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Public sector commercial orientation and the social contract: a study of performance management in a non-competitive environment

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Abstract

Purpose - The aim of this paper is to study the workings of commercial orientation, with a focus on performance management, in an environment that is characterised by limited competition between the public and the private sectors and a high level of government social responsibility. Design/methodology/approach - An interpretive case study approach is adopted for this study. It draws on primary data from interviews with key personnel in public sector organisations, and on secondary data from government publications such as annual reports and budget papers. Findings - This study shows that the market-based performance management system has failed to achieve its intended objectives because it was introduced in a socio-economic context that is hardly supportive of market management practices. The study shows that service delivery to the public has remained driven by social rather than economic imperatives. In the absence of other service providers, the Government's social responsibility towards its citizens has compelled service provision irrespective of the cost and reduced the cost-benefit relationship in having informative costing systems. Practical implications - Examining the workings of a market-based performance management system in a non-competitive setting provides evidence of the difficulty of achieving the intended benefits from the adoption of commercial practices in public sector agencies in some cases. Originality/value - Whereas extant literature focuses on the adoption of business practices in the process of public sector reform, no prior study has looked at this concept in a non-competitive market. Understanding the workings of the market practices in such an environment where contestability is limited is fundamental to policy makers and researchers.

Keywords

contract, public, study, performance, sector, management, non, commercial, orientation, competitive, social, environment

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Findings – This study shows that a market-based performance management system has failed to achieve its intended objectives because it was introduced in a socio-economic context that is not supportive of market management practices. The study shows that service delivery to the public has remained driven by social rather than economic imperatives. In the absence of other service providers, the Government's social responsibility towards its citizens has compelled service provision irrespective of the cost and reduced the cost-benefit relationship in having informative costing systems.

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Keywords Performance management, commercial orientation, stakeholder theory, social contract, non-competitive environment, cost information, Northern Territory.

Paper type Case study

Introduction:

During the past three decades, governments around the globe and in Australia have been increasingly pressured by a competitive environment and a thrust to reduce the costs of their public sectors. Hence, information on the performance of public sector organizations became increasingly important. This has been recognized at all government levels that aimed to reform their public sectors within the theme of public accountability and the underpinning philosophy of the emerging New Public Sector Management (NPM). The NPM introduced a new wave of management techniques to the public sector, and was defined by the infusion of market principles into the government world, largely based on the justification that they are necessary to improve government performance and accountability (Ferlie et al., 1996; Gore, 1993; Savas, 2000; World Bank, 2000). These new market principles have encompassed the adoption of many private sector management and accounting practices. Accrual accounting was at the heart of these commercial practices, with governments shifting their accounting systems from cash to accrual to mirror the accounting practices applied in the private sector.

The shift from cash to accrual accounting was not an end in itself. Governments believed that accrual accounting provided additional performance information than that available under the cash system, which would lead to better decision making and enhanced performance. Accrual accounting was perceived to be useful in providing information that would have a positive impact on the efficiency, effectiveness, service quality, performance management, resource allocation, and accountability of public sector organizations because it was a more comprehensive system of accounting which would improve government management practices (Harris, 2001; Hood, 1995a, 1995b; Hopwood, 1992, 2000; March and Olsen, 1989; Savas, 1987).

This study examines the commercialization process in the Northern Territory (NT) public sector with an emphasis on the new output performance management adopted in the process of commercialization of the public sector. The evidence comes from interviews with key personnel from the Northern Territory (NT) government departments and secondary sources of information, particularly NT government reports. This involved the adoption of accrual accounting for performance management purposes as this was viewed as a more comprehensive system of accounting than the cash accounting system in use before the reforms. Most writers and all governments seem to suggest that the adoption of accrual accounting would make a great contribution to government efficiency and contribute positively to performance management. However, this research carried out in the NT indicates that there was no improvement in the NT, partly due to local circumstances, where there was a very large public sector presence and a small and dispersed population, with few large concentrations of population. This indication is developed and discussed in light of stakeholder theory that embeds two different approaches that shape each other. The first approach reflects a managerial philosophy that is based on NPM principles so that government organizations deliver public sector services with the aim to achieve cost efficiency and financial feasibility. The second approach reflects an ethical dimension, a social responsibility mandate, so that government organizations attended also to community needs and social welfare. Hence, according to stakeholder theory, government organizations would need to consider the two approaches to attend to all different stakeholders' interests (Deegan and Samkin, 2004; Freeman, 1984; Gibson, 2005; Heath and Norman, 2004; Hyndman and Anderson, 1991; Stiglitz, 1989).

The remainder of the paper is structured as follows. Section 2 provides a brief literature review, section 3 introduces the methodology and some relevant theory, section 4 discusses the economic and social specifications of the NT as a non-competitive environment followed by an overview of the commercial orientation initiatives that have taken place. The subsequent sections provide an explanation of the results-focused performance management system that was introduced in the process of commercialization. Before ending with a conclusion, the paper analyses the performance management system and assesses its working within the environment of its application.

2 Literature Review:

Reviewing the literature on accrual accounting in the public sector revealed a dearth of publications on accrual accounting before the 1990s that was followed by an extensive stream of publications which is continued today. Advocacy for accrual accounting dominated the early stage of the literature, with arguments that accrual accounting in the public sector would improve performance and accountability (Carpenter, 1987; Regan, 1987; Robson, 1988; Rowles, 2002). It was clear from the literature that accrual accounting in the public sector has been controversial and that much advocacy for or against its implementation appears in the literature currently (Barton, 2009; Broadbent and Guthrie, 1992; Carnegie and West, 1997; Carnegie and Wolnizer, 1995; Funnell and Cooper, 1998; Guthrie and Parker, 1998; Guthrie et al., 1999; Kelly and Wanna, 2004; Modell, 2001, 2004; West and Carnegie, 2004).

The call for accrual accounting in the public sector has been confronted by a growing stream of literature that criticised or questioned its implementation and usefulness because of the unique characteristics of public sector services. While there have been many studies that recognised the importance of market practices in the public sector and their relevance in assessing performance and promoting accountability (Guthrie, 1994; Micallef, et al., 1994; Christensen and Yoshimi, 2001; Carlin and Guthrie, 2001; Walker, 2001, 2002), there have been also some concerns regarding their use and usefulness in the public sector context. For example, various studies have examined the extent to which accrual accounting and performance information have been used in the public sector (Rivenbark and Kelly, 2000), and the difficulties relating to the implementation of the accrual framework in the public sector (Christensen and Yoshimi, 2001; Guthrie, 1994; Guthrie and Parker, 1998; Modell, 2001, 2004; O'Faircheallaigh et al., 1999; Polidano, 2001; Siddiquee, 2010; Walker, 2001, 2002). Most of these studies used mainly theoretical analysis of accounting information and its relevance to performance and accountability. Other studies investigated its use at country level or local government level.

None of the studies in the literature has examined the relevance of accrual information and market-based performance management in an environment characterized as having little competition, especially whether market-based practices were infused into the public sector to encourage competition, primarily because of the belief that competition would drive efficiency and effectiveness. This could arise because it made government agencies become cost conscious to deliver a competitive price, and to ensure performance excellence when performance was evaluated and benchmarked against others. Hence, this study fills a gap in the literature by examining the extent to which the adoption of commercial practices has been useful and relevant in government departments that operate in a very unique environment characterized by limited competition throughout the economy. For example, Carlin and Guthrie (2001) showed that the implementation of accrual budgeting in Queensland and New Zealand has not achieved the intended results.

While it was clear from the literature, in both cases for and against accrual accounting, that accrual accounting implementation was not an end in itself but rather an accounting system change within the NPM movement that called for a more efficient, effective and accountable public sector. The NPM was based on the notion of competition, and governments and accrual accounting advocates believed it would stimulate performance improvement. In this regard public choice theorists believed that competition provided external pressure on public sector managers to provide better services. It was anticipated that competition would result in improved efficiency and effectiveness in providing public service, and hence accrual accounting was seen as a necessary but not sufficient change which would produce a more complete financial information system that supported the objectives of competition and performance appraisal. Therefore, this study offers a unique contribution by studying the working and usefulness of accrual accounting in a unique economic environment characterized by limited competition and diseconomies of scale.

3. Methodology and Theory:

To address the research objectives of this study, a qualitative approach has been adopted. The utility of the qualitative approach in the accounting field has been established and discussed at a general level by several researchers (see for example Humphrey and Scapens, 1996a, 1996b; Kloot, 1999; Scapens, 2004). The choice of a particular method of inquiry (qualitative or quantitative or a mix of both) should not be determined by the researcher's commitment to a particular strategy (Hopper and Powell, 1985). Hopper and Powell (1985, p.429) argued that "certain fundamental theoretical and philosophical assumptions underlie any piece of research; there is no such thing as totally objective or value free investigation". Furthermore, some accounting researchers tend to consider their research as either belonging to the 'narrative' or 'interpretive' category. Traditionally, narrative research has been depicted as seeking to identify and describe specific events in a factual and non-analytical manner (Funnell, and Cooper 1998). Interpretive research, on the other hand, is argued to go beyond the narrative style and it aims to explore and explain the issue under investigation while at the same time preserving a thorough and comprehensive description (Parker, 1999).

The present study is built on the understanding that organizational realities exist as a social product of human interaction, symbolic discourse, and creativity (Humphrey and Scapens, 1996a, 1996b; Lee and Humphrey, 2006; Morgan, 1980; Morgan and Smircich, 1980). They all suggest that the researcher needs to consider the wider social environment for understanding a phenomenon. Hence, the view taken in this study is that accounting, as a central component of performance management, is socially constructed and therefore it is subject to a variety of social, economic, and political pressures (Berry et al., 1985; Hoque & Hopper, 1994; Miller, 1994). This implies that in order to get a good understanding of accounting system change, from cash to accrual, and its working in the NT public sector, an interpretive case study approach is a suitable approach.

This case study has been constructed using analysis of primary and secondary data. Primary data were collected by semi-structured interviews from senior managers and decision makers in NT Government departments, mostly the Department of Corporate and Information Services (DCIS) and the Department of Health and Community Services (Health). Emphasis was placed on these two departments as one was the main driver of improvements in performance management (DCIS) and the other was the main provider of direct services to the community (Health). Approximately 60 interviews were carried out with departmental CEOs, CFOs, interdepartmental directors (i.e. people in positions of payroll manager, human resource manager, asset manager, purchasing manager, accounting manager, budgeting manager). All interviews were tape-recorded and later transcribed for analysis. Records were kept of the content of all interviews. The interviews varied from 1 hour to 3 hours in length, and sometimes further clarifications and updates were obtained by email or telephone contact. Interview questions sought the opinions of these managers on the usefulness of accrual accounting in their departments and the extent of its actual usage. While there was no clear order of questions in the interviews, they were selected based on themes prepared beforehand. This method has enabled alteration and adjustment of questions to encompass the understanding of the interviewee's ideas and conceptions. Secondary data from archival records also provided an important part of the data collected. Annual and semi-annual reports, budgets, parliamentary debates, administrative records, discussion papers, accounting concepts and standards, newspapers and journals were all used to complement the data needed and to validate interviewees comments wherever possible. Thematic analysis was applied to analyze the data. Hence interview data together with data from secondary sources, were coded according to a number of themes that corresponded to focal issues developed from research questions. This method helped analysis to capture a rich and detailed appreciation of the institutional environment in which the adoption of market practices evolved, and accrual accounting functioned.

The NPM has generally been subject to a great deal of debate amongst scholars and practitioners, and irrespective of whether it is seen as positive or negative, the commercial orientation has some implications for the social responsibility of the government. This is because the commercial orientation represented by the market-based reforms, and the social responsibility of the government require some contrasting institutional capabilities (Hayek, 1994). The commercial orientation, in making the government operate like a business, may relieve government organizations of their social responsibility mandate as they may abandon or curtail unprofitable activities. Government organizations may restructure their operations in accordance with more traditional business principles and take the necessary actions to replace service provision that has traditionally been based on needs, social obligations, and privileges, by one that is market-based and driven by profitability and the customer's ability to pay (Narver and Slater, 1990; Pierre, 1995). This implies that the traditional social contract between the government and its citizens is potentially subjugated, especially when service delivery is abused or abandoned because of the absence of profit.

The commercial orientation is in line with the public choice theory which provided the theoretical justification for the business approach to government activities, and in particular it advocated the pursuit of 'self-interest' in the operation of the public sector with no 'public interest' (Barton, 2009; Buchanan and Musgrave, 1999; Mueller, 1997; Self, 1993). However, this study draws on a broader theoretical notion that is derived from stakeholder theory which integrates both the resource-based view as well as the market-based view, and adds a socio-political level (Barney, 2001; Deegan and Samkin, 2004; Freeman, 1984; Gibson, 2005; Heath and Norman, 2004; Hyndman and Anderson, 1991). This means that an organization's performance and accountability should not be assessed merely in terms of profit or financial terms but rather more generally in terms of achieving the interests of a range of different stakeholders. In the public sector there are multiple stakeholders with an interest in the performance and accountability of government organizations (i.e., ministers, parliamentary representatives, employees, voters, business partners and associates or the community at large).

Hence government organizations in the NT are accountable not only for the economic decisions associated with spending public money but for its efficiency and effectiveness and the value achieved. Thus, the adoption of some commercial practices in the NT public service was justified as an attempt to provide better value to the community in the provision of public services. Also, the social mandate between the government and its community requires the NT Government to ensure its people have access to mainstream services on an inclusive rather than exclusive basis. This stands in contrast with the commercial orientation that requires service provision to focus on cost efficiency and economic feasibility (Stiglitz, 1989). Hence, to satisfy the conflicting demands and interests of the various stakeholders, stakeholder theory suggests that the survival of the organization depends on its ability to satisfy all these interests (Deegan and Samkin, 2004; Gibson, 2005; Heath and Norman, 2004).

The essential research question addressed in this study is whether the adoption of accrual accounting contributed positively to the performance of government organizations in the NT. It is appropriate to examine this question within the notion of stakeholder theory to see how the interests of the different stakeholders have been coordinated. That means, whether the NT Government in its adoption of accrual accounting and the market based performance management system has focused on satisfying economic imperatives (i.e., cost saving, profit increase, user pay) or it has also considered the social responsibility towards its people to satisfy the interests of a range of stakeholders.

4 The NT and its commercial orientation

The Northern Territory of Australia has followed the global and national commercial orientation and adopted market practices in the thrust for public sector reform, though this commenced later than in the rest of Australia. The reform of the public sector in the NT started in 1978 when self-government was granted by the Commonwealth. Before that, the Territory's administration had a colonial nature resulting from the fact that responsibility resided with the Commonwealth government in Canberra. The Territory was grouped with a number of other dependent areas for the purposes of central control and administration (Hawkes and Moir, 1997). The newly elected NT Government in 1978 took over an economy that was markedly different from those of the other Australian states in the following aspects:

- The demography of the NT: where 1 per cent (200,000 people approximately) of the Australian population is scattered over an area the size of France, Spain and Italy combined (17.5 percent of the nation's geographical surface area). This dispersion of the population made the cost of provision of services higher than in other states and territories. In addition, 30 percent of the NT population are indigenous people (Aboriginal and Torres Strait Islander), while these are less than 4 per cent in other state/territory populations. Indigenous people are more likely to live outside urban areas, than other Australians. Statistics show that 70 percent of the Territory's indigenous population live in remote or very remote localities (Australian Institute of Health and Welfare, 2008). In 2001, there were 342 discrete communities in the NT; there were only 139 in Western Australia, 72 in Queensland, 42 in South Australia, and 10 in New South Wales (Australian Bureau of Statistics, 2005). This situation resulted in an increase in the cost of services to reach this group of the population.

- The isolation of the NT and the remoteness of many of its communities have resulted in a limited ability to recruit and retain professional staff in rural and remote areas. This affected the ability to deliver services in those areas and made it necessary to offer higher remuneration packages to attract staff which resulted in cost increases in provision of services in the NT.
- The relative absence of a private sector: The high cost of service provision and the lack of economies of scale have not made the NT a viable market for most private service providers.

These characteristics have put the Government at a fiscal disadvantage and made it challenging to provide a level of services compared with the other states of Australia. The higher cost of service provision made the Government more dependent on Commonwealth grants than the states (NT Treasury, 1999, 2000). This resulted in making the Territory vulnerable to changes in Commonwealth policy and especially subject to pressure from the Commonwealth through the imposition of any condition that could be associated with those grants. This volatility was evidenced by the considerable cut in Commonwealth grants experienced in the mid-1980s (NT Treasury, 2000). For example, in 1981 the Commonwealth/State Cost Sharing Agreement ceased to cover its share (50%) of the net operating costs of NT hospitals and associated central services. Commonwealth funding for the NT has become limited to a number of national programs and projects such as the Alice Springs to Darwin railway. Hence, the funding of NT Government agencies became primarily a responsibility of the NT Government and it became necessary for Government agencies to contribute more to their own expenditure through a wide range of charges to make up for the reduced flow of funding from the Commonwealth. Within this context, NT governments embraced market reforms with the intention of creating a competitive environment that would improve public sector performance by reducing costs and increasing revenues, or where possible relinquishing public service delivery to the private sector. This reform process can be divided into three periods in which three major tranches of the reform were implemented, 1978/90 during which most privatization and outsourcing activities commenced; 1991/2001 during which most of the management and accounting initiatives were issued to emphasize the commercial direction of the Government; and 2002 when the 'Working for Outcomes' framework and accrual accounting were introduced.

After 1995, NT Government efforts to improve its financial and management practices continued. In 1996, there were a number of significant developments in the financial relations between the Commonwealth and the states and territories (NT Treasury, 1996). However, most of the management and accounting practices that were being applied in the public sector in the NT were only applied in the corporatized entities with some practices being also applied at the whole of government level. The non-corporatized government businesses such as government departments did not become affected by the full commercialization process until year 2002 when the NT Government initiated a performance management framework that mandated government departments to use private sector practices.

At first, the NT Government saw privatization and outsourcing as an opportunity to transfer risks to the private sector with the potential for improved business efficiency. This was based on the premise that private sector organizations are more efficient than their counterparts in the public sector. In doing this, the Government intended to increase the size of the private sector with the aim of creating competition between service providers with positive performance implications (Hoque and Hopper, 1994, 1997; Parker and Bradley, 2000; Sarker, 2006). However, all examples of privatization in the NT that took place in the last two decades were small in terms of their revenue size and did not have a major impact on the economy or the welfare of the people. And so by the year 1990, the NT Government still owned most of the economic infrastructure, including hospitals, universities, schools, mines, postal services, insurance and electric power. This was due to the lack of private providers' appetite for privatization in the NT because of its poor economies of scale and the high cost of service delivery. The relatively small and dispersed markets in the NT mean that the level of utilization was too low for many investments to be of interest to the private sector. Unless the private sector can capture an income stream that makes an investment profitable, then private sector investment is likely to be limited (Barrett, 1997; Reilly and Tamkin, 1996).

While privatization and outsourcing were not significant enough to entice competition into the NT, the Government continued its market-based reforms. In this respect, the Public Sector Employment and Management Act was introduced in 1993 and incorporated a range of private sector reform principles, such as devolution of responsibility, performance management and accountability. Also, in 1995, the NT Government accepted the reforms set out in the National Competition Policy (NCP), which was considered by all governments to be a major catalyst for public sector reform. It was considered by most Australian governments that in a market-based economy competition plays a major role in generating productivity and cost efficiency improvements (Hoque and Moll, 2001; NT Treasury, 1996) and some Federal government funding was tied to the adoption of appropriate competition policy. In this regard it is interesting to note that payments to the NT under competition policy in the 2000-01 financial year fell to their lowest level of only \$4.5m, from \$14.4m in the preceding year, because of the limited progress made in compliance with competition policy. After the adoption of accrual accounting in 2002 the payment rose to \$7.6m, indicating that the NT had moved to comply with the policy and that it was then in a comparable position to the states and the Australian Capital Territory.

The principal implication of the NCP for government entities was that they should not demonstrate any anti-competitive conduct. The NCP required the NT to develop a competitive neutrality policy which aimed to eliminate any competitive advantage public sector agencies have as a result of Government ownership (NT Treasury, 1996). Examples of such advantages may include: discounted interest rates; guarantees on debts; regulatory preference; and tax exemptions (McTaggert, 1996; NT Treasury, 1996). The Independent Committee of Inquiry (1993) stated that where these disparities exist, there is a "potential to reduce economic efficiency and community welfare by distorting the allocation of resources" (p.297). Without competitive neutrality the "society's resources are not being put to their best use" (Hilmer et al., 1993, p. 297). So the NT Government aimed to remove advantages occurring as a result of government ownership, and introduced measures to ensure that government businesses competed on equal terms with private business (Girle, 2004). It is clear that the NCP and its competitive neutrality has aimed at eliminating agencies' advantages resulting from Government ownership and to put them on similar grounds with their counterparts in the private sector to increase competition and provide a real market test of service delivery. However, this did not add much value in the NT because public sector agencies were not in competition with the private sector because of the limited range of private sector activities and investment. Furthermore, wherever a private sector investment developed in the NT, public sector agencies were prohibited from competition through a deliberate government policy of developing and maintaining the private sector at large.

5 Working for Outcomes: a performance management framework

The Northern territory government was reluctant to adopt the full range of reforms required under the NCP and it resisted the adoption of accrual accounting and performance management for a number of years because of grave doubts about their usefulness in a largely non-competitive environment. All interviewees who witnessed the process of change stated that the major impediment that prevented the implementation at an earlier stage was the Under Treasurer of that time. According to some, 'he did not see any value or usefulness for accrual accounting and performance reporting in the context of the NT'. A senior Treasury executive supported this by stating that 'if the Under Treasurer has recommended (accrual accounting and performance management) any time after the 1990s it would have happened because he had a lot of credibility'. However, 'the Under Treasurer at the time, was no, no, no', the Treasury executive affirmed.

After the retirement of the Under Treasurer market-based reforms were extended to the management of public sector agencies with the aim of achieving better performance and promoting accountability. In this respect, the NT Government in 2002 introduced and mandated for all public sector agencies the financial and performance management framework titled 'Working for Outcomes' (WFO). The Government intended, from this framework, to provide agencies with the necessary tools to monitor, evaluate and enhance their performance by functioning under a business-like structure. This framework reflected the Government response to national calls for full commercial orientation.

The WFO framework, introduced the 'purchaser/provider' model which substituted the Government and its agencies' traditional collective relationship in public service delivery, by one that mirrored the market based relationship between businesses and customers. Under this new relationship, agencies produce outputs (services) and take on the role of a provider, and the Government purchases these outputs and fulfils the role of a purchaser. Figure 1 below provides an example of this relationship for an agency in the NT public sector. Under this relationship the Government wanted to create a new competitive setting by making agencies operate like independent businesses and to place them on an equal competitive footing with potential private suppliers. It was expected that agencies would, as a consequence, experience unprecedented pressure to improve performance and productivity in order to reduce cost and enhance quality, hence achieving value for money.

The purchaser/provider model was a performance management structure based on linking funding to outputs and results achieved. This should produce efficiencies if the outputs are directly relevant to the government policy objectives. The NT Government believed that linking funding to achieved results would bring a greater customer focus, enhance productivity, and promote accountability. This idea is based on the market principle where it is anticipated that customers pay businesses a price that is based on a specified quantity and quality for their goods and services (Adams and Embley, 1988; Kaplan and Norton, 1992; Kloot, 1999; Otley, 1999;

Williams, 1998). Similarly in the NT public sector, the funding of agencies was to be based on the price that is paid on behalf of the community for a specified output. Cost information has become more important and subject to increasing attention by Government agencies in ensuring quality service delivery at the best competitive price, especially as they became required to adopt full-cost pricing. The availability of cost information and its management became the key to achieving price competitiveness, though there was little competition of any kind in the NT. Agencies needed cost information in order to ensure their prices were cost-reflective and not under-costed. Ultimately, cost information was expected to help in achieving value for money by providing a basis for measuring agencies' performance and evaluating cost trends over time and by benchmarking these costs against other governments' providers or private competitors locally or across other jurisdictions.

[Insert Figure 1 here]

The first layer of the Figure depicts the vision, which generally reflects the policy of the Government that is mandated to the department to satisfy the needs of the community. The second layer, the outcomes, represents the objectives that the Department is responsible to achieve and these outcomes reflect the Government's policy direction. The third layer shows the output groups that highlight links and relationships between individual outputs and enable a strategic view of services. The fourth layer, Outputs, is meant to be the term that describes the goods and services produced by the department, and ideally these outputs should be uniform. However, in practice, many government services are not easily grouped in uniform outputs. For example, primary education is quite a general term and sub-outputs can be identified such as primary education to disadvantaged students. Under WFO it is important to identify outputs clearly as resource allocation decisions will concentrate on outputs and agencies will be funded for them. Performance indicators, in the last layer, reflect the performance of the department in delivering its listed outputs. These indicators assist different stakeholders and decision makers to determine whether value for money has been achieved. Hence the Government and the agency would set, for each output, a range of performance measures or benchmark indicators in terms of quantity, quality, cost and timeliness. These measures are the output characteristics that agencies are funded to achieve and accountable for (NT Treasury, 2003).

6 Paradox of the theory of commercial orientation and social responsibility

The previous discussions have indicated that public sector performance management has undergone reforms which aimed to foster a results-based management culture. Government agencies became required to report their financial as well as their non-financial performance against key measures (quantity, quality, cost, and timeliness) to demonstrate their efficiency and to discharge their accountability (NT Treasury, 2003). These measures have also been made the basis for budgeting and funding. Unlike the past, agencies became required to cover their costs and charge cost-reflective prices in their thrust for resource independence. Hence, they became required to operate on similar grounds to private sector institutions and to eliminate all traditional advantages resulting from Government ownership. Theoretically, this commercial orientation and its associated reforms represented an enormous departure from the past and implied that

Government agencies should become less socially and more economically-oriented in the sense that they would focus on activities that are economically effective and avoid many of those that are uneconomic even if socially necessary. But, how practical has this commercial orientation been in the NT? And how was it affected by the social responsibility of the Government?

The NT experience discloses substantial discrepancies between the intentions of the reforms and the practices that resulted. Evidence shows that there are several factors rooted in the economic environment that have weakened the intended results-focused culture. The following discussion shows the extent to which performance management has been applied in accordance with market principles, and the role of social responsibility in shaping this. Performance management under market principles was intended to achieve greater customer focus and improved performance through the use of full cost information for pricing competitiveness, benchmarking, performance evaluation, and resource allocation. But can this be achieved in an environment where there is little private sector activity?

Use of full cost information

The adoption of market-based practices by the NT Government, while not literally specifying profit as an aim for government agencies, has implied the necessity to attract and retain sufficient clientele in competing for resources (external revenues and government funding). In order to retain clientele, agencies needed to supply services at the right price and the right quality, which means that they needed to utilise their resources more efficiently. In this regard, accrual full-cost information became indispensable, to make agencies cost conscious in competing for resources with the limited pool of private providers. However, in addition to the absence of private sector providers from most industries, the Government prohibited agencies from competing with private business where it existed. This was to develop the private sector and to direct the resources needed for these investments into new areas. This situation has resulted in divergent goods and services been provided by the public and the private sectors and not contributed much to an overall increase in competition. This did not allow for a real test of price competitiveness to take place with all of its anticipated benefits in improved cost management and performance.

In addition, it was anticipated that cost and price information would be useful for performance evaluation through time and benchmarking against other providers, but many interviewees explained that such evaluation *'has never taken place'*. A departmental CFO stated, *'no single price review was done to see whether our prices improved or not'*. Another department's CFO added *'I am not aware that there has been any sort of in-depth evaluation on how agencies are actually costing or pricing their outputs'*. Some other executives have even expressed concerns regarding the reliability and consistency of this cost and price information and the basis for their determination. They revealed that prices were arbitrary and not associated directly with costs, and in some cases prices were determined based on similar prices in other states. An agency executive explained that every quarter the top administration in his department meets to review prices and adjust them in a way to avoid deficit at the agency level at large. This, sometimes, results in some services being priced at a profit and some others at a loss.

> *"Although not a formal pricing committee, the CEO and CFO set a price list for the services produced by the department every year and review them twice a year. In*

reviewing the prices, the committee assesses how each service division is performing in delivering its services in comparison with the estimated budget and they will adjust the prices accordingly. This means that if they see that the department as whole might be under budget in its estimated revenue, because of under estimation of revenue in some divisions or because the estimated work in divisions has not been coming in from clients, then they will try to adjust the prices up" An agency budgeting director.

"I could be under budget, others could be over budget, but the main thing is to be right at the agency level" A payroll manager.

Interviews revealed that in the NT the notion of cost recovery pricing was applied at the whole of the agency level rather than at the product or output level as was anticipated under the market model. Hence, in the absence of price reliability, price comparisons and benchmarking became largely irrelevant and meaningless with each agency having some 'loss leaders' and some high demand high price outputs which more than recovered their full cost.

Also, a number of interviewees indicated that the use of full cost as a performance measure was not as easy as the Government initially anticipated, with many indicating that '*some outputs are easy to cost and the majority are not'* and others *'some of the outputs are difficult to measure',* some of the more interesting specific comments were:

"The Government here and in other jurisdictions are realising that it is not as simple as it was first envisioned to cost outputs", The NT Auditor General.

"The relationship between outputs and dollars is still a very fragile relationship and it is really hard to find", A Treasury executive.

Interviewees indicated that there are a range of interpretation problems which impact upon the appropriateness of unit full-cost as a performance indicator. Some of these problems are generic ones that exist in other settings, such as measuring outputs. The non-physical nature of outputs – i.e. services – delivered by most government agencies made the measurement of output quantity difficult. This is because of the complexity of factoring the quality dimension of output into a quantity measure in the way in which consumer valuations of quality are factored into revenue measures in a market context. One executive stated *'Many of the agencies' outputs are difficult to quantify because of their non-physical nature, for example, 'policy advice' as an output for an agency, and 'health research' for another'* Another executive observed that *'The provision of these outputs draws on multiple service areas where the inclusion of overheads and indirect costs would require arbitrary allocations'*. This is the general problem of accrual accounting where many of the numbers do not have a clear empirical basis as they result from arbitrary allocations, even the notion of profit under the accrual system is not an empirical phenomenon because of these allocations. This inevitable arbitrariness, given real world uncertainty on the pattern of output over time, creates potentially serious distortions in full cost estimates (Kaplan, 1990; Robinson, 1998). In the NT the arbitrariness of cost allocation has been a great problem because of the absence of costing systems that allow the provision of full-cost information. A senior director stated that investing large amounts on costing systems that allow accrual full-cost information was not seen as a priority by the Government, which will not invest in the absence of a favourable 'cost benefit relationship', because:

> *"Operating in a budget like the NT budget, the department cannot afford to implement expensive software solutions that allow for the availability of such information",* A Health Department CFO.
>
> *"We do not have the skills, resources, and the capacity to develop the costing information needed",* A Health Department Director.

The NT Government saw that it is still responsible to deliver services at any cost because of the absence of other providers and hence it did not see value in investing in sophisticated costing systems. One director added that *'The management would not put in half a dozen system analysts to figure out best costing system and leave out services for communities that are needed'*. This situation resulted in unreliable and highly arbitrary cost figures being produced. This situation is probably best reflected by the comment of a high level agency director who, when asked about the basis of the cost figure, answered:

'We guess, we scratch, someone will sit down at night and try to work something out'.

This helps to explain why cost was not appropriately used in pricing and as a performance indicator in performance management.

Another more serious problem with using cost as an indicator for performance evaluation is that capital cost 'disabilities' will frequently raise unit capital costs and consequently unit full costs, because of reasons that have nothing to do with efficiency. Sources of capital cost disabilities include the lack of scale economies in smaller communities and higher capital costs in more remote areas in the Territory. The unique NT characteristics provide a good example for capital cost disabilities where actual costs for services are higher than in other jurisdictions. For example, the higher cost of labour and service delivery to remote areas would result in higher cost of the same output when compared across jurisdictions. The lack of belief in the cost figures being produced for agencies' outputs has raised concerns about its usefulness across agencies. Some directors argued that the cost measure '*did not add value to anyone*' and it has never been actually used as a performance indicator. Such a view, which appears to be prevalent across agencies, has led them to take the 'cost measure' out of their annual reports after it had been in place for a few years since the Working for Outcomes system was first introduced.

Resource Allocation

The use of the full-cost of output as the basis of resource allocation to agencies could mean that funding covers some of the accrual expenditures that constitute a part of the full cost of outputs. This means that agencies could receive cash for both their cash requirements during the year and at least some of their accruals that required future cash settlement. This kind of allocation could encourage behavioural change within agencies in managing resources as they became responsible for maintaining resources for their future needs to replace assets or to pay employee benefits (Blondal, 2004; Kelly and Wanna, 2004). However, detailed analysis of the NT budgets supported by interviews revealed that all appropriations excluded accruals for future expenditures because the Government wanted to avoid the risk associated with agencies spending the cash received for accrual items on unrelated initiatives and recurrent items, and also to maintain Parliament's control over capital acquisitions. As a result of this, two distinct types of appropriations became recognised, appropriations for capital assets' purchase and replacement, and output appropriations for the 'cash' requirements of recurrent expenditures, especially the production of outputs. Funds were never appropriated for the accrual items such as superannuation, and other employee entitlements. The cash disbursement for these expenses, when they fell due, was met directly by the Government through a special agency known as the Central Holding Authority. These appropriation arrangements showed that the effect of the traditional cash-based budgeting system was continued and the desired 'behavioural' change in managing resources did not take place. Interviewees explained that agencies do not get funded for the accrual cost of outputs but for their cash operating requirements.

Allocating funds based on the accrual cost of outputs was considered problematic for several reasons. First, the allocation of funds was subject to a political negotiation process between politicians and officials and it has been difficult to get politicians to agree on budgeted revenues and budgeted expenses prepared by agencies. Several senior public sector executives explained that budgeting in the NT starts from *'How much money the Government has available'* and what they can do with it to approach their outcomes. Therefore funding allocation decisions are influenced by the priority agenda of Government and subject to each portfolio's ministerial power in getting all or most of the funding requirement of agencies. Second, the difficulties in measuring agencies' outputs and the absence of informative costing systems have made output funding irrelevant. Using the cost of an output as a basis of output budgeting would require a clear definition of what constitutes a unit of each of the agencies' outputs. In the private sector, especially manufacturing businesses, there has not been such great ambiguity about product types and units of product because they are usually standardised types of products (such as a car, chair, book, and computer). Unfortunately, defining outputs and units of output in the public sector has been difficult mainly because these outputs are usually heterogeneous (not standardised) services. This is most obvious in services where there are considerable variations in the extent of resources required for the same unit of output. For example, each service within 'family reunification and reconnection' as an output for an agency, may have some variations between one case and another, as some families may need more extensive counselling and advocacy services than others. However, some agencies were able to overcome the problem of heterogeneity by using the 'average cost' per unit instead of the full cost of each unit of output. This meant that agencies would lose money each time they deliver a higher-cost unit of output, which will be offset by profits made from delivering lower-cost units of output. Such practice is likely to result in producing suboptimal concentration on quick and easy outputs to the detriment of the overall social goal of the agency. Third and most importantly, in the absence of private sector providers for many services, the NT Government did not abandon its social responsibility in providing services to accommodate economic efficiency. The Government believed that, in the absence of other providers, a necessary minimum amount of resources and services has to be maintained regardless of the output quantity produced or the lack of economies of scale.

The social sensitivity and closeness to the people of the Government in the NT makes service provision independent to some extent from the resources available in the budget. This is to say, that Government cannot close a particular division or service because the resources allocated ran out, nor it can stop treating a patient with a threatening condition because resources spent have reached the amount budgeted for such condition. The use of unit cost in budgeting did not show relevance in the public sector. Also, the increase in quantity for a particular output may require a funding increase but the decrease does not deserve a funding cut all the time. In service agencies that dominate the public sector in the NT, the unit cost is attributed mostly to fixed expenditures, including depreciation and personnel, which are not proportionally related to changes in output volume in most cases. Subsequently, an agency that achieves a lower quantity of outputs than initially funded does not necessarily deserve a funding cut, as this reduction may not affect the total cost of inputs required, and may not necessarily reflect an inefficiency of the agency in managing its funds but rather it may be because of the decrease in customers demand for a service with a high level of fixed costs. For example, a senior executive stated that *'if your output is the number of students and if you achieve that number you will get X amount of dollars, and even if the number of students has decreased you may still need the same amount of inputs (funds)'* to pay the cost of teacher salaries and to provide teachers for all children in the school system.

7 Discussion and Conclusion

The increasing reliance on market-based approaches in public service delivery has posed serious questions about the social responsibility of government. On one hand, market orientation was an approach to align government organisations with their external environment by making them 'customer oriented' and 'result focused' with all the implications for improved performance and efficiency. On the other hand, the social responsibility of governments required them to maintain a minimum and necessary investment on social rather than on economic grounds. This paper has shown something of the discrepancies between the rhetoric and the reality of market reforms in an environment where there is little competition and which is largely driven by social rather than economic imperatives. It should be of practical relevance to new jurisdictions in the region which are contemplating the adoption of accrual accounting and a market focus without having an economy with a strong private sector. Results indicate that the social responsibility of the Government in the NT, in an environment with little competition, has focused service delivery on providing a minimum level of social needs as a primary focus, rather than economic efficiency. This has made many market practices irrelevant in the context of the NT. This paper shows that the benefits of commercialization and of market practices cannot be taken for granted without considering the surrounding environmental conditions. There are many examples that show that actual implementation of market practices have been challenging and have produced limited results (Polidano, 2001; Siddiquee, 2010). Yet, the NT experience demonstrates another case where the implementation of market practices has been unsatisfactory, given that performance management and resource allocation decisions have remained unaltered.

Stakeholder theory suggests that an organization owes a duty to a range of people or groups that interact with the organization. Consequently, this paper has taken the view that it should help to explain the actions of the NT Government in adopting its working for outcomes (WFO) framework and accrual accounting. If these two developments were to realise improvements in the efficiency of government then a range of stakeholders would benefit. Territory residents (both human and corporate) would benefit directly if the government was able to provide more and better quality services through the extra resources generated by increased efficiency and the Government of Australia would benefit as it is the main provider of funding to the territory. Increased economic efficiency is in the interests of all Australian governments and people if it results in more resources being made available to all. Unfortunately, there was no evidence of an increase in efficiency associated with these developments and evidence of a tendency by all departments reviewed to revert to old practices so that the overall result was no improvement in performance management or stakeholder value.

Performance management reform in the NT has not achieved the intended results, due essentially to the close connection between government and community and the social responsibility recognised by the Government. The output-based performance management system has been introduced in a socio-economic context which is hardly supportive of output-based management, and as a result the management system has remained input based. Thus, Government service delivery in the NT has continued to be based on social rather than economic grounds and this has made agencies less concerned about their budgeted performance indicators in terms of quantity, quality, cost and timeliness. Results-based performance management, in terms of improved resource allocation and accountability, was not achieved given that resource allocation and funding were not based on actual performance and continued to be socially driven and subject to the traditional political negotiation process.

Full-cost information was a necessary but not sufficient key to the success of output performance management and market reforms. Such information was intended to be useful for reliable costing, pricing, benchmarking, resource allocation, and performance measurement with all of their implications for performance, efficiency, and effectiveness. However, the absence of a favourable ‘cost benefit relationship’ deterred the Government from investing in sophisticated costing systems that allow the availability of such information. The Government saw more value in directing funds to social needs than to costing systems that they believed not to be relevant and the Government did not see the relevance of cost information because of the absence of its usefulness in the NT context. The social mandate to continue service delivery at any cost, and the absence of a real market test of cost and price competitiveness due to the absence of private competitors were key aspects of this context.

The ‘multi-stakeholder’ responsibility and the accompanying ambiguity of the ‘multi-task objectives’ imposed upon Government organizations in the NT have resulted in some concerns regarding accountability and performance management, these concerns are:

Trade-offs: The requirement of government organizations to attend to the interests of multiple stakeholders in an environment where both social and economic performance is evaluated would provide them with an opportunity to escape accountability from their own failings. For example, agencies may explain additional expenditures in meeting a particular activity as the ‘cost’ of meeting a social necessity in a very small community (Heath and Norman, 2004; Stiglitz, 1989).

Performance evaluation and benchmarking problem: Evaluating the performance of government organizations that operate in an economic environment that has a single measure of performance based on market principles is quite possible. However, in the context of the NT, where government organizations have objectives which are both social and economic, such an evaluation of performance was not relevant because the basis for comparison disappears as these organizations have different operating environments which are not comparable to that for organizations that focus on profitability as the sole objective. Hence, performance information about NT government agencies, that provide services based on an inclusive rather than an exclusive basis and on social rather than economic imperatives, would not be comparable with that for agencies that are solely profit oriented (Carlin and Guthrie, 2001; Guthrie, 1994; Guthrie et al., 1999).

Redistribution: Government organizations in the NT were expected to help the Government to achieve its redistributive goals. Hence they were expected to provide all services across all the Territory on an inclusive basis even in the absence of economies of scale in remote and rural areas (Hayek, 1994; Gibson, 2005).

Macroeconomic Issues: Because of the limited private investments government organizations in the NT were required to help the Government to develop the NT economy by facilitating private investments. Hence, government agencies were expected to abstain from investments that profit-seeking private providers would engage in (Hayek, 1994; Heath and Norman, 2004).

The experience in the public sector in the NT shows that it is challenging to effectively apply performance management structures under market conditions while government organizations still hold a comprehensive 'social responsibility' mandate to the community. The absence of the private sector in most industries and especially in rural areas made the NT Government organizations operate with an eye to their social mandate first and then their financial performance. This was played out across the NT to the advantage of the social mandate over the investment in performance management systems.

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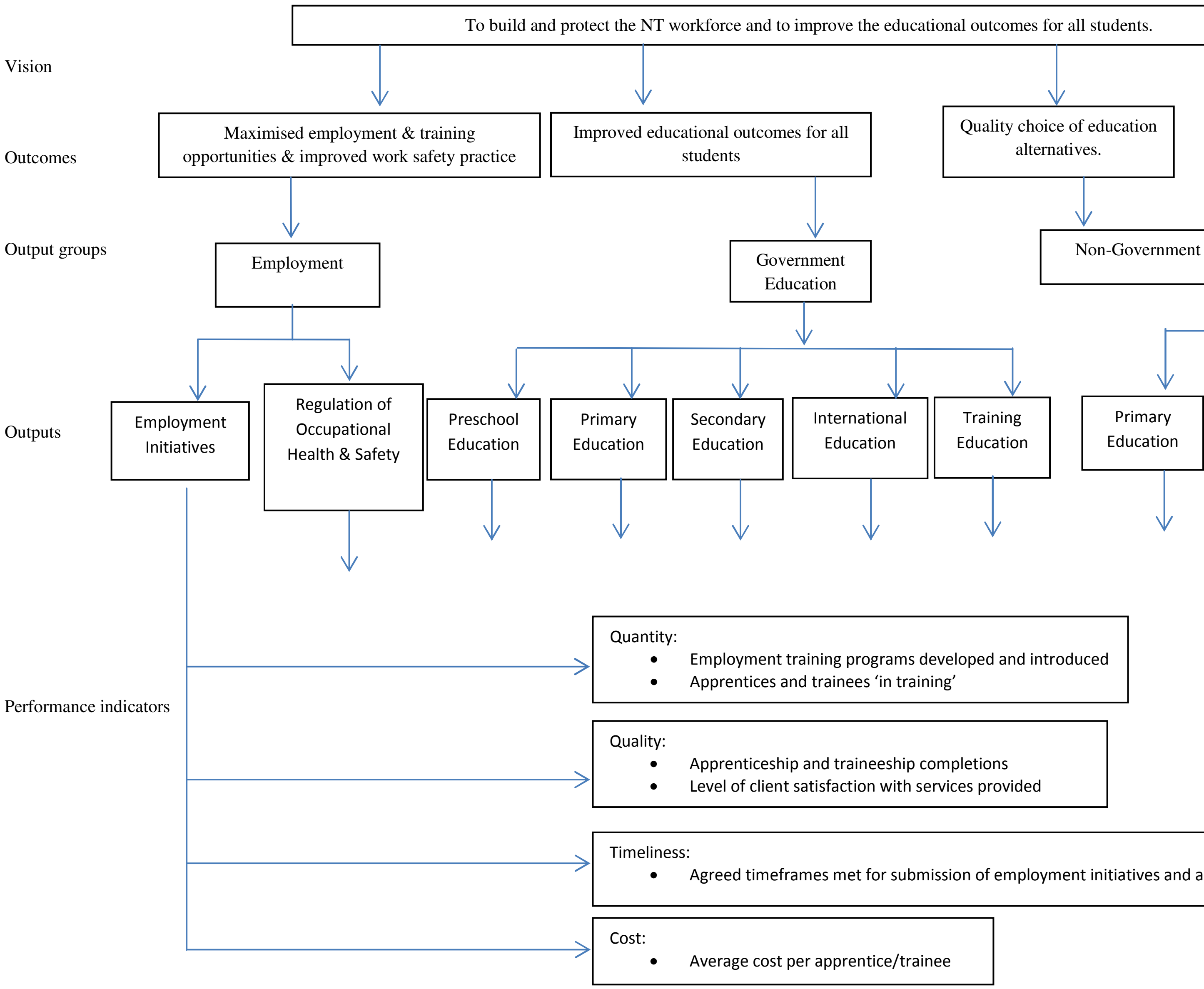
Figure 1



To build and protect the NT workforce and to improve the educational outcomes for all students.
Vision
Outcomes
Maximised employment & training opportunities & improved work safety practice
Improved educational outcomes for all students
Quality choice of education alternatives.
Output groups
Employment
Government Education
Non-Government
Outputs
Employment Initiatives
Regulation of Occupational Health & Safety
Preschool Education
Primary Education
Secondary Education
International Education
Training Education
Primary Education
Performance indicators
Quantity:
Employment training programs developed and introduced
Apprentices and trainees 'in training'
Quality:
Apprenticeship and traineeship completions
Level of client satisfaction with services provided
Timeliness:
Agreed timeframes met for submission of employment initiatives and a
Cost:
Average cost per apprentice/trainee