as a result of strong professional influence.

As stated earlier, adoption of accrual accounting is very costly. Thus, the change must be managed properly to ensure successful implementation of accrual accounting. Since several countries have already adopted accrual accounting in the public sector, the Malaysian government could learn from these countries' experiences. In the case of New Zealand (International Federation of Accountants (IFAC), 1994), the key factor in the successful implementation of the new financial management regime was attributed to support from leaders in the public sector as well as effective risk management. The government employed intensive communication strategy to ensure change message reached the intended targets and the reforms are fully understood and embraced by individuals affected by adoption of accrual accounting.

In a study conducted for the Treasury Board of Canada, lessons to be learned from the Government of New South Wales, Australia and organisations that have fully implemented accrual accounting in Canada among others include the following:

- The need to first analyse the various options for implementation, followed by a strategic plan for introducing the selected option with full costs.
- As part of preparation for conversion, the government should identify the accounting principles as well as introduce organisational and procedural changes that will take place.

- The need to manage resistance to change. According to the study, “changes not only involve implementing new systems but also a significant cultural change in the ways managers understand and use financial information and in how financial transactions are handled.” (Treasury Board of Canada, 1997)
- The need to ensure that everyone is involved and committed which require strong leadership.

Learning from the experiences of other countries in implementing accrual accounting, it is evident that the Malaysian government has to ensure the change process is properly managed to achieve its intended objectives. The next section discusses issues related to managing change.

## 2.2 Managing Change

Change is conceptualised by Damanpour (1987) and Daft and Becker (1978) as the extent of changes adopted in a given period or as the extent to which changes are integrated into the operations (Downs and Mohr, 1976). Carnall (1986) defines organisational change as an attempt or series of attempts to modify organisational structure, goals, technology or work task. According to Armenakis et al., (1999), the process of organisational change typically consists of three phases: readiness, adoption, and institutionalisation. The first phase, readiness, involves the process of preparing organisational members for the change. During the second phase, adoption, the change is implemented and employees need to adopt and adjust to the new systems. During the third phase, the change is maintained and reinforced until it is internalised and becomes a norm.

In the context of public sector organisations, managing organisational change is among the greatest challenges to politicians and officials. In embracing change, the designers of the new system must ensure that elements in change must be understood and aligned (Halachmie and Bouckaert, 1996). Those elements include objectives for change, measurement items, targeted levels in an organisation, who would be responsible, what kind of information is expected and who would need the information must be clear and agreed upon.

For most organisations either private or public, change can be hindered by lack of top management support, lack of infrastructure support, employee resistance, poor communication, lack of readiness and lack of expertise. Organisational change initiatives often fall short of expectation or abandoned halfway through due to lack of skills among contemporary leaders in handling the changes rather than flaws innate in the change initiative itself (Choi, 2011; Armenakis and Harris, 2002).

Change may also cause problems to productivity if applied or implemented incorrectly (Gabris, 1986). The author outlines several traps in introducing or implementing new system or making changes in it as time goes by:

- i. Process Burden: the implementation and maintenance of procedural and control

requirements for the measurement system that distracts employees from their actual responsibilities (Gabris, 1986, p. 6);

- ii. Georgia Giant Syndrome: management techniques that work only under comprehensive supervision and control conditions. The expected and potential of the technique will not be achieved if control conditions are not met (Gabris, 1986, p. 8);
- iii. Internal Incapacity: the result of superimposing a technique on an organisation that lacks the in-house capacity to implement and monitor the technique beyond its initial phases (Gabris, 1986, p.10); and
- iv. Credibility Anxiety: many management techniques piled on top of one another, although they do not work well. New techniques are expected to produce dramatic and quick results; when results do not materialize after a short time, top-level appointed and elected officials deem the techniques' application a failure and responded to it by trying a different set of techniques (Gabris, 1986, p. 13).

The traps mentioned above would affect employees and organisation in terms of productivity, motivation and morale.

Most theorists acknowledge the significance of structural stability for organisations commissioning change. Managing for change as discussed widely in the literature emphasized the importance of ensuring proper structure are in place for organisations to have successful change and permits organisation to evolve (Schwarz and Shulman, 2007). A properly managed and smooth change process can facilitate and persuade people to embrace change (Edmonds, 2011). In relation to this, the literature has identified that one of the most critical challenges organisations need to address is limited structural change (Hannan and Freeman, 1977). Limited structural change refers to "a resistance to change rooted in the size, complexity, and inter-dependence in the organisation's structures..." (Tushman and O'Reilly, 1996, p.18). Structural change literature presented five reasons why limited change structural come about. First, limited structural change occurs due to a default homeostasis position or the tendency among organisations to maintain existing structure (Schwarz, 2006). As a result, change in an organisation is limited or slow because of lack of alterations made to the existing structure. Thus, to facilitate change, significant alternations must be made to current structure to reflect proposed change.

Second reason is lack of critical reflexiveness i.e. people do not consciously monitor the ongoing need for change and therefore lack of motive or intent to change (Giddens, 1984). The next reason for limited structural change is when organisational members only allow their personalized experience and anchor their previous experiences; expectations and habits which somewhat limit the overall change to take place (Ocasio, 1997). This reason views organisational members involved in change as part of the organisations' structure. Limited structural change also said to be due to limited implementation within organisations (Carlopio, 2003). What works best is widespread implementation across the organisation permits successful change and prohibit artificial internal barrier to change. The final reason that restricts change is regulative, normative and cultural institutional pillars (Scott, 2001). According to Mizruchi and Fein (1999), this reason is a powerful constraint contributing to limited structural change

in organisations.

In view of the importance of change initiatives in achieving organisational objectives as well as the significant amount of resources involved in implementing the changes, identifying the factors contributing to the success of change programs is paramount. This renders discussion on factors that influence organisational readiness to embrace change or employees commitment to change.

### **2.3 Commitment to Change**

Commitment to change has been argued to be one of the most important success factors for any change initiatives and organisational effectiveness (Isa et al., 2011). Often times change efforts fail due to unwillingness of employees to support or participate in the change initiatives. As a change process is usually difficult and demands adjustments from employees, they often feel threatened and insecure. Thus, it is pivotal for organisations to identify factors that will help organisations to garner support and commitment from their employees.

Commitment to change is described as “the glue that provides the vital bond between people and change goals” Conner (1992, p. 147). According to Herscovitch and Meyer (2002, p. 475), commitment to change refers to “a mindset that binds an individual to a course of action deemed necessary for the successful implementation of a change initiative”. Herscovitch and Meyer (2002) developed a model of commitment to change which proposes three components of organisational commitment to change: Affective, Normative and Continuance commitment to change. Affective commitment to change refers to “a desire to provide support for the change based on a belief on its inherent benefit” (Herscovitch and Meyer, 2002) or ‘want to change’ (Rashid, 2008). Normative commitment to change reflects the “sense of obligation to provide support for the change” (Herscovitch and Meyer, 2002) or ‘ought to change’ (Rashid, 2008). Continuance commitment to change is based on “recognition that there are costs associated with failure to provide support for the change” (Herscovitch and Meyer, 2002) or ‘have to change’ (Rashid, 2008).

### **2.4 Organisational and Individual Factors Influencing Commitment to Change**

It has been argued that organisational and behavioral factors such as organisational support, leadership, effectiveness of change message and information flow, attitude towards change, and employee participation are pertinent in enhancing commitment to change. According to Choi (2011), many researchers have argued that organisational change can only be successful and sustainable over long term if the organisation is able to alter the on-job behaviour of its employees appropriately. In other words, it is believed that employees are at the centre of organisational change. As accrual accounting represents change in a system, both organisational and individual factors influencing change must be identified and effectively managed to ensure successful implementation of the change program.

Having adequate and efficient organisational support which include information systems and

human resource is one of the most critical factors in successful change programs. The implementation of accrual accounting will require certain modifications to the current information and communication technologies (ICT) to support additional information needs under the new system. In addition, organisations need to ensure that they have adequate number of well trained staff. Staff who are directly involved in the implementation of the change programs must be well informed through relevant information channels and training programs. It has been argued that understanding of the needs, efficacy, appropriateness, and top management support for the change, as well as the impact of the change on the employee, will “shape an individual’s motivations, positive (readiness and support) or negative (resistance), toward the change” (Armenakis and Harris, 2002, p. 170)

In addition, it is relevant to note that leadership is significant for organisation in adopting any reforms, and leaders have to support their subordinates in embracing the reforms. Leaders and their leadership style are important during transformation time. Reforms are normally made through top down exercise, which requires strong leadership. Based on Leader-member exchange (LMX) theory, Scott and Bruce (1994) argue that high quality relationship between supervisor and subordinate, which allows greater autonomy and decision latitude to subordinates, is related to greater acceptance to change. Thus, leadership and staff participation are two vital factors in ensuring successful reforms in the public sector.

Leaders are normally expected to provide supervisory feedback to subordinates: positive feedback for commendable performance and negative feedback for unacceptable performance. This reward and punishment system is viewed as a transactional leadership style (MacKenzie et al, 2001). Several researchers have promoted a transformational leadership style over other traditional forms of leadership (i.e. transactional) as best suited to achieve organisational goals (Awamleh, 1999; Conger, 1999; Dubinsky et al, 1995). Transactional and transformational leadership are common in providing clarity of desired outcomes, recognizing accomplishments, and rewarding high performance but differ in process and behaviour (MacKenzie et al, 2001). The transformational leadership style requires adaptation of values, goals, and aspirations to be consistent with subordinates, implements change through communicating vision, clarifying performance expectations, promoting acceptance of group goals, providing individualized support and intellectual stimulation.

Change initiatives often fail to achieve the targeted goals due to lack of employee commitment and poor communication between the various departments affected by the change program (Conner and Patterson, 1982). Researchers have proposed several ways for reducing and overcoming people’s resistance to change. For example, Argyris and Kaplan (1994) have stressed the importance of communicating the proposed change to the people in the organisation. Since communication is an instrument to pass information regarding the change, it can increase the recipients’ knowledge about the change. Good communication about the change process or effective change message to all employees is paramount. Employees need to be well informed about the change initiatives in order for them to be committed. It is difficult to gain support from employees if they do not know what specific changes are going to take place, how the changes are going to affect them and how they will benefit from the change process. Thus, through communication, people’s attitude and perception toward the proposed change become more optimistic (Jermias, 2001).

Through effective flow of information, employees are informed about the change initiatives and their opinion or belief will be affected by the effectiveness of the change messages, which will be part of the process of deciding whether to support or resist the change. In essence, effective change message forms the backbone for successful change implementation (Armenakis et al., 2007). Change messages are usually transmitted between the various levels of organisations by the various change agents (top leaders, supervisors) as well as other individuals such as peers of change recipients. Furthermore research has shown that improved communication leads to employee job satisfaction and commitment which later result in benefits to organisations (Hargie and Tourish, 1996).

Another way of overcoming resistance to change is by allowing people to participate in the change process, which can induce their initial commitment to the new initiatives. Change also requires active commitment of staff through team-working, increased communication and consultation besides employees compliance and conformity (Walton, 1985). Staff participation and involvement has been widely recognized as key to successful modernization and reform in public administration system (Powls and McDougall, 1984). Allen et al. (1997) defines participation as the degree to which a person participates or continually engages in organisational activities. Employee involvement and participation are recognized ways to increased organisational adaptability, reduce resistance to change among employees, and enhances employees' support for workplace changes (Delaney and Sockell, 1990). Literatures suggest that employee active participation in organisational change process contributes in at least one of these three aspects:

- i. Participation in the change process will increase employee commitment to change and reduce resistance towards change;
- ii. Involvement in the change process will unveil the creative potential of workers, allowing the organisation to identify ways of changing that can enhance organisational performance;
- iii. Participation in the change process also works as control mechanism that reinforces change, thus reducing the need for monitoring of organisational changes afterwards.

In addition, attitude towards change may also influence success of a change program (Dunham et al., 1989; Isa, 2007). Attitudes toward change generally consist of a person's cognitions about change, affective reactions to change, and behavioral tendency toward change (Dunham et al., 1989). Elizur and Guttman (1976) also provided similar classification of individuals' or groups' response to the introduction of organisational change. They classified the response into three types. Affective responses are a greater or lesser feeling of being linked to, satisfied with, or anxious about change. Cognitive responses are the opinion one has about the advantages and disadvantages, usefulness, necessity, and about the knowledge required to handle the change. Instrumental responses are the actions already taken or which will be taken in the future for or against the change. Responses to a particular change may vary from one individual to another.

Different individuals may react differently to a particular change. For some, change may result in satisfaction, joy and advantages, while for others the same change may bring pain,

stress, and disadvantages (Yousef, 2000a; 2000b). Individuals with positive attitude towards change are more receptive to changes while those with negative attitude may be resistant to changes. The level of attitude towards change of accountants or the financial controller who are involved in the implementation of change programs such as the implementation of accrual accounting will influence the level of commitment to change. Those who are more receptive to change would be more likely to initiate changes and ensuring the changes are effectively implemented (Isa et al., 2005).

### 3.0 Conclusion

The implementation of accrual accounting involves significant cost to the government. Thus, critical factors for success including infrastructure support, human capital as well as organisational and behavioural factors influencing change must be assessed to gauge the level of readiness to the change and to devise appropriate strategies in managing these efforts carefully to ensure its success. Many public sector studies have forwarded evidence of the critical role that public managers play in bringing about organisational change (e.g. Abramson and Lawrence, 2001; Bingham and Wise, 1996; Borins, 2000; Hennessey, 1998). Therefore, it is pertinent to obtain awareness and perceptions of policy makers and implementers regarding organisational readiness to adopt accrual accounting. The development of accounting information system and adequate skilled personnel involved in implementing accrual accounting, in particular, warrants explanation.

Based on the discussions forwarded above, the main question that arises is whether the Malaysian government is ready to embrace change or otherwise. This includes organisational readiness in terms of structure and operational, adequate infrastructure particularly accounting information system and individual readiness which include appropriate knowledge and skills. Specifically, the following questions should be addressed to explore the possibilities of successful embracement of change for Malaysian government:

- i. What is the current organisational readiness to change towards accrual accounting?
- ii. What is the current level of individual awareness and commitment to change towards accrual accounting?
- iii. What are the factors influencing commitment to change towards accrual accounting?
- iv. How should the government organisation be structured to successfully embrace change towards accrual accounting?
- v. How operations of a government organisation should be arranged to ensure change towards accrual is successful?
- vi. What should be an appropriate information system of a government organisation in successfully embracing change to accrual?
- vii. What are the appropriate level of knowledge and skills of government employees to guarantee change towards accrual accounting is successful?

Hence, to feed into the above questions, a research is worth conducting to assess and measure factors that contribute toward commitment to change and the level of readiness to change among policy makers and implementers of accrual accounting in the Malaysian federal government. Additionally, the research could also be extended to investigate the role of organisational (structure, operations and system) and individual (knowledge and skills) factors in enhancing commitment to change will also be investigated.

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