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## Accounting Change and Institutional Capacity: The Case of a Provincial Government in Indonesia

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### Abstract

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### Keywords

Accrual accounting, accountability, performance improvement, Indonesian local government



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## Abstract

This study examines a reporting system change of a provincial government in Indonesia. The study also draws attention to the institutional capacity of the provincial administration and implementation problems it encountered in adopting an accrual accounting system. Following the work of Lapsley and Pallot (2000), this study uses economic and institutional perspectives in conceptualising how an accounting change has been undertaken. The study shows that from an economic based perspective, the adoption of the new reporting system was stimulated by the wish to improve government organisations' performance in the country. It is also found that the change of the reporting system was not accompanied by the separation of the roles of elected local officials (i.e. the governor) and local parliamentary members as politicians and decision-makers in the allocation of funding and budget formulation in the provincial government. This situation undermines the instrumental roles of accounting for decision making. Moreover, drawing upon institutional theory, the adoption of the new reporting system at provincial level in the country is indicated by the presence of coercive pressure as local administrations in Indonesia are required to comply with rules imposed by the central government. However, based on the experience of a provincial government in implementing the new accounting system, the policy to adopt the new accounting regime fails to recognise a low level of institutional capacity of local administrations. As a consequence, the institutionalisation of the new accounting system has yet to bring intended outcomes. In this vein, the role of accounting as a political tool for controlling people overshadows its roles for efficiency and performance improvement. As the study demonstrates the use of mixed methodological perspectives (i.e. economic and institutional theories) is useful to fully capture and understand the dynamic process of accounting change in a specific setting.

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**JEL Classification:** M40, M41, H70.

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## Introduction

The debate about the implementation of business-like accounting systems for government entities has existed since the 1970s. Earlier studies in this area (e.g. Ingram 1984; Zimmerman 1977) employed an economic based theory in providing explanation for accounting innovations in the public sector. As Zimmerman (1977) suggested, economic factors influence the practice of government financial reporting in the United States. He also believed that any adoption of specific accounting practices within the government context is aimed to signal the quality of management to external stakeholders. Ingram (1984, p130) also adds a similar notion that "...the higher quality of management may lead to benefits in the form of lower interest costs on municipal debt, and increase in the politician's popularity as a result of recognised performance". Under the banner of public sector reforms, the adoption of business style accounting regimes has been a global phenomenon in the developed and developing nations in the last two decades as part of broader economic and political reforms (Carlin 2005; (Chang 2009; Christensen 2002; Lapsley & Pallot 2000).

Following the resignation of President Suharto in 1998, Indonesia has experienced dramatic reforms in the political system and the public sector governance in the country. Unlike the Suharto regime (1966-1998), successive administrations have adopted a more democratic political system, in which people can directly elect the presidential and parliamentary member positions through free election. As Baswedan (2007) suggests, coupled with the political reform, an autonomy policy has also been granted to local governments at the provincial and district levels in governing their own administrations. In addition, the Government has adopted accrual accounting in the public sector. In this case, a new law and a set of governmental accounting rules have been issued aimed at improving the quality of the Government's reports and public sector practices in the country. The Law (*Undang-undang keuangan negara*, UU No. 17) issued in 2003 defines that the Government's departments and agencies at the national level are required to prepare their reports in accordance with the accrual based reporting system. This policy also applies to local governments. Specific rules about the types of reports and accounts relating to the Indonesian government financial accountability and reporting systems are outlined in the Government Accounting Standards (*Standar Akuntansi Pemerintahan*, SAP) issued in 2005.

Drawing from the new public management (NPM) philosophy, the Indonesian government initiatives are aimed at improving the quality of its public sector reports and this shows that the country follows a similar pattern to other nations where private sector managerial tools are incorporated into government institutions' practices (Guthrie 1998; Lapsley & Pallot 2000; Ryan 1999; Sharma & Lawrence, 2008). The Government believes that the adoption of the new government accounting standards will enhance the quality of financial information about the assets, liabilities and the operation of public sector agencies.

However, a formal adoption of accrual accounting would not automatically bring intended outcomes as officially stated. In this case, especially in developing countries there are many technical and institutional problems that the authors believe could potentially hamper the government's efforts to reform the public sector accounting for improving efficiency. Moreover, recent literature in the public sector accounting has critically questioned the claimed benefits of accrual reports for government organisations when it comes to actual implementation (Carlin 2005; Christensen 2007; Christiaens & Rommel 2008; Connolly & Hyndman 2008). On the one hand such a critical assessment run counters the globalisation movement towards the adoption of business-style practices that still continues (Broadbent & Guthrie 2008). On the other hand, this trend indicates that public sector accounting policy makers around the globe have paid little attention to the potential obstacles

that have made the use of the private sector practices overweighs its implementation costs. A number of technical and institutional constraints have been identified as major problems which have contributed to the failure of public sector reforms in developing nations (e.g. Mimba, Van Helden & Tillema 2007; Rahaman 2009; Sharma & Lawrence 2008). In developing countries these problems include the lack of technical capacities, underused of accounting information for managerial purposes, also old managerial practices and culture (Mimba et al. 2007; Rahaman 2009; Sharma & Lawrence 2008). Technically, ignoring these issues would be a waste of tax payers' money as the adoption of business-styles accounting systems is costly and time consuming (Van Peurseem & Pratt 1998). It also runs counter to the basic rhetoric behind the use of accrual accounting for efficiency improvement as promoted by the proponents of NPM-based practice. The rest of the paper is structured as follows: purpose of the study, literature review and theoretical lenses of the study, methods, result and discussion and conclusions and suggestion.

### Purpose of the Study

The purpose of the study is to theorise how an accounting system was adopted by a Provincial Government under Study (henceforth PGUS) in Indonesia and to examine institutional capacity of the provincial administration in adopting a new accounting system. In accordance with the definition of institutional capacity proposed by Howitt (1977) and the World Bank (2004), Mimba et al. (2007, p196) conceptualise it as the ability of an institution to decide on and pursue its goals, to perform tasks, and to improve performance constantly. In a government organisation, institutional capacity can be defined as the organisation's ability to identify problems, to develop and evaluate policy alternatives, and to operate the government's programmes. Thus in an organisational context, the level of institutional capacity of an organisation would depend on technical capacity and understanding of its employees to perform a specific task with the resources provided. Moreover, the presence of implementation problems also determines the institutional capacity of organisations in implementing their tasks. Therefore to examine how a new reporting system in an Indonesian provincial government has been changed and institutional capacity of the local government in Indonesia in adopting a new reporting system (i.e. the SAP), the study focuses on four issues:

- The nature of the reporting system change.
- The availability of skilled human resource required in adopting the new accounting system.
- The understanding of senior officials on technical and managerial aspects with respect to the adoption of the new accounting system.
- Potential implementation problems.

By uncovering and discussing these issues this study will not only contribute to provide knowledge about the role of accounting in a specific organisation and but also how an accounting system is actually implemented as suggested by Hopwood (2000), Lüder and Jones (2003) and Nor-Aziah and Scapens (2007).

### Theoretical Lenses

Public sector accounting research has used numerous methodological frameworks in theorising public sector accounting reforms. Two of these frameworks are economic and

institutional theories. Following Lapsley and Pallot's (2000) work this study uses both theories.

### *Economic Theory*

From an economic theory perspective, it is assumed that that the accountability and performance of public sector organisations can be enhanced by transforming the ways public organisations are managed, evaluated and financed into private sector managerial practise. Under the banner of NPM based principles, since the 1980s the role of business-style practices in the public sector across the globe has been strengthened (Broadbent & Guthrie 2008; Guthrie, 1998). According to Lapsley and Pallot (2000) the transformation of the public sector practices falls into seven key components:

“(i) the disaggregation of large public service bureaucracies into decentralized, corporatized units based on ‘products’, (ii) the introduction of contracts (short term) for employees and public service organization outputs (as an incentive), (iii) the adoption of what is considered to be private sector management styles and techniques, (iv) a greater stress on ‘frugality’ (economy and efficiency in resource use) and discipline,(v) a greater visibility to top management direction, (vi) greater quantification of ‘standards’ of service and performance measurement and (vii) a greater emphasis on outputs” (Lapsley and Pallot: 215-216).

Given the focus of NPM-based practices is to record, measure and present the economic data of organisations, accounting technology plays a central role. As a consequence, private sector accounting systems (i.e. accrual information, activity based costing system) that have been promoted as “more informative and objective” than cash based systems which are now formally institutionalised into public sector arena across the globe (Christensen & Parker 2010). Following the path of developed nations, NPM based-programs which emphasise the adoption of private sector style practise, accounting technology also has been integrated into public sector accounting reforms in developing economies (Sharma & Lawrence 2008).

Lapsley and Pallot (2000) suggested that NPM philosophy is drawn from three paradigms: public choice theory, agency theory and transaction cost economics. They also stated that the proponents of the public choice theory suggest that the attitude of organisations' employees as human beings is mainly driven by their own interest (Lapsley & Pallot 2000). Therefore, the adoption of a more informative accounting system is required to reduce that tendency. In this vein, it is necessary to separate regulating agencies from providing services and information about costs, subsidy policies and contract procedures available to the public (Boston *et al.*, 1996).

Agency theory assumes the human's tendency to maximise their self-interest (Lapsley & Pallot 2000). This situation can create conflicts between the principal and agents of an organisation. To overcome these problems, each organisation needs to develop a mechanism to reduce these conflicts by emphasising a system that can measure, report and evaluate performance as the basis in formulating incentives and sanctions (Lapsley & Pallot 2000). With respect to the transaction cost economics paradigm, this school of thought is concerned with the efforts to optimise governance structures. Based on this vein, rational agents will select governance structures which minimise their aggregate production and transaction costs (Williamson 1985). It can be concluded that the central notion of the economic-based perspectives is emphasised on rationality as the core concept of the paradigm. As suggested

by Lapsley and Pallot (2000) that concept differs from institutional theory perspectives as explained below.

### *Institutional Theory*

One of theoretical frameworks used by accounting scholars to understand accounting changes is institutional theory. According to this theory, organisations tend to adopt specific systems, structures, or procedures that are valued in their social and cultural environments (Ribeiro and Scapens 2006, p96). Therefore, an institution is defined as an established order comprising rule-bounded and standardised social practices (Dillard, Rigsby & Goodman 2004, p508). DiMaggio and Powell (1983) suggested that there are three types of institutional pressures which lead organisation to adopt a new rule or practice: coercive (rules and regulations imposed by regulatory authorities); normative (general societal beliefs and norms, including professionalisation); and mimetic (the tendency of organisations to copy the successful behavior of other organisations in the same field)” (DiMaggio & Powell 1983, p150). Thus, the rational function of accounting for promoting efficiency is only part of wider roles of accounting socially, economically and politically (Hopwood, 2000).

Institutional theory has been employed by numerous studies of public sector accounting reforms in developed and emerging economies. These studies include the work of (Lapsley & Pallot (2000) who observed the effect of the adoption of the accrual regime in New Zealand and UK; and Canada (Baker & Rennie 2006). Moreover, ter Bogt and Van Helden (2000) also investigate the influences of public sector accounting on the actions of managers and politicians in local governments in the Netherlands. In a developing country context, Nor-Aziah and Scapens (2007) also use Institutional theory in examining the implementation process of a private sector accounting technology adopted by a government organisation in Malaysia.

Although there is a growing number of accounting studies using institutional theory, these studies have been criticised as they were mainly focused on legitimacy and decoupling issues as the central notions in explaining accounting change phenomena (Dambrin, Lambert & Sponem 2007; Siti-Nabiha & Scapens 2007). Beyond this, accounting researchers need to expand their arguments in examining the detailed aspects of an institutionalisation process. In this process a number of issues can be further explored such as the ways organisations’ actors operate, the motives of these actors and also the implications of their actions (Nor Aziah & Scapens 2007). This is required to provide a better insight about how and why an accounting system is actually institutionalised.

### **Methods**

This study employed a case study approach as a means to provide a deep understanding of how a specific organisation as a unit of analysis adopted a new accounting system. As Yin (2009) suggests that a case study approach can be used for both developing and constructing theory. In contrast to the quantitative approach which emphasises the testing of specific hypotheses to explain and predict future phenomena (Luder 1992), a qualitative approach is designed to answer why and how questions related to a specific setting as suggested by Yin (2009). In collecting the data, the study uses two source of information: (1) document sources and (2) depth interview and questionnaire. The use of such methods has previously appeared in numerous accounting studies investigating an accounting change in an organisation (e.g. Dambrin *et al.*, 2007; Sharma & Lawrence 2008; Siti-Nabiha & Scapens 2005).

*Document Sources*

This study used document sources such as official policies of public sector reporting systems used in PGUS. There are two main sources that we examined: the Indonesian government's law and regulations about finance and reporting systems in the country including UU No 13 issued in 2003 and the SAP issued in 2005. In addition, we also examined the reports of the PGUS and published papers about the public sector accounting reforms in Indonesia.

*In-depth Interview and Questionnaire*

To capture the views of the people who have been assigned the task to implement the SAP in the organisation under study, interviews were undertaken with six managers in accounting, financial and internal audit divisions of a provincial government in Indonesia. The author used open-ended questions as guidance for discussion with the participants, but the interviewers were allowed to speak freely (Table 1).

**Table 1**

Main questions asked for open-end interviews

No.	Questions
1.	Why did this provincial government implement the SAP
2.	What is your opinion about the SAP?
3.	Do the staf here prepare the reports in accordance with the SAP?
4.	What are the main problems ecountered in adoptiong the SAP?
5.	Do you use the reports for decision making?

. The length of the interviews was 60 up to 90 minutes. All interviews were tape recorded. In addition, the study also used a simple questionnaire technique to capture the views from 23 staff in accounting and financial sections representing one person of each division. Their views are also important to gauge the level of understanding and technical capacity of those who have been assigned the task to produce financial statements based on the SAP. As Hepworth (2003) states, accrual accounting is not only about preparing reports. This also includes the whole process of preparing and using these accrual reports for decision-making. Accrual accounting is about the whole process of financial management. It is partly about obtaining a better understanding of the nature of 'costs', but it is also about a better understanding of what those costs mean for the financial management of government and the outcomes that a government is trying to achieve (Hepworth 2003, p38).

In collecting the information through the questionnaire, the participants were given an opportunity to complete the questionnaire over a period of one week. Any issues related to the questionnaire were clarified during the first meeting with the participants. The authors directly approached the participants in their office and their responses were collected one week to ten days later. The interviews were conducted in December 2007-January 2008. To protect the confidentiality of the participants, they were allowed not to disclose their identity (name and position) in the questionnaire. Twenty participants of twenty three interviewees who were approached replied to the questionnaire, which indicates a high level of response (86%). As this study is a case study, the questionnaire was only used to complement their views captured through open-ended interviews. Moreover, the unit of analysis of the study was a provincial government, thus each participant was treated as an informant in the context of an organisation under study. Therefore, statistical tests were unnecessary (Mignot & Dolley, 2000; Rutherford, 1992).

## Results and Discussion

This section reports the findings; (1) reporting system change and (2) institutional capacity and (3) implementation problems with respect to the adoption of a new accounting system in a provincial government in Indonesia.

### *Reporting System Change*

Significant reforms of laws about public sector management practices only occurred following the overhaul of the political system since the late 1990s. These reforms included the adoption of accrual accounting for local governments (provincial and district levels) in 2003. As explained earlier the policy to adopt accrual accounting is based on UU No. 17 promulgated in 2003, and SAP (a set of government accounting standards) issued in 2005. These rules required the Government at all levels to produce financial statements. Each local provincial government, for example, must produce not only budget realisation reports but also balance sheets, cash flows & notes to financial statements. These reports must be available both at provincial level (consolidated reports) and each division (agencies, organisations, hospitals) of a province.

**Table 2**  
Reporting systems

<b>Reporting system</b>	<b>Types of report</b>	<b>Reporting level</b>
Old reporting system 1945-2003	Budget realisation reports	Provincial level
New reporting system (Since 2004)	<ul style="list-style-type: none"> <li>• Budget realisation reports</li> <li>• Balance sheet</li> <li>• Cash flow</li> <li>• Notes to financial statements</li> </ul>	<ul style="list-style-type: none"> <li>• Provincial level</li> <li>• Divisions level (24 entities)</li> </ul>

Source: Harun (2007), SAP (2004), UU No. 17 (2003)

According to SAP the implementation of the new government accounting standards is necessary to enhance the relevance, neutrality, timeliness, completeness and comparability of the government's reports. Beyond this, the SAP states that the implementation of the new accounting system will support the Government's efforts to combat corruption as the producers of government reports at the central and local levels are required to publish their reports for the public. It is also expected that by producing more informative financial information in accordance with the SAP – it enables the tax payers and recipients of the public sector services to identify the level of the effectiveness and efficiency of public sector agencies' operation in the country. Moreover, with the availability of accrual reports, the managers and decision makers across public sector's agencies in the country will be better informed in making better decisions in investment and operational spending (SAP 2005). Thus, the availability of high quality financial information is believed to reduce the gap of information asymmetric between the government and society and other stakeholders on the use and allocation of state finances. As stated by the former Head of the State Audit Board, Anwar Nasution (Nasution 2008), the lack of public financial transparency contributed to the flourish of corruption during the Suharto era, thus the adoption of a more informative reporting system is necessarily required to strengthen the transparency of the government and prevent the misuse of the government assets. This fact indicates that the Indonesian government policy to adopt the SAP was driven by NPM based philosophy, in which the

adoption of a business -styles accounting systems would improve the efficiency and performance of public sector organisations.

### *Institutional Capacity and Implementation Problems*

The issue of the institution capacity belonging to the provincial government is drawn from information about human resource availability and the understanding of senior officials in the PGUS about the new accounting rules. Moreover, implementation problem issues reflect the views of the participants with respect to the most critical problems in adoption of the GAS in the provincial government.

### *HUMAN RESOURCE AVAILABILITY*

Human resource availability is one of the most important factors that determine the extent to which institutional capacity of an organisation can successfully implement a new accounting system (Christensen 2002, 2010; Luder 1992; (Jones and Puglisi (1997); ter Bogt & Van Helden 2000). Nonetheless, this study finds the adoption of the SAP in the PGUS has not been equipped with a significant number of personnel to implement the new accounting system. There were only two senior officials who have bachelor degrees in accounting (without professional accreditation) and none of them have experience in accounting jobs. Other officials mostly graduated from political science, law, and public administration and none of them have had prior experience in the private sector accounting. This situation indicates these officials have irrelevant educational backgrounds to adopt the new accounting system (Table 2).

This finding indicates that the lack of accountants is confronted with the abundant tasks to prepare twenty three sets of financial statements of all divisions (or agencies, organisations, hospitals) and one set of consolidated reports at the provincial level. To prepare these reports, the provincial government under study was forced to hire accountants from outside consulting or accounting firms to do the jobs. A senior official in financial and accounting of the provincial government stated:

“It is more complicated, but the law [Law 17/2003] requires us to implement it. We have no choice, but to outsource the work to outside.”

The statement also represents the views of three other senior officials interviewed who suggested that the technical capacity of existing employees in the PGUS do not allow them to cope with the requirement of the new accounting system. As a consequence, the application of the new accounting system has increased the costs incurred in preparing the PGUS's reports. Moreover, the PGUS still pays the salary of existing employees in the accounting function. This is due to the fact that the existing human resource management system in PGUS, as with other government institutions in the country still gives privilege to civic employees as they can only be dismissed if they are involved in criminal acts or voluntarily resign (McLeod 2006). As stated by an interviewee, it is not easy to dismiss a government official regardless of his or her actual work. Therefore as the policy to adopt a new accounting system in the PGUS is institutionalised into an old type of human resource management system, the adoption of the new accounting system produces an outcome that contradicts the very notion of NPM-based practices for efficiency improvement as it increase the cost of the accounting function in the provincial government.

**Table 3**  
Profile of senior accounting and financial officials in PGUS

<b>Tertiary education background</b>	<b>Number of employees (%)</b> <b>N = 23</b>
Accounting	2 (8%)
Political sciences	6 (25 %)
Agriculture	8 (33%)
Public administration	3 (12 %)
Others	4 (16)

#### *LEVEL OF UNDERSTANDING*

The information captured through the questionnaire indicates that the majority of the officials lack understanding about the importance of the SAP. As Table 3 shows only a small minority (10%) of the interviewees indicate that that they have a good understanding of the purpose of the implementation of the SAP. Only five 5% of participants stated that they have the technical capacity to use the SAP in preparing the annual reports of the PGUS. Although they recognised the implications of their failure to present the reports in accordance with the SAP<sup>3</sup>, only 15% of the interviewees suggest that they can independently analyse the information reported in the financial statements of the PGUS (Table 3).

**Table 3**  
Level of understanding

<b>Interviewees's statement</b>		<b>N= 20</b>
1.	I fully understand the purpose of the SAP's implementation	10%
2	I am able prepare the annual reports based on the SAP	5%
3.	I am able to independently analyse the information in the financial statements prepared based on the SAP	15%
4	I understand the consequence if the organization fails to prepare the reports based on the SAP	80%

The views from three interviewees in the accounting division of the PGUS also confirm the lack of understanding among the officials and politicians (the governor and local parliamentary members) in using the PGUS's reports in making decisions.

“These reports are complicated to understand.”

“We also do not use these reports in the budget formulation”.

The interviewees also suggest that the political reasons are more important factors in the decision making process in the provincial government:

<sup>3</sup> If local governments fail to produce a set of reports based on the GAS, the auditors (from the State Audit Board) will issue them with qualified or no opinion. At the time of this paper being written (2010) there were no formal rules about sanction for the failure to produce SAP-based reports.

“I doubt these reports are used by our boss [the governor] for making decisions. These reports are only used for complying with the law [Law 17/2003 on state finance]”.

Making decisions about the budgets and projects are more related to the interests of these people [politicians].

Thus it appears that both the lack of understanding and political motives have undermined the managerial function of the accrual reports in the PGUS. In other words, the change in the reporting system has no or little impact on the process of decision making.

#### *IMPLEMENTATION PROBLEMS<sup>4</sup>*

In responding to the question about the most critical (number one) problem in implementing the GAS, a great number of the participants (40%) point to the lack of skilled staff in accounting. Two interviewees of the study state:

“The biggest problem we are facing is the lack of people who can do the job [preparing the reports in accordance with the SAP]”.

“We are struggling to prepare the reports as no one can prepare the reports properly”

This factor was followed by the lack of experience in the relevant area (30%) and facilities (15%) and leadership deficiencies from senior managers (10%). Only five percent of them point out lack of penalty as the most essential implementation constraint (Table 4).

*Table 4*  
Implementation problems

<b>No.</b>	<b>Interviewees’ statement on the most critical implementation problems</b>	<b>Participants (%)</b>
1.	Lack of skilled staff	40%
2.	Lack of relevant experience	30%
3.	Facilities deficiencies	15%
4.	Lack of leadership	10%
5.	Lack of penalty	5%

## Discussion

This section discusses the findings based on both economic and institutional perspectives:

### *Economic Perspectives*

<sup>4</sup> In this case the participants were instructed to choose only one answer they suggest as the most crucial problems in the implementing the SAP in the PGUS.

From an economic-based perspective, the adoption of a more informative accounting system indicates that the provincial government follows the path of government entities in the developing countries in adopting a NPM-based practise. Nonetheless, the political and managerial roles of the executive officials (the governors and the managers of the provincial government's divisions) have yet to be separated. In other words, the change in how the local government's reports are prepared is not coupled with the separation of the roles of the governor and the local parliamentary members as politicians and managers. This fact contradicts the core argument of NPM-philosophy that to ensure the conflict of interests, it is necessary to separate the roles of elected politicians by the people from managerial decisions and actions (Lapsley & Pallot 2000).

Therefore, it can be argued that from NPM-based principles, the organisational framework of the PGUS limits the usefulness of accrual information for making economic decisions. As Lapsley and Pallot (2000) state, the NPM-based philosophy promotes the separation of regulating agencies from managerial roles. This is necessary to prevent people's tendency from serving their own agenda in allocating and using public money (Boston *et al.*, 1996). As there is no separation between the political and managerial roles of the elected politicians in the PGUS (i.e. the governor and the local parliamentary members) – this situation potentially opens an opportunity for them to allocate the local government's resources that can serve their own political interests regardless of the economic reasons.

In addition, the study also shows a gap between the rhetoric or the intention behind the policy to adopt the SAP for improving efficiency and the lack of institutional capacity of the PGUS. This situation is indicated by the fact that policy to adopt the new accounting system failed to recognise the lack of skilled human resources and existing implementation problems. As a consequence, the adoption of the SAP has made the expenditures incurred to run the accounting function of the PGUS more costly. From economic based perspectives, the increasing of costs in the accounting function of the PGUS contradicts the views of the proponents of NPM-based practices to make public sector organisations be more efficient.

### *Institutional Perspectives*

This study finds the decision to adopt the accrual based reporting system in the PGUS was beyond its authority. From an institutional perspective, the adoption of the new accounting system at the provincial level in Indonesia is indicated by coercive isomorphism as local authorities are obliged to comply with accounting rules (i.e. SAP) issued by the central government. This situation differs from the early process of the public sector accounting reforms in New South Wales, Australia (for example) where accounting consultants and senior local government officials played a leading role in diffusing the ideas to adopt accrual accounting (Christensen 2002). The nature of the political and legal systems in Indonesia implicates how an accounting system is institutionalised in the public sector in the country (Fitriani, Bert & Kai 2005). This point supports Luder's (1992) assessment that the nature of legal and political systems shapes the framework of a government's reporting practice. This fact is not surprising as the decision-making of the administration system in Indonesia has been determined at the central level. As Luder (1992) argues that the nature of legal and political systems is one of dominant factors influencing a public sector accounting reform of a nation. Institutionalised orders and practices influence how a new practice is adopted (Siti-Nabiha & Scapens 2007).

Moreover, at the implementation level this study also shows that the PGUS has not been equipped with sufficient institutional capacity in terms of human resource deficiency and the presence of implementation barriers. This fact implies that the decision for adopting a new accounting system at the local level in Indonesian did not carefully consider the

technical capacity of an organisation assigned to adopt the new accounting system. In this vein, the policy to use the new accounting system was primarily imposed by the government at the central level regardless of the institutional capacity of local administrations and related costs incurred. Therefore, the gap between the rhetoric behind the accounting reform for efficiency improvement contradicts its consequences.

In this case the accounting reforms at the local level in Indonesian governments can be seen as “an arena” for powerful actors at the central level to exercise their power rather than a search of efficiency improvement. The power of the Government at the central level has been effectively demonstrated through the accounting change at local level. As the study shows, accounting has been used by the central government to determine financial and reporting practices at lower administrations. This observation falls under the notion that “[a] central government normally has the power and authority to define the norms and standards of conduct that direct behaviour of local units (Chang 2009, p149). Beyond this, the argument supports Covalleski and Dirsmith’s (1995) view that the process of institutionalising calculative techniques such as accounting systems in the public sector is a political process and often influenced by the relative power of organisational constituents. This finding also emphasises the notion that the formulation of a reporting system is not a neutral process but dominated by the institutional interests of a more powerful Government (Chang 2009, p149).

## Conclusions and Suggestion

The study attempts to understand how accounting change has been directed in a provincial government in Indonesia. The study also examines the institutional capacity of the provincial administration and problems it encounters in adopting a new accounting system. Both economic and institutional perspectives have been useful to demonstrate how accrual accounting has been incorporated into the public sector arena and its consequences in a public sector context.

Drawn from an economic perspective, the policy to adopt the accrual accounting system in provincial government level Indonesia indicates the country follows a similar pattern to other countries aimed at strengthening a more accountable, and transparent efficient government. As with the managerial reforms of public sector organisations in Australia, New Zealand and UK, the decision to adopt accrual accounting has been the central theme of these reforms (Ryan 1998; Carlin 2005). In the context of the PGUS, accrual accounting has also been promoted for efficiency improvements in the government organisations at the national and local level. Nonetheless, the reporting system change was not followed by the separation of conflicting roles between the governor and local parliament in PGUS as politicians and managers. This situation undermines the technical role of accounting for economic reason.

From institutional theory, the study shows two critical points. Firstly, this study indicates how accounting has been used by the central government in determining the nature of a reporting system at provincial level in Indonesia. The nature of the political system in Indonesia which gives significant roles of the central government to oversee local administrations has easily facilitated accounting to be “a political instrument” to control local governments. This differs (for example), from the Australian approach in the public sector accounting reforms, where the process of the adoption of accrual accounting was more complex and involved competing stakeholders from government and professional organisations (Christensen 2002, 2010; Ryan 1999). These arguments imply that for the Indonesian context -- the role of accounting as a political tool for controlling people (and organisations) undermines its roles of enhancing performance and efficiency improvement. In other words, the arguments of the study also add a further example, how established orders

(in terms of organisational structures, old practise, existing institutional capacity) can hamper the values of public sector reforms as a managerial tool to improve the operation of public sector entities.

For further studies, the use of economic-based perspectives along with institutional theory has \ potential in examining a specific accounting change of an organisation from different perspectives. Moreover, the use of multiple approaches in collecting the data was useful in providing a complete picture of the dynamic process of accounting changes in a public sector context. Therefore this approach can be replicated in the context of local governments in other countries. However, the insights presented here cannot be generalised as the data of the study was only drawn from a provincial government in Indonesia.

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