Mastering the Transformation

New Public Management
Accrual accounting and budgeting
# Foreword

# Executive summary

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# Acknowledgements
The aspirations of citizens across the world are placing new demands on governments and the success of government leaders is increasingly being measured by the benefits they are creating for their constituents – citizens and communities; companies and industries. Such benefits demand top efficiency and performance, proper accountability and public trust, and a true focus on delivering better service and results.

As a result of this pressure, public sector reform is taking place, governments across the world are increasingly transforming management operations to make their decisions more effective and efficient, and their performance more transparent. The targeted result is greater value for their constituents.

Deloitte is a trusted business advisor to its global public sector clients and a source of best practice for world class government organisations. Every day across the world, Deloitte teams work with public organisations to help them build relationships of trust with their constituents and deliver exceptional benefits to their citizens.

In this challenge, public authority accounting systems at state, regional and local levels, as well as the financing structures and reporting of government-owned businesses represent a focal point of advisory services.

This document portrays some of the benefits for governments and government bodies of mastering the transformation from traditional to more advanced and transparent accounting methodologies. It provides insights into effective change management. It extracts essentials from practical experience and offers how-to coverage. It provides global public sector expertise in support of public authorities improving their services to their citizens and in their transformation objectives from cash-based to accrual accounting.
Over recent years, a trend towards reforming public sector (financial) management has emerged in many countries. Growing demands by citizens for improved government services at reduced levels of taxation have led to increasing burdens on government. One result of this has been that government bodies have been steadily moving toward a model of management more akin to the private sector than traditional public administration approaches.

A key part of this is a new approach to financial management, which has, at its core a focus on outputs and outcomes rather than inputs; and a new results-oriented approach to contract management whereby performance agreements are laid down in contracts between the different levels of public management, sometimes in combination with performance-based remuneration schemes. Additionally, deregulation; responsibility to decide how performance is realised to a large(r) extent delegated to tactical and operational management; and a shift from cash-based accounting to accrual accounting to obtain more meaningful financial information, where expenditures are laid against performance achievements rather than previously agreed budgets.

This reform of financial management is enabling governments to improve the transparency of budget and financial performance; decision-making, public spending effectiveness; and allocation of funds.

Around the globe, governments are engaging in transforming their financial management and lessons are being learned from the efforts. One of these is that reform of public sector financial management involves organisational change. The reform of public sector financial management is a long but rewarding journey, at the start of which numerous questions need to be considered.

What is our vision? To be defined and backed by all stakeholders and then translated into clear goals for the transformation.

How are we to achieve these goals? How do we manage such complex and extensive change? What resources do we need? What are the main obstacles we have to address? How can we make certain the changes are lasting?

When do we want to achieve our goals? What is a realistic timeframe for the transition process to take place given the choices to be made?

What will it cost? Is there sufficient commitment to allocate the required resources to the project from start to finish?

Over recent years, Deloitte has developed a vision and detailed practice for managing this transformation process. Through its global experience in working with the public sector, it has developed an approach that has helped many public sector executives successfully manage the transformation. Its essence is the design and deployment of activities to support organisational and employee transition.

Essential elements to this are numerous. They include empowerment by stakeholders understanding the benefits of accrual accounting processes; politicians’ and government officials’ values and behaviour aligned with the vision behind public sector management and accrual accounting, and an infrastructure and plan created that builds awareness of change goals, communicates progress towards their attainment and encourages collective ownership of the process and its outcomes. A training programme must be outlined to prepare people for the transformation process and future situation, the timeframe and resources must reflect the importance of the transformation.

An explicit plan and structure should be in place to ensure that each department can satisfactorily implement the changes. The organisation structure and reward of performance must be aligned to motivate new practices in support of new financial public sector management and increased transparency. And the approach to the specific requirements of the culture of the organisation or country concerned, should be tailored using proven methodology. This approach has been shown on numerous occasions to create lasting change and ensure the success of the implementation of accrual accounting. Accrual accounting is no end in itself but a tool for achieving greater value for taxpayers’ money.

This document presents Deloitte’s vision of ‘Mastering the Transformation’. It is illustrated with best practices and case lessons from countries taking a leading role in new public management.
Introduction

The subject of accrual accounting is under discussion across many constituencies and many states are at different stages of implementation.

1.1 New Public Management
Over recent years a trend of reforming public sector (financial) management has emerged in many countries. Growing demands by citizens for improved government services coupled with lower taxes have led to increasing expenditure burdens. As a result, governments have been steadily moving toward a model of management more akin to the private sector than traditional public administration approaches. A key part of this is a new approach to financial management, which has, at its core, the following elements:

- a focus on outputs and outcomes rather than inputs;
- performance agreements laid down in contract between the different levels of public management, often including performance-based remuneration components;
- performance responsibility to a greater extent delegated to tactical and operational management; and
- the shift from cash-based to accrual accounting to obtain more meaningful financial information, where expenditures are laid against performance targets rather than simply against previously agreed budgets.

The worldwide shift from cash-based accounting to accrual accounting and budgeting should be seen in this context of public (financial) management reform. Accrual accounting is a key instrument for achieving greater value for taxpayers’ money.

1.2 Objectives and benefits of accrual accounting
The worldwide trend from cash-based accounting to accrual accounting and budgeting (hereafter referred to as ‘accrual accounting’) is a key building block in progress towards the broader context of public sector financial management reform. What can it achieve?

Accrual accounting can contribute significantly to:

- improving decision-making to enhance efficiency and effectiveness of public spending through the creation of more accurate and accessible financial information;
- improving resource allocation due to a better insight into costs of policy and transparency of results.

Accrual accounting provides meaningful information both for accountability and decision-making. Financial information prepared on an accrual basis allows users:

- to make better balanced comparisons between alternative dispositions of resources;
- to better assess performance, financial position and cash flows of the entity;
- to better evaluate a government’s ongoing ability to finance its activities and to meet its liabilities and commitments;
- to gain clearer insight into how a government finances its activities;
- to better evaluate a government’s performance in terms of its service costs, efficiency and accomplishments; and
- to gain more understanding into how successfully a government is managing its resources.

To achieve these benefits a transformation of the financial management system is required.

Summary of the benefits of Resource Accounting and Budgeting as applied in the UK

For each department
- Better information on costs, assets and liabilities
- Management for the first time of working capital
- Focus on outputs and outcomes
- More financially aware Civil Service

For the management of central government
- More sophisticated strategic planning
- Support to modernising government
- Cash control at a higher level
- Better measurement of public expenditure
- Better decision taking on resource allocation
- Reduction of the perverse effects of annuality

For the management of the economy
- New macroeconomic aggregates
- Better asset information
- Better use of resources through capital charging

For Parliament
- More and better-focused information
- Links to departmental objectives
- Scope for better scrutiny of public spending

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1 How the Resource Accounting and Budgeting Project was Managed, Her Majesty’s Treasury, 2001.
1.3 Mastering the transformation
The realisation of these benefits requires a transformation of the financial management of the public sector that includes much more than simply implementing accrual accounting. This transformation takes place at several levels. At the highest level a vision on public management is needed, the decision made to implement instruments to support this vision and the conditions created for successful implementation. Generally referred to as the governmental level, it usually includes Parliament, Council of Ministers or Cabinet and the Treasury.

The next level is referred to as the organisational level and consists of individual organisations which have to implement the accrual accounting instrument. Successful implementation at this level is dependent upon both the effectiveness of the conditions created and specific measures taken. Processes at lower organisational levels follow similar patterns. The whole must be enveloped in a supportive atmosphere of consensus, guidance, encouragement and support.

1.4 Deloitte's vision
This paper presents Deloitte’s vision for the successful implementation of accrual accounting at governmental level. The vision is illustrated by international best practices and lessons learned, and by interviews with key public sector executives with hands-on experience. Thanks are due to them all for their valuable contributions.

Of the extensive available literature the IFAC study ‘Transition to the Accrual Basis of Accounting: Guidance for Governments and Government Entities’ and HM Treasury’s report ‘How the Resource Accounting and Budgeting Project was Managed’ proved valuable sources.

Chapter 2 discusses the framework for change enablement on which our model for mastering transformation is based as well as change enablement best practices. Chapter 3 discusses the most important issues regarding the transformation environment and organisation based on issues discussed in chapter 2. Chapter 4 casts a glance at the future.

Output-driven process management

Figure 1.1 Levels of decision making

Mastering the transformation is a complex interrelated mix of decisions, processes, checks and reinforcement exercises.
Change enablement is the creation of an environment in which the transformation process can most effectively be implemented. On the one hand it is the creation of consensus and support among all involved parties and on the other the removal of all physical and spiritual barriers to its implementation.

Accrual accounting in public management has an impact far beyond the finance function. It affects regular work practices across government from political decision-making to daily operations. Patient and determined guidance of this is essential to successful implementation.

The first requirement is for a comprehensive plan to support staff throughout the change process and to ensure that the transformation project is kept in balance with other organisation operations. This can strongly impact the pace and smoothness of the performance enhancement process.

This chapter looks at the approach to change. Section 2.1 looks at some primary obstacles to it. Section 2.2 reviews a change enablement framework. Section 2.3 suggests keys to lasting change.

2.1 Primary obstacles to successful change

**General obstacles for all transformation processes**

Many best practice studies of organisations undertaking change confirm that for change to be successfully implemented and improvement to be permanent, a number of critical factors need constant attention. If this is not done properly then major barriers can arise and cause transformation difficulties. According to Information Week, general obstacles to successful implementation include resistance to change, lack of executive commitment, and inadequate team skills. Figure 2.2 shows the main barriers with an estimate of their relative importance. This study focuses on the change element; methods for avoiding pitfalls are shown in the Change Enablement Framework on page 9.

Evidence suggests the benefits of the implementation of accrual accounting are long term and destined to grow.
Specific obstacles to public financial management reform

These principally relate to the political environment, and budgeting and accounting system. While implementing accrual accounting involves change, the realisation of future benefits of accrual accounting depends on what a government and its organisations do with the system once it is in operation. Accrual accounting increases the transparency of budget and financial performance and therefore impacts operating and reporting procedures of politicians and government officials. Accrual accounting does not only provide meaningful information for decision-making, but also makes officials less protected from public scrutiny and therefore more accountable for the efficiency and effectiveness of their government programmes.

If stakeholders are not able or willing to understand the objectives of change, and subsequently to accept the new business processes, roles and responsibilities, then risk of failure is present. It is therefore essential to invest time and effort in creating the shared vision among stakeholders and ensure there is the commitment, support and resources to successfully complete the transformation. A complicating factor here is the possible change in composition and thinking of a government due to elections. To assure ongoing long-term support for a reform initiative, it is essential that the need for change and the vision on the future are broadly shared among the various political parties, and especially the main opposition parties. Broad political consensus is essential.

Change of the budgeting and accounting system

To change the budgeting and accounting system from a cash basis to an accrual basis, several accounting issues need to be addressed, beginning with the definition of the accounting principles to be adopted - the basis for the valuation and allocation of assets and liabilities on the balance sheet, and revenues and costs on the profit and loss or expenditure account.

Decisions must be made, for instance, on what assets need accounting for and at what value, under what conditions liabilities must be accounted for and when and how are taxes, grants and subsidies allocated. Examples of typical accounting issues include definition of capital expenditure, valuation of assets, liabilities and provisions, capital charges, and consolidation issues. Each require clear cut definition and policy.

Current state of the art suggests adoption of accounting principles which are internationally accepted (IPSAS), or proven in use by one of the countries where the public sector has already successfully implemented accrual accounting. Extensive literature on the subject is available.

While the generally accepted accounting principles applied in the private sector can be used as a reference for the public sector, it should be remembered that circumstances are different between them. In the private sector the goal is to earn as much money as possible and operations are the means to reach that goal. In the public sector the goal is the operations themselves such as education of children or building roads, and money is dedicated to reaching these goals.

Figure 2.2: General obstacles to successful change (% respondents)
The obstacles to change are primarily of human character. Consensus is favourable to success.
2.2 Vision on change

Change Enablement may also be seen as the sum of activities supporting organisational and individual transition from the current situation to the desired future situation.

So far we have seen that various stakeholders are represented, all with their own interests and influence on decision-making processes. These different interests and opinions require a shared vision. This vision consists of clear objectives to achieve and as a result a necessity for implementing accrual accounting.

Change processes within organisations involve not only changes to the organisation, but also to individuals within it. This includes the psychological process every individual goes through in order to accept a new situation and is something that always happens, irrespective of the way the process is managed. This transition has its own pace independent of the pace of the organisational change, and it is as a result of a mismatch between organisational and employee change that problems often occur. Most obstacles shown in figure 2.2 are based on human factors:

- resistance to change (or lack of acceptance of the need for change);
- lack of executive commitment;
- unrealistic expectations;
- lack of cross-functional teams; and
- inadequate team and user skills.

In order to avoid or overcome these obstacles, a continuous focus on both organisational change and individual transitions is required. This can be visualised as follows (figure 2.3):

The systematic application of the eight best practices described has been shown to offer the smoothest transformation in implementation.
This approach allows the user to define the process to support organisational and individual transitions successfully from the current situation to the desired future situation. This requires not only a shared sense of urgency and need for change, based on a common understanding of the current situation, but also a clear and shared vision on the desired situation.

The realisation of the desired future situation takes place by taking into account the eight elements in the centre of the model in figure 2.3. Below we describe the organisational and individual paths towards the desired future situation.

Organisational Transition consists of the changes in structures, processes, systems and technologies required to implement successfully an integrated accrual accounting system. There are three distinct phases from current situation to desired future situation: Designing, Building and Implementing.

- **Designing**: The organisation must have a vision for the future – that is, it must understand what overarching purpose it should have and what the organisation should look like to best serve that purpose. Once the vision is clear, the vision must be broken down into specific goals and a strategy developed for achieving those goals. At the same time, the transformation project organisation is structured.

- **Building**: This covers creating an implementation plan to close the gap between the current situation and desired future situation by defining the major tasks and activities for the transition period, and determining the structures and management mechanisms necessary to accomplish those tasks. The link between organisational change and individual transition is made in the implementation plan.

- **Implementing**: This concerns the actual implementation of the reforms. Assessing and implementing desired changes, measuring results, and identifying required adjustments to the change plan. This is important as, triggered by the resistance to implementation, the organisation could deviate from its original intentions.

Individual transition refers to changes in behaviours, skills and attitudes of individual stakeholders (especially employees). These changes are just as important as the changes in organisational strategy and structure.

The behavioural side of change ultimately determines the success of the change effort. Individual transitions require unique planning and action to ensure their alignment with the organisational transition. There are three distinct phases in individual transitions: Ending, Exploring, and Beginning.

- **Ending** is the process of understanding the personal impact of change, letting go of the past. Fear of loss contributes to resistance to change. This is an obstacle as accrual accounting impacts the way politicians and officials in the government work and report to each other.

- **Exploring** is the process of overcoming anxiety and resistance, experimenting with changes and defining new roles. Chapter 3 presents ways to address these obstacles.

- **Beginning** is the process of adopting new values, attitudes and identities and seeing the tangible benefits of implemented changes. Lasting change can only be assured if this phase in individual transition is also appropriately addressed.

Organisational transitions are critical to an organisation’s change efforts, but without individual transitions, the likelihood of success of the organisation’s change effort is severely diminished. Managers and individual employees play a very different role in these transitions. Managers need to agree on their shared vision, formulate objectives for the change and make the step to new structures, processes, systems and technologies. Beyond this, they play a very important role in convincing the stakeholders (including employees) of the necessity of the changes. To achieve success in the final transition every individual employee is important.

Fast and cost effective routes to accrual accounting
2.3 **Keys to lasting change**

Change Enablement allows a customised project approach meeting a government’s unique organisational situation. A journey of organisational change and individual transition from current to future situation supported by eight central elements creates lasting change and ensures the success of a project. If the current or future situation is blurry, or one of the other change elements is absent, they can be major causes of project failure. Experience in providing change enablement support has led to the conclusion that a handful of best practices account for the success of most change efforts. These best practices are grouped around the different elements of the change enablement framework and tailored to the implementation of accrual accounting.

![Table of keys to lasting change](image)

*Figure 2.4: Keys to lasting change*

This simplistic overview of best practice impact highlights the effects of their absence. All are necessary.
**Elements of Change Enablement Framework** | **Best Practices**
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**Need for Change** | Effective financial management and top support in decision making processes need to be clearly understood by all stakeholders.

**Shared Vision** | The vision on future public management needs to be clear and compelling and shared by all stakeholders.

**Stimulating Leadership** | Politicians’ and government officials’ values and behaviour should be aligned with the vision behind public management and accrual accounting (walk the talk); They should possess the authority, know-how and skills to drive the change process to completion and accept the responsibility for doing so.

**Effective Communication** | An infrastructure and plan needs to be in place that builds awareness of change goals, communicates progress towards attainment of these goals and encourages collective ownership of the change process and outcomes.

**Individual & Team Capacity** | Implementing accrual accounting affects the way the whole government operates. Training programmes should be in place to prepare people for the transformation process and the future situation. To create this new future the best people from all relevant functions and level of the government should be assigned to the project.

**Change Architecture** | The scope, timeframe and available resources should be aligned with the importance of the project. An explicit plan and structure should be in place to ensure that each government department can achieve the changes with its given resources.

**Performance Measurement** | Organisational design and the measurement and reward of performance must be aligned to drive new behaviours in support of new public management and increasing transparency.

**Process Management** | The ways in which change is managed and people are supported will be different in every country or organisation. Reactions to change will vary. Tailor the approach to the specific requirements of the culture of your organisation or country.

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**Figure 2.5: Best Practices**

Heading 3.2 describes these eight Best Practices in more detail.
Towards a framework for implementing accrual accounting

In the previous chapter we discussed several issues with regard to implementing accrual accounting. In Section 2.1 we dealt with barriers and enablers which could hamper or facilitate the implementation of accrual accounting at governmental organisations. In Section 2.2 we described an enablement framework for facilitating major organisational changes.

In this chapter, we present best practices for implementing accrual accounting related to keys to lasting change described in Section 2.3. Before further detailing these Best Practices, we describe in Section 3.1 the environment of change processes at central governmental organisations. Which stakeholders are present in such an environment? What are their interests? Do these interests enhance or conflict with each other?

3.1 Transformation environment
Stakeholder assessment and defining a short term communication strategy are essential steps in the early stages of a significant change project. Stakeholder assessment describes the positions of the various stakeholder groups and establishes the degree of impact the accrual accounting system will have on them, especially management and employees, both as groups and individuals. This, in turn, defines the short term communication strategy, which details specific audiences for communication and how to communicate with them. The underlying assumption is that the greater the level of a person’s active involvement in the change process, the greater the degree of change required of them. So audiences are differentiated by the degree of change required of them. They are defined as follows:

**Awareness:** Those who need only to be aware of the changes. It is beneficial but not absolutely necessary that they actively support the changes, but it is important that they know what is happening. These are the people who are less directly affected by the changes and see them as something outside their realm of influence and responsibility.

**Initiation**
Changes within government organisations occur in a very specific environment. Various stakeholders are present who may initiate change enablement processes and influence decision-making processes. We identify the following stakeholders for the introduction of accrual accounting (see Figure 1.1):

- Parliament (representing the citizens);
- Council of Ministers;
- Treasury;
- Ministries and governmental organisations.

Implementation of accrual accounting can be triggered by each of the stakeholders, depending on their influence. Sometimes an incident or a financial crisis will create a sense of urgency for reform. In other cases governments may implement accrual accounting as part of a drive for a general improvement of their finance function.

Citizens need to be assured that their taxes are spent effectively and efficiently. They demand insight in the way public budgets are allocated and to which results those expenditures lead. Accrual accounting is extremely effective when financial reporting must provide information useful in precisely evaluating the government’s performance in terms of service costs, efficiency and accomplishments. It can assist users by providing better and more accessible information for decision making and accountability. Members of Parliament, representing citizens, have a comparable interest. They want to be assured public money is spent usefully and according to agreed plans. Accrual accounting can help in creating this transparency.

The interest of ministers and top executives is more double-edged. Focus on outputs and accrual accounting enhances the transparency of information. This can enable a minister to substantiate a budget request for a certain output, or to successfully negotiate a decrease of outputs. It might also be easier to convince Parliament of the necessity for an investment-based than cash-based system. On the other hand, increased transparency will make ministers more accountable, since ineffective or inefficient implementation of policy will be more visible. Extensive training and a fair and effective performance management system are key to convince this group of the benefits of the new system.
3.2 **Eight best practices**

Both the transformation environment and elements of Change Enablement as described in chapter two, have implications for the transformation approach. Our experience in providing change enablement support has led us to the conclusion that a few best practices are critical for the implementation of accrual accounting and budgeting. These have been grouped around the elements of the Change Enablement Framework and are further detailed below.

### 3.2.1 Need for change

Resistance to change is one of the largest obstacles to a successful implementation of new public management and a more business-like approach. The most effective way to overcome this obstacle is to create a shared need for change.

In the various countries that have already transformed their financial management the decision to transform was primarily based on the fact that there was a need to:

- increase transparency of budget and financial performance;
- improve decision-making;
- improve efficiency and effectiveness of public spending;
- improve fund allocation to consumer and capital expenditure.

In some cases, a financial incident might expose the shortcomings of the current system. In other cases a financial crisis might create a sense of urgency and trigger the need for change.

It is essential to make a thorough assessment of the shortcomings of the current situation and to obtain a good understanding of the elements of financial management which need to be transformed. If this assessment is not properly made there is a real risk that the transformation process will not focus on all the required areas for improvement. This assessment, which forms the base for the transformation process, might cover the following issues:

- lack of relevant, reliable and timely (non) financial information for decision makers;
- focus on annualised inputs and expenditures leading to suboptimal allocations;
- over-regulation leading to inefficiencies and a lack of accountability for results;
- organisational structure that is not logically aligned with areas of responsibility and services to be provided to achieve objectives.

Transforming to new public management involves considerable change of the way politicians and officials in the government work and report to each other. It requires a change of mindset. In order to realise this change, there should be agreement at the governmental level as to the necessity of implementing new public management and accrual accounting as a supporting tool. This acknowledged need for change needs to be broadly shared among stakeholders, including the majority of Parliament, the Council of Ministers and top executives in the government.

Adequate support and commitment is required for successful implementation. It is essential to invest sufficient time and efforts to acquire this commitment. This might require significant efforts in creating awareness, debating, convincing, and investment in education and training.

**Shortcomings cash accounting**

The 1994 Green Paper in the UK commented “With cash accounting, spending on what is used over many years is recorded only when the money is spent. No subsequent account is taken of whether the asset is still in use, has reached the end of its useful life, or has been sold.”

In a 1995 report, the Comptroller and Auditor General agreed “Cash-based accounts lack any framework for accounting for assets and liabilities: once an asset is acquired, it effectively disappears from the accounts.”

### 3.2.2 Shared vision

The next step is to create a shared vision on the direction of the change: the future situation. The vision on the future situation needs to be clear and compelling. In the future situation the identified shortcomings of the current situation need to be addressed.

The most critical questions that must be asked in the development of the shared vision are:

- What do we want to achieve? How does government want to manage and how will it be measured if this desired situation is realised?
- How are we going to achieve our goal? What organisational structures, processes and supporting methods and tools are required? This might include accrual accounting and budgeting, programme budgeting, performance and risk management.

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• When do we want to achieve our goal? What is a realistic timeframe for the huge transition process to take place and will the implementation be phased or not?
• What will it cost? Is there sufficient commitment to allocate the required resources to the transformation from start to completion?

When the vision is clear and shared by all stakeholders, a feasibility study including a business case, needs to be built to gain further insight in the transformation process and the future situation. A business case summarises the costs and benefits of the transition to determine if the benefits outweigh the costs. In addition to the financial benefits, the intangible benefits should naturally also be taken into account. It is essential that the business case be built by a multidisciplinary team consisting of experts in a broad range of disciplines, including finance, ICT, change management, processes, auditing, HR, performance management and legal issues in order to be able to present a complete picture. Information from countries where accrual accounting has already been successfully implemented can be very useful in building such a business case.

As part of the business case, drivers and barriers must be identified. A study of these will outline the most important factors that will hinder or facilitate transition. Examples of drivers include strong leadership, pride in improved operations, sharing knowledge and experiences and enhanced career opportunities.

The study of barriers should include their quantification. It is important to distinguish between issues that (just) increase the complexity of implementation, and the serious so-called ‘show-stoppers’. If show-stoppers such as lack of commitment, lack of resources or lack of shared vision are identified, the continuation of the transformation is at risk; in the case of unresolved show-stoppers, a decision not to proceed should be considered. An assessment can be made if and to what extent such implementation barriers are applicable and what strategies are feasible to overcome them. The outcome of this assessment should form part of the business case.

The decision to implement accrual accounting should not be taken lightly. From the decision to proceed, a transformation project like this can take anywhere from 5 to 10 years, involve large-scale change and be highly demanding. The special arena (split governmental/organisational level) demands a strong political mandate in order to guarantee a successful implementation and a long term acceptance after the change, especially since the political forces might shift during implementation due to elections. Only with a strong need for change and a broadly shared commitment, will the implementation be successful.

Business case considerations

In an occasional paper ‘The Modernization of Government Accounting in France: the current situation, the issues, the outlook’ the IFAC describes considerations in France of a dual system. While extolling accrual accounting, it also points out the cash-based system is robust, immediately accessible and adapted to reporting in real time. Accrual accounting makes it possible to develop financial information which enables a more reliable assessment of the government’s asset base and financial position. It enables managers to develop more reliable assessments of assets and actual costs of service delivery. The solution of maintaining the current system for the budget while changing government accounting, is a progressive and realistic approach consistent with orderly development and implementation.

Phased implementation

The answer to the question what a government wants to achieve in new financial management will differ from country to country. A significant amount of literature is available on this topic. In this report we go into more detail on the questions “How are we going to achieve our goal” and “When do we want to achieve our goal” that should be asked during the development of the shared vision. These two questions in turn trigger the query as to the way that should be chosen in achieving the goals as set out in the vision on the future situation. In other words, the question arises whether the government wants to implement new public management with a ‘big bang’ approach or a more phased implementation approach.

Many countries have chosen phased implementation of new public management. This can be done in different ways.
• First implement an output-focused budget and then accrual accounting and budgeting.
• Start with implementing accrual accounting and introduce accrual budgeting at a later stage.
• Use a number of pilots before starting an integral roll-out.
• Make the shift from cash accounting to accrual accounting in a number of steps.

Given the size and the complexity of a transformation of public sector financial management on the national level, a phased implementation is strongly recommended. Different forms of phasing can be applied, also in combination.

Some countries implement an output and outcome focus in the budget cycle first. This involves identification of products and services provided by the government to achieve the policy goals. This activity contributes significantly to the improvement of management information and is also a relevant step towards accrual accounting.
Wide experience

Sweden introduced accrual accounting in 1993, with only minor changes to the budget system. No organisational changes were needed, as the Swedish system of having a large number of agencies responsible for the execution of policies was well suited for the implementation of accruals and management by results. As a result the implementation could be dealt with on the bureaucratic level and was realised in a period of 2-3 years. A disadvantage of this approach was the need for analyses and reconciliations between the budget and the accounts which were prepared on different bases. Flexibility in spending over fiscal years was introduced before accrual accounting. This spending flexibility meant that organisations could carry over unused appropriations to the following year and also make possible spending a portion of the following year’s budget in advance.

The UK produced its first resource (accrual) accounts for individual departments in 1999-00 and the first request for parliamentary approval of spending on a resource basis for 2001-02. A staged approach for the preparation of consolidated financial accounts for the whole of the public sector is planned. This process will include consolidation of unaudited central government accounts using information from the national accounts for 2001-02, consolidation of central government accounts using generally accepted accounting principles for 2003-04 and whole of government accounts for 2005-06.

In The Netherlands the decision was made first for agencies to change to accrual accounting since this type of (business-like) organisation would benefit the most from accrual accounting. For the ministries the implementation of accrual accounting would be delayed.

South Africa adopted a phased approach in four steps from a cash basis to a modified cash basis to a modified accrual basis to an accrual basis.

Constraints and leadership

France experienced five constraints in implementing accrual accounting. The specific nature of French government operations, notably the scope for government intervention, transfer operations, sovereign revenues, off-balance sheet items, financial statements. The wide range of doctrinal sources such as the General Chart of Accounts (PCG), and charts of accounts for Credit Institutions (PCEC), IAS, IFRS, IFAC were sometimes contradictory resulting in the problem of choosing between several options. An unequal level of interest for deciders meant that they did not immediately perceive the benefits of the transparency, bonds between budgeting and general accounting. There was a slow pace in setting up adapted information systems. And the struggle of accounting teams when confronted with advice and recommendations from all sides.

Initiatives and actions to overcome these constraints include:

- Close attention from the level of the Director General of Government Accounting creating alliances and shaking up the ‘financial bureaucracy.’ He creates a dedicated department, which is responsible for the standards design, exploration of the information systems, the accounting function’s organisation, accounting quality, promotion and training.

- Adopting a pragmatic approach i.e. not favouring an overly doctrinal approach that hinders implementation but rather encouraging the production of useful information for the various players. Thirteen standards were elaborated in committee on an ad hoc basis, validated by the CNC (National Accounting Committee) and approved by decree.

- By adopting a modular approach, i.e. not considering the French government as a whole, but rather completing the implementation step by step with achievable goals. Implementation of accrual accounting as set out in the new accounting law (LOLF) will be in two stages:

3.2.3 Stimulating leadership

As discussed in Section 3.1 there are various levels of decision-making: Parliament, Council of Ministers (Treasury), the Programme Director and project leaders at the level of ministries and governmental organisations.

In order to achieve stimulating leadership, politicians’ and government officials’ values and behaviour should be aligned with the vision for public sector management and accrual accounting (practise what you preach). If the objective of the transformation is to create a culture of transparency and result-driven organisations, it is important that the transformation be organised on the same principles. Implementing accrual accounting by using a very direct approach with very tight regulations can be contradictory to the objective of the transformation as people may still not know what it means to work in a transparent, results-driven way. Therefore, leaders should use an open and results-driven approach in their project management.

ESU (Ekonomistyrningsverket), 2001

Footnote: Accrual accounting in Swedish central government
the 2006 stage, i.e. the implementation of LOLF basic essentials in the existing information systems; implementation of new information systems tailored to all requirements of LOLF (ACCORD III).

- By constantly demonstrating what the French government can achieve: by multiplying the areas of excellence where progress is visible and which may have a training role.

- Relying on the profession’s best practices - the public accountants join the Accounting Academy of Science, set up by the President of the Order of Chartered Accountants.

Accrual accounting - as part of new public management - will impact the way a government accounts for its (public) budget spending and enhance the quality of financial information available to Parliament. So Parliament should be one of the driving forces behind the transformation project. At this level a (small group of) leader(s) advocating accrual accounting and stimulating leaders at the ministerial level is crucial. In practice strong advocacy from Parliament appears to be a very significant success factor. Parliament should show its commitment, not only by defining a compelling future situation and allocating sufficient resources for the transformation, but also by practising principles of new public management in daily practice; focusing on outputs and costs instead of inputs and regulations.

Double budget information
The following best practices are good examples of initiatives that help politicians in their individual transition to gradually explore and accept the new presentation of information, while they can still dispose of the information presented in a way they were used to.

The Hamburg State and City Government plans to implement accrual accounting as of 2006. Two systems are to be used in the first two years. The first one based on the old system (cash-based) and the new one based on accrual accounting. This will allow politicians and professional observers to assess the difference in information provided. From 2008 accrual accounting should impact the public budget.

In Italy political resistance to change has proven to be the biggest hurdle. Politicians focus on decisions based on ‘expenses’ rather than ‘costs’ or ‘outcomes’ on an economic basis to highlight the efficiency of resources employed. This resistance has been countered by an extensive political education process to convince parliamentarians of the benefits of the new approach. Both the budget and general accounting system operate on a modified cash basis of accounting.

However, a second budget format is produced using ‘economic accounting’ to provide comparable budgetary information on an accrual or cost accounting basis. Presently, this second budget format only supplements the information provided in the current budget system rather than replacing it. However, the eventual aim is that the ‘economic’ (accrual-based) budget will replace the ‘financial’ (cash-based) budget.

Implementation of accrual accounting at the governmental level is a demanding challenge. It is a long term, highly visible process that changes the way a government is managed. The transformation affects many influential stakeholders. This requires a well-respected leader at all decision levels with the authority, know-how and skills to drive the change process to completion and accept the responsibility for doing so.

It is essential to appoint a senior executive to supervise the transformation as a whole – the Programme Director. This person acts as a linkpin between the Council and the project managers of the separate ministries. He or she has a steering and coordinating role for all ministries and is accountable to the government. In line with this the Programme Director needs a strong (political) mandate from the Council of Ministers to be able to take fundamental, country-wide decisions which will impact all ministries.

Programme Director
In Sweden the Financial Management Authority (ESV) is a government agency responsible for financial management and the development of generally accepted accounting principles in Swedish central government. This agency has the authority to implement changes and operate as the Programme Director for implementation. It installed a form of account management for the agencies by appointing within ESV fixed contact persons per agency available to provide information and training and act as a sounding board for the agencies.

Towards a framework for implementing accrual accounting

Interests of the citizen


3.2.4 Effective communication

In order to achieve effective communication a communication infrastructure and plan needs to be in place that builds awareness of change goals, communicates progress towards attainment of these goals and encourages collective ownership of the change process and outcomes. Regarding the communication architecture the following steps should be taken.

Determine a communication strategy in the early stages of the transformation: When a feasibility study is being undertaken, people will begin to hear about the potential transformation and want to know what is going on. Consideration should be given to how much should be told to stakeholders and when or whether an open or cautious communication strategy should be adopted. With an open communication strategy, one communicates up-front with stakeholders that implementation of accrual accounting is under review; a cautious approach involves delaying any communication until the feasibility study has been completed and a decision has been taken.

The choice of communication strategy will depend on local political traditions and customs. We notice that in designing a communication strategy the barriers and driving forces relating to human factors are of major importance. Given the fact that a broad consensus and shared vision is a key success factor for successful implementation, open communication - if feasible given the culture - is generally preferable.

Internal communication

In the UK\(^4\), although a very large amount of useful advice and guidance was issued by the Treasury during the course of the project, communication from the Treasury to departments and within departments did not always succeed in reaching the right audiences. Even though normal channels were used, and special committees and publications were created to supplement them, the Treasury was not aware that some of the messages sent out were not always reaching their intended destinations within departments. With hindsight, it might have been possible to have done more to check that messages were in all cases getting through to, and within, departments and, in doing so, help to achieve the necessary cultural change.

- Share experiences during implementation: The implementation process will be similar in the individual organisations, though there might be differences in the pace of implementation. The Programme Director will have to build a structure for the organisation's project managers to share their experiences and learn from each other. The knowledge and experience sharing processes can be facilitated by an intranet application.

- Provide feedback to stakeholders: periodically Parliament needs to be informed about the progress of the transformation, the costs involved and the results achieved. This requires a transparent reporting format which can easily be understood.

3.2.5 Individual and team capacity

Implementing accrual accounting as part of a broader initiative of new public management will affect the way the whole government operates.

- To make this transformation really work significant effort has to be invested in training and education. This can be done in various forms from newsletters, presentations, awareness workshops, and traditional training in class to forms of e-learning. For each of the stakeholders a tailor-made training and education programme should be in place. The main challenge is not just to teach the technicalities of the new system, but most of all to teach the objectives behind it to avoid traditional input-focused issues remaining under discussion.

Training

In the IFAC study 14\(^5\), skills assessment and training include the following lessons from a report on behalf of the Treasury Board of Canada. They found it was almost impossible to overestimate the amount of training required. They recommended anticipating staff turnover during implementation, since this increases the burden on training and can delay project implementation. They found training is best when using real data because it is more meaningful to personnel being trained and that an integrated training approach which allows participants from different work areas to discuss what they do and how they interact was most effective.

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\(^4\) How the Resource Accounting and Budgeting Project was Managed, Her Majesty's Treasury, 2001.

\(^5\) Transition to the accrual basis of accounting. Guidance for governments and government entities, (second edition) IFAC Public Sector Committee, 2003,
• Define the roles carefully at all levels and ensure job descriptions are suitably altered to reflect the new roles after the implementation of accrual accounting. The people responsible at management level must have management experience and a good theoretical understanding of their relevant areas. Hiring should be based solely on merit.

• Individual and team capacity should not only be built for the desired future situation but also for the transformation process itself. To create this new future the best people must be assigned to the transformation. This is always a difficult decision. Individual organisations do not want to lose their best people in daily operations to a long term project. The people themselves might be afraid that their careers will slow down if they are not visible in their daily environment. This is a serious risk in a project ideally managed by a pro-active human resources policy in which the career opportunities for people in the project are shown to be secured.

• It is essential that the transformation be implemented from the early stages on by a balanced multidisciplinary team consisting of experts in a broad range of disciplines. They should include finance, ICT, change management, processes, auditing, HR, (performance) management and legal. The exact composition will depend on the exact definition of the future situation. Team members should work together as a single integrated team striving for the same objective, instead of individual disciplines trying to progress the interests of their own discipline. If the team is unbalanced in a way that is dominated by one of the disciplines, there will be a risk of skewed goals and domination of group thinking by one of the disciplines. This may ultimately lead to the future situation not being (fully) realised.

• The team will generally consist of a mix of internal and external team members. It is important that a substantial part of the positions in the team are filled by civil servants. This is essential to create a sense of ownership for the outcome of the transformation. External team members can bring expertise to the table in those fields in which insufficient expertise is available in the government. They can also bring experience with similar transformation projects and can fill positions for which the capacity of government staff is not sufficient. External consultants can give objective advice and provide independent quality assurance.

• Active involvement of all levels and functions within the government is a prerequisite for the success of the transformation process. Individuals and teams should be prepared and rewarded for their role in the implementation process and in the operational stage. Due to the long timeframe for such implementation projects, the people closely involved in the project require attention and incentives in order to keep them motivated. In addition it is very important for the motivation of team members that milestones achieved in the project are celebrated and individual employees rewarded for their efforts.

Human resources
The Portuguese Institute of Employment and Professional Training presented the following attention points:

• Ensure a training plan is produced. This training should address, in order of importance: What is the organisational structure? What are the processes? How to use information systems to support them?
• Hire the right people for the right jobs.
• A third party auditing/consulting firm should be hired to provide independent advice on account structures etc, provide independent quality assurance as well as to advise on implementation.
• Do not simply appoint managers in departments and hope all will go well. Proper hiring and training must be conducted at all levels, and especially at the intermediate manager level.
• Do not rely on the goodwill of people to devote time to the project. Ensure that key people have time officially dedicated to the project, including taking some people offline from their usual duties in order to ensure the proper level of attention is given to the project.

3.2.6 Change architecture
The scope, timeframe and available resources should be consistent with the importance of the transformation. An explicit plan and structure should be in place to ensure that each government department can achieve the changes with its given resources. In connection with the change architecture the following should be considered:

• Autonomous governmental organisations: The decision should be made to what extent governmental organisations involved should be free to make their own choices. The decision to be made will vary by country and depend on the way the government is organised. Due to the importance of a shared vision it is imperative that all organisations achieve the same objectives. There can be freedom of choice, however, on the issue how to
achieve these objectives; in that case the organisations are free to choose their own tools, such as ICT. The decision on the level of autonomy of governmental organisations is important for the choice of project structure and leadership, as a different set of skills and experience is needed.

- Set standards for the transformation: The implementation of accrual accounting at the organisational level will follow a certain pattern similar for all organisations. In order to prevent these organisations all reinventing the wheel at the same time a number of generic tools should be prepared. This should be a joint effort by the governmental and organisational levels, initiated by the Programme Director. They may include standard implementation plans, describing the required phases and steps, deliverables, the timeframe and project structure; mapping of financial processes, reflecting the changes in them to be made as a result of the introduction of accrual accounting, with a reference to the relevant legal and regulatory requirements; design of a financial organisational model, including segregation of functions, processes, and structure; identification of financial information requirements for accrual accounting; standard formats could be drafted for internal management information, but also for reporting to the Treasury; standard formats for budget and annual reports; standard accounting principles and chart of accounts, training programmes for all levels focused on skills, knowledge and attitudes; and material for creation of awareness and commitment, such as presentations and workshops. This would represent a full spectrum of capabilities.

Depending upon the autonomy of the individual organisations these tools can be offered for use on a voluntary or obligatory basis.

**Freedom of choice**

Different countries made different choices as to the autonomy of individual organisations involved:

In Sweden the government agency responsible for financial management distributes and supports a commercial accounting system, which the agencies are recommended to use. However, if an agency wants to use another system, it can usually buy any system offered on the open market.

In the UK6 decentralised decision-making on systems by departments was seen as essential for the successful implementation of the project, in order to cater fully for individual departments’ own circumstances and needs. This meant that the project depended on the ability of those systems to deliver the necessary information. Departments made assertions about the quality of existing systems and their ability to deliver change.

In retrospect, these assertions were not always justified, and in some departments the levels of skill and knowledge were insufficient to carry through the change process. More rigorous monitoring of departments’ systems would have meant the Treasury was more aware of deficiencies in the systems. This would have been picked up by the risk analysis approach and Office of Government Commerce (OGC) gateway methods are now being used. At that time these were not available.

With hindsight, it might have been helpful to have developed a minimum specification that all departments should have been required to apply when procuring a new system, or to have had a more limited number of packages to ensure the benefits of collaboration.

- Build a knowledge and quality structure: Implementing accrual accounting involves many different knowledge areas, ranging from specific financial knowledge to ICT, risk management, change, human resources and legal. It is therefore essential that this tremendous amount of knowledge be easily accessible to everyone involved. Advisory committees can be considered to provide knowledge and expertise.

A board of experts can act as a sounding board for key players when validating their ideas with recognised specialists in relevant aspects of the transformation.

A knowledge centre can support transformation team members with knowledge on every aspect of the implementation such as finance, IT, organisation/HR, process design and change enablement.

The knowledge centre collects best practices from all departments and from appropriate foreign countries and makes this information available. It can also be made responsible for training and the Helpdesk function.

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The services and products of the knowledge centre might include:

- evaluation of laws and regulations on information aspects;
- access to experiences of departments with the selection and implementation of EDP systems;
- insight in new developments in the field of information systems and information dissemination for management;
- acting as intermediate between suppliers of EDP systems and the departments, in particular for aspects beyond the capabilities of one supplier or department;
- facilitation of interdepartmental meetings with suppliers.

Dos and don’ts in change architecture

The Portuguese Institute of Employment and Professional Training presented the following attention points:

- Understand clearly the financial organisational model.
- Understand clearly the segregation of functions, processes, structure, systems, etc. The system must reliably represent the organisation (in terms of a true and fair representation of the economic nature of the organisation and its transactions).
- Define the information and document flows carefully to avoid bottlenecks.
- Ensure an accurate and comprehensive Operations and Procedures Manual is produced to clearly define the proper processes (through process mapping) with reference also to the legal and regulatory requirements.
- Do not set too ambitious timeframes for the implementation and do not succumb to political pressure to do so.
- Do not underestimate the size of the job and do not commit to specific results too soon. For example, the institute’s inventory of assets took three years even though it originally promised to complete the job within 12 months.
- Do not bow to political pressure. The consequences of doing so are far worse than remaining politically aloof.
- Ensure there is strong central coordination of the implementation, including a project office or a separate agency.

3.2.7 Performance measurement

Organisational design and the measurement and reward of performance must be aligned to drive new behaviour patterns in support of new financial public management and increasing transparency. This can be applied not only to the desired future situation but also to the transformation project. If the desired future situation includes a focus on outputs and outcomes and deregulation, then an individual manager should be allowed to make his own choices how to realise the agreed objectives within the agreed budget. The performance measurement system should be designed to measure the effectiveness and efficiency of the choices he made and their implementation.

The trigger points

In order to ensure that the final key stages of introducing resource accounting and budgeting (RAB) and resource-based supply in the UK were successfully completed, the Treasury introduced formal monitoring and assessment of departments’ progress towards full RAB implementation. This involved the development of a series of ‘trigger points’ against which progress in implementing RAB would be monitored and assessed, and which would allow sufficient time to resolve any problems emerging.

The trigger point strategy was effective in a number of respects:

- it provided a clear framework for assessing departments’ progress in implementing RAB at key stages, and meant rigorous progress checks – both for monitoring and in order to maintain the credibility of the project;
- it signaled clearly that RAB was going to happen preventing complacency, and put pressure on departments to deliver at each key stage of the process or be ‘named and shamed’;
- it provided reassurance to Parliament that departments’ progress was being properly supervised and scrutinised against tough criteria;
- it provided a framework for departments to benefit from National Audit Office input into the implementation process; and
- it provided a vehicle for meeting Parliament’s concerns about, and securing Parliamentary approval for, what has been described as the most important overhaul of financial management in Whitehall since the Gladstonian reforms of the 19th century.

The design of a new performance measurement system should be an integral part of the transformation. It should reward behaviour that fits the desired situation and discourage behaviour that was an undesirable part of the old situation.

7 How the Resource Accounting and Budgeting Project wasManaged, Her Majesty’s Treasury, 2001.
By adopting a new measurement system management shows that leadership of the government really accepts the future situation and is willing to be measured in line with its objectives.

**Performance based remuneration**

Italy is in the initial steps of the process of developing appropriate benchmarks. Negotiating the expected results and Key Performance indicators (KPIs) for performance measurement with senior managers has proven one of the most difficult parts of the whole process (15% of managers’ salaries are results-based). The process that has been adopted involves a review every three months of objectives, goals and expectations. A budget programme document has been developed for each programme in which quantitative and qualitative KPIs are established.

A performance-based remuneration schedule can support the implementation of output-focused management significantly. This requires a meticulous process of target setting and evaluation of achievements.

Performance measurement should be applied to any transformation project. Transformation requires a significant investment of resources. Because it is important to put a system in place to measure whether foreseen benefits are realised in the business case the costs and benefits are analysed. This requires that objectives be defined in a measurable way. If for instance one of the objectives would be to increase efficiency by a certain percentage, efficiency should be measured in the current situation and the change in the efficiency should be monitored in the course of the transformation. Performance management and human resources should be aligned with the new standards according to the new public financial management. Openness and transparency on actual performance should be rewarded and stimulated. Performance measurement should be part of the management development programme and based on the results of the project under managements’ responsibility.

**3.2.8 Process management**

In order for the transition process to be successful, effective process management should be in place. The way in which change is managed and people are supported is different in every country and organisation. Responses to change also vary. The approach to the specific requirements of the culture of the organisation or country will therefore differ. The aspect of culture is of major importance in order to achieve successful change in a complex transformation environment. Cultural barriers, for example, mean a government mandate will not automatically ensure a willingness in the various ministries to implement accrual accounting. Each ministry has its own culture. Culture should therefore be part of process management.

Furthermore process management involves quality assurance and risk management. It helps key players identify, monitor and analyse risks and create guidelines and procedures how to deal with them. Quality assurance assists key players in assuring the quality of deliverables and project control.

Process management is the responsibility of all players involved. To assure the overall quality of a transformation project. Quality assurance and risk management should also be assigned to a central team at the political level. This central team can also assist the Programme Director and project leaders at the ministries and governmental organisations to improve the quality of their process management.

**Implementation plan**

In IFAC study nr. 14 in an attachment to chapter 2 a generic implementation plan is presented. Reference is made to a number of websites where examples of implementation can be found. In order to facilitate process management it is strongly recommended to adopt a proven methodology involving the following:

- Help project managers see the big picture;
- Arm project managers with a proven approach and provide a common language;
- Accelerate work and enhance quality;
- Include deliverable templates and hand-picked samples;
- Provide a consistent approach and best practices;
- Incorporate Quality and Risk Management, making it easier in turn to improve quality and reduce risks to project deliverables;
- A system to manage the programme as a whole as well as individual projects.

Professional preparation and planning have been shown on numerous occasions to be the keys to successful implementation.

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The trend towards the implementation of accrual accounting has long been visible in the private sector across the western world. And over more recent time there has also been a distinct movement towards accrual accounting in the public sector. Australia, Canada, Finland, Iceland, New Zealand, Sweden, the UK and the US have already introduced it. Countries at an advanced stage of investigating its introduction include Belgium, Denmark, France, Germany, the Netherlands, Norway and Portugal. Various international institutions such as NATO and the EU are also well advanced in progressing its implementation. The primary conclusion suggests that accrual accounting will shortly achieve the status of standard in the public sector.

The evidence from those taking and having taken the step towards accrual accounting is clear. Handling the transformation challenge is becoming easier and less stressful, results are more clearly showing the cost-benefit picture favours the benefits, the benefits are becoming easier to realise, and their management is becoming less complex. It is enhancing the efficiency and effectiveness of public spending. It is providing better balanced comparisons between alternative dispositions of resources. It is allowing better evaluation of a government’s ability to finance its activities and meet its liabilities. It is more clearly profiling successful government performance.

But the benefits of accrual accounting are not to be achieved without investment. Practice has shown that these long term gains and betterment are available to those willing to invest the effort and accept the complexities of organisational change for a short time. Experience has also shown that the way in which the transformation process is planned, prepared, managed and polished has a clear influence on the ease of introduction of accrual accounting and avoidance of subsequent operational difficulties. With the process generally a complex one, the wisdom of entering into it with a team of competent and experienced professional advisers is undisputed.
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