

# **THE ROLE OF PERFORMANCE BASED BUDGETING IN THE INDONESIAN PUBLIC SECTOR**

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## **Declaration Page**

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I certify that the research described in this thesis has not already been submitted for any other degree. I certify that to the best of my knowledge that all sources used and any help received in the preparation of this dissertation have been acknowledged.

**Signature: Andy Dwi Bayu Bawono (Student ID: 42307023)**

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## ABSTRACT

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Performance-Based Budgeting (PBB) has been, and continues to be, implemented within developed and developing countries as part of a wider public sector reform process. The purpose is to embed accurate performance measurement within public sector organisations (see Franklin, 2006, Aristovnik and Seljak, 2009, Schick, 2007) and provide a more efficient and effective approach to resource allocation (Shah and Shen, 2007). PBB adoption and implementation has not been without criticism and there is ongoing debate as to the real use and effectiveness of PBB. The historical context within which PBB developed, and the justification for why countries decide to implement PBB, has been the subject of scant research, which has led to a lack of understanding as to its purpose and effects.

This thesis undertook an historical examination of PBB as part of fiscal reform within the public sector. It specifically used a case study regarding the adoption and implementation of PBB within the Indonesian government as its central field of analysis. The study used qualitative research methodology, beginning with a historical review of the evolution of PBB as the new public budgeting system, using the Lüder FMR model (2002) as a conceptual framework. It then utilized new institutional sociology (NIS) theory as a theoretical framework to examine the extent to which isomorphism was evident during PBB implementation within the Indonesian central government. Finally, the Lüder FMR model (2013) was employed as a conceptual framework to investigate the motives that underpinned the development of PBB within Indonesian local government, and the factors influencing its implementation.

This study offers three conclusions about the historical context of PBB evolution and the decision by countries to adopt. First, PBB was initially implemented in the United States in 1949 and expanded to developing countries through United States (US) and United Nations (UN) funded projects. Using the Lüder FMR model (2002), this study finds that the primary motive underpinning PBB implementation in the US was public sector demand for more informative and measured budgets. Similar motives were also found in the UK, Australia and Denmark. That the implementation of PBB within the US and UK budgeting systems were largely seen as positive, was the primary stimulus for PBB implementation across the globe. Furthermore, this study found the outcome of budgetary reform varied between countries, from that of a single format that involved traditional budgeting methods, to 'old PBB', to a dynamic approach involving multiple stages that culminated in PBB modification.

Second, the change to the budgetary system was a consequence of the Indonesian central government's institutional environment. Two phases of PBB implementation occurred within the Indonesian central government. In the initial period (1990s), most of the impetus for change originated from Indonesian technocrats (internal governmental officers and academics) who proposed PBB after their participation in an international public sector workshop. During the second period (2003), pressure to implement PBB emanated from the IMF and the World Bank, and the Indonesian central government responded to moderate coercive pressure with an avoidance strategy. This avoidance response, coupled with the occurrence of weak mimetic and strong normative pressure (from Indonesian technocrats) in the institutionalisation of PBB, is evident through the modified form of PBB implemented across the Indonesian central government. This avoidance strategy appears to be the result of the Indonesian government seeking legitimacy from the international community rather than the rational motive of gaining efficiency.

Third, the primary motivation for PBB implementation within Indonesian local government was the demand to modernise its financial and reporting system, with support from Indonesian technocrats (government officers and scholars) and foreign donor projects. The harmonisation of planning, budgeting and accounting helped to embed reform. Furthermore, the study found that the Lüder FMR model (2013) is a useful framework to identify the key factors (such as stimuli, reform driver and promoters, and structural features) behind the implementation of PBB within Indonesian local government. However, the weak performance identified after PBB implementation indicated that budgeting reform was at least partly cosmetic.

In practical terms, the Indonesian experience of PBB implementation has lessons for other developing countries who are adopting or intend to adopt and implement PBB.

## Table of Contents

Declaration Page .....	ii
Acknowledgement .....	iii
ABSTRACT.....	v
Table of Contents .....	vii
List of Figure .....	xii
List of Table.....	xiii
List of Acronyms and Abbreviations .....	xiv
1. Introduction .....	1
1.1 Overview .....	1
1.2 Public Sector Budgetary Reform .....	6
1.3 Research Methodology .....	12
1.4 Conceptual and Theoretical Framework .....	15
1.4.1 <i>The Lüder Financial Management Reform Process (FMR) Model</i> .....	16
1.4.2 <i>New Institutional Sociology Theory</i> .....	20
1.5 Overall Introduction .....	24
1.6 References .....	25
2. Paper 1: A Conceptual Framework for Budgetary Reform within Public Sector Organisations.....	31
2.1 Abstract.....	31
2.2 Introduction and Purpose.....	32
2.3 The Budgetary Context .....	33
2.4 What is Reform?.....	36
2.4.1 Public Sector Reform .....	37
2.4.2 Public Sector Management Reform.....	38
2.4.3 Public Financial Management Reform .....	39
2.4.4 Accounting Reform .....	40
2.4.5 Budgetary Reform.....	41
2.5 Budgeting in the Public Sector .....	42
2.6 What is Performance-Based Budgeting? .....	46

2.7 The Lüder Financial Management Reform Process Model .....	49
2.7.1 Stimuli .....	51
2.7.2 Reform Drivers .....	52
2.7.3 Political Reform Promoters .....	53
2.7.4 Institutional Arrangements .....	54
2.7.5 Stakeholders .....	55
2.7.6 The Reform Concept.....	56
2.7.7 Implementation Strategy .....	56
2.7.8 Outcome of the Reform .....	57
2.8 The Historical Development of Performance-Based Budgeting .....	57
2.8.1 1940s-1960 .....	58
2.8.2 1960s-1980s .....	61
2.9 The Lüder FMR Analysis .....	67
2.9.1 The Stimuli .....	67
2.9.2 Reform Drivers .....	67
2.9.3 Political Reform Promoters .....	68
2.9.4 Institutional Arrangements .....	68
2.9.5 Stakeholders .....	69
2.9.6 Concepts of Reform .....	70
2.9.7 Implementation Strategy .....	70
2.9.8 Outcome of the Reform .....	71
2.10 Conclusions.....	72
2.11 References.....	74
3. Paper 2: The Transformation of Indonesia's Central Governmental Budgetary System .....	82
3.1 Abstract.....	82
3.2 Introduction and Purpose.....	83
3.3 Performance-Based Budgeting .....	85
3.4 Theoretical Framework .....	91
3.4.1 Coercive Pressures .....	94
3.4.2 Mimetic Pressures.....	94
3.4.3 Normative Pressures .....	95



3.4.4	NIS and Public Sector Organisations.....	95
3.5	Research Method .....	97
3.6	An Historical Overview of Indonesian Public Sector Budgeting.....	100
3.7	Institutionalism of PBB within Indonesian Central Government Budgeting	107
3.7.1	Coercive Pressures .....	107
3.7.2	Mimetic Pressures .....	113
3.7.3	Normative Pressures .....	116
3.8	The implementation of PBB within the Indonesian Central Government ...	121
3.9	Conclusions, Implications and Limitations .....	125
3.10	References .....	131
4.	Paper 3: The Implementation of Performance-Based Budgeting within Indonesian Local Government .....	138
4.1	Abstract.....	138
4.2	Introduction .....	139
4.3	Performance-Based Budgeting in Public Sector Organisations .....	142
4.4	Conceptual Framework .....	146
4.4.1	Stimuli .....	148
4.4.2	Structural Features.....	148
4.4.3	Project-Specific Contextual Factors .....	149
4.4.4	Political Promoters.....	150
4.4.5	Reform Drivers .....	150
4.4.6	Epistemic Communities .....	151
4.4.7	Institutional Opponents.....	152
4.4.8	Information Producers and Users .....	152
4.4.9	Initiation.....	152
4.4.10	Conceptual Design.....	153
4.4.11	Implementation .....	153
4.4.12	New System .....	154
4.5	Research Method .....	155
4.6	A Historical Overview of Indonesian Local Government Budgeting .....	157
4.6.1	Indonesian Government System Prior Budgeting Reform .....	157

4.6.2	Budgeting Reform in the Indonesian Local Government .....	159
4.7	The Factors Influencing Indonesian Local Government Budgeting Reform ....	168
4.7.1	Stimuli .....	170
4.7.2	Reform Drivers .....	171
4.7.3	Structural Features.....	173
4.7.4	Project-Specific Contextual Factors .....	176
4.7.5	Initiation.....	178
4.7.6	Conceptual Design.....	178
4.7.7	Implementation .....	179
4.7.8	New System .....	179
4.8	Conclusion.....	180
4.9	References.....	185
5.	Conclusion .....	191
5.1	Overview .....	191
5.2	Summary of Findings .....	193
5.2.1	Budgetary Reform within Public Sector Organisations .....	194
5.2.2	The Transformation of Indonesian Governmental Budgetary System .....	196
5.2.3	The Implementation of Performance-Based Budgeting within Indonesian Local Government.....	197
5.3	Reflections on Lüder's Financial Management Reform Process Model .....	198
5.4	Reflections on New Institutional Sociology Theory .....	200
5.5	Implications of the Study .....	201
5.6	Recommendations .....	203
5.7	Limitations .....	204
5.8	Directions for Future Research .....	204
5.9	Overall Conclusion.....	205
5.10	Reference .....	206
	Full Reference List .....	208
	Appendix 1: Table of Application of the Lüder model (FMR and LCM) .....	224
	Appendix 2: Coding for the Transformation of Budgetary Reform in the Indonesian Central Government.....	225
	Appendix 3: Example of Central Government Budget Plan Using PBB.....	227

Appendix 4: Central Government Expenditure Classification (Line-item) .....	228
Appendix 5: Example of Local Government Budget Plan Using PBB .....	230
Appendix 6: Example of Budget Classification Using PBB .....	231
Appendix 7: Example of Local Government Budget Plan Using PBB .....	232
Appendix 8: Example of Budget Classification Using PBB .....	233
Appendix 9: The Interview Guide for Paper Two: Performance-Based Budgeting Implementation in the Indonesian Central Government .....	234
Appendix 10: The Interview Guide for Paper Three: The Implementation of Performance-Based Budgeting within Indonesian Local Government .....	237
Appendix 11: An Approval Statement of the University Human Ethics Committee for Paper Two .....	241
Appendix 12: An Approval Statement of the University Human Ethics Committee for Paper Three .....	242
Appendix 13: Participant Information and Consent Form (Paper 2) .....	243
Appendix 14: Participant Information and Consent Form (Paper 3) .....	245

## List of Figures

Figure 1: Financial Management Reform Process Model	17
Figure 2: The Financial Management Reform Process Model (Actors – Process – Context modules) from Lüder (2013)	19
Figure 3: Focus of Budgeting: Performance Measurement Type	48
Figure 4: Financial Management Reform Process Model	50
Figure 5: Decentralisation vs PBB implementation in Indonesia	105
Figure 6: The Financial Management Reform Process Model (Actors – Process – Context modules)	147
Figure 7: Author's Elaboration of a New Financial Management Reform Process Model (Actors – Process – Context modules) in the Indonesian Local Governments Budgeting Reform (an Adoption of PBB)	169

## List of Tables

Table 1: Research Outline	4
Table 2: Number of Participants by Institution	15
Table 3: Summary of Thesis	192

## List of Acronyms and Abbreviations

ADB	Asian Development Bank
ARC	Administrative Reform Commission (India)
AusAID	Australian Agency for International Development
BAS	<i>Bagan Akun Standar</i> (Account Standard Chart)
BAPA	Budget and Accounting Procedure Act (USA)
BIGG	Building Institutions for Good Governance
BPKP	<i>Badan Pengawas Keuangan dan Pembangunan</i> (Financial Development and Supervisory Agency, Indonesia)
CIDA	Canadian International Development Agency
CIGAR	Comparative International Governmental Accounting Research
CIMA	Chartered Institute of Management Accountants
CTA	Cash Toward Accrual
FAA	Full Accrual Accounting
FASAB	Federal Accounting Standards Advisory Council
FMI	Financial Management Initiative
FMIP	Financial Management Improvement Program
FMR	Financial Management Reform
GASC	Governmental Accounting Standard Committee ( <i>Komite Standar Akuntansi Pemerintahan</i> ) (Indonesia)
GPRA	Government Performance and Results Act (USA)
GR	Government Regulation ( <i>Peraturan Pemerintah</i> )
GTZ	<i>Deutsche Gesellschaft für Internationale Zusammenarbeit</i> (German Organisation for Technical Cooperation)
IAI	<i>Ikatan Akuntan Indonesia</i> (Indonesian Institute of Accountants)
IBS	Integrated Budget System (Philippines)
ICAC	Institute of Chartered Accountants of Ceylon
ICMA	International City/ County of Management Association

IMF	International Monetary Fund
KSAP	<i>Komite Standar Akuntansi Pemerintahan</i> (GASC) [the Governmental Accounting Standard Committee]
LAKIP	<i>Laporan Akuntabilitas Kinerja Instansi Pemerintahan</i> [Government Agency Performance Accountability Report]
LAN	<i>Lembaga Administrasi Negara</i> [State Administration Office]
LCM	Lüder Contingency Model
LGSP	Local Governance Support Program
LoI	Letter of Intent
MBO	Management by Objectives
MBS	Modified Budget System (Malaysia)
MoF	Ministry of Finance
MoHA	Ministry of Home Affairs
MTEF	Medium Term Expenditure Framework (Indonesia)
NDI	National Democratic Institute
NGO	Non-government organisation
NIS	New Institutional Sociology Theory
NPFM	New Public Financial Management
NPM	New Public Management
NSA	National Security Act (USA)
NSW	New South Wales
OECD	Organisation for Economic Cooperation and Development
OMB	Office of Management and Budget (USA)
PAP	Program, Activity, and Project
PBB	Performance Based Budgeting
PFM	Public Financial Management
PMB	Program Management and Budgeting (Australia)
PPB	Programme and Performance Budgeting
PPBS	Planning Programming Budgeting System
SAKIP	<i>Sistem Akuntabilitas Kinerja Instansi Pemerintah</i> [Government Agency Performance Accountability System]

SAP	<i>Standar Akuntansi Pemerintahan</i> [Governmental Accounting Standard]
UK	United Kingdom
UN	United Nations
UNDP	United Nations Development Programme
UNP	United National Party (Sri Lanka)
US/USA	United States/United States of America
USAID	United States Agency for International Development
UU	<i>Undang-undang</i> (Law)
VNG	<i>Vereniging van Nederlandse Gemeenten</i> [Netherlands Association of Municipalities]
ZBB	Zero Based Budgeting



# **1. Introduction**

This chapter provides an overview of a study of performance-based budgeting (PBB) in Indonesia, including the motivation for and background to the research, and establishes the overarching research questions and aims. This thesis takes the form of a thesis by publication, constituting three separate research papers. An overview of the thesis and the themes of the papers is provided in this chapter. It shows how they are interrelated in order to build a coherent account of the process of PBB implementation across selected countries, and specifically within the Indonesian public sector. The chapter also explains the research methods used to collect and analyse the data, and contains an overview of the theoretical perspective taken in the analysis of the adoption and implementation of PBB. The following section gives an overview of the research field, including motivation and background information, and the themes of the individual papers.

## **1.1 Overview**

This study undertook an historical examination on the evolution of PBB within the public sector. Specific emphasis was placed on the adoption and implementation of PBB within the Indonesian government, as a developing country case study. This research was designed to create new knowledge about the historical development of PBB by examining its implementation as part of fiscal reform within the Indonesian public sector. This study makes an important contribution to the management accounting literature on budgeting systems through the application of the Lüder financial management reform (FMR) process model (Lüder, 2000; 2013) as a conceptual framework and new institutional sociology (NIS) theory (DiMaggio and Powell, 1983; Meyer and Rowan, 1977) as theoretical frameworks.

Performance-based budgeting has become the dominant budgeting system in many countries that have sought to measure public sector performance. It is an efficient

and effective approach to resource allocation (Shah, 2007). PBB has a clear focus on resource allocation in order to measure outputs and/or outcomes using performance information within budget documents. Researchers believe that PBB has the ability to address traditional budgeting weaknesses, such as information being presented via inputs or resources purchased (Curristine, 2005; Melkers and Willoughby, 2001). Researchers have argued that PBB seeks to improve accountability, efficiency and performance in government budgeting and develop the capability of departments or agencies within government to compete for budgetary allocations using performance information (Curristine, 2005; Joyce, 2011; Walker, 2002).

However, PBB adoption and its implementation has not been without criticism. This adoption of PBB requires an assessment of the design, implementation approach, use and impact that PBB will have on the government budgeting system. Moynihan (2006) indicated that many decisions surrounding the use of performance information are still made for political reasons and are not entirely factually based. Furthermore, Lu (1998) argued that how public sector organisations use performance information and performance measurement in the budgeting process remains unclear. Some researchers (Melkers and Willoughby, 2001; Andrews, 2004) have found that parliamentary budget committees rarely use performance information in deciding to approve government budgets. Moreover, the link between performance budgeting and budgetary decision-making and outcomes is debatable. Jordan and Hackbart (2005) found assessing management outcomes and budgetary processes difficult due to inaccurate performance data captured in budgeting systems. Furthermore, Kelly (2003) questioned whether PBB was warranted and whether traditional budgeting was problematic for public sector budgeting. Although PBB is intended to replace traditional budgeting within government, line-item and incremental formats (parts of traditional budgeting) are still being used in conjunction with PBB in several countries, including the United States and Greece (Schick, 2001; Andrews, 2004; Karkatsoulis, 2010; Aristovnik and Seljak, 2009). Consequently, doubts persist as to whether PBB constitutes a suitable budgetary replacement for traditional budgeting. In the context of PBB

implementation across countries, a research problem arises in that we do not understand the historical context in which PBB developed from traditional budgeting. Ongoing criticism surrounding PBB implementation has led to questions as to the motives for its adoption in various countries, which this study sought to address.

Although the relevance and purpose of PBB is still debatable, the Indonesian government in principle adopted it as its primary budgeting system in the early 2000s. This came about due to the fall of the Suharto regime in 1998, which led Indonesia to seek reforms in its political system. This 'reformasi' transition from authoritarianism ('new order' era – *era Orde Baru*) to the post-Suharto democratic era has been termed 'reform order' (*Orde Reformasi*) (Harun, 2007; Hadiz and Robison, 2005). Following political reform there was greater focus on financial management, and consequently the Indonesian government moved from traditional budgeting to PBB. Whilst Indonesia is still experiencing the effects of the early stages of PBB implementation, as indicated by officers within the Indonesian Ministry of Finance (Salim and Eckardt, 2008), it is a useful case study for the examination of whether PBB implementation is problematic or conducive to developing countries that are also in political transition.

This study examined the evolution of PBB from an historical perspective, as part of public financial management reform, across several countries from approximately 1949 to 1989. In building upon prior work exploring the many issues that influenced the adoption and implementation of PBB within developing countries, this research examines how and why PBB occurred in Indonesia. The research focused on the motivation for and implementation of budgetary reform across Indonesian government at both the central level from 2003 to 2010 and local level from 1999 to 2010. Although this study placed most emphasis on government budgeting reform between 1999 and 2010, analysis extended to the beginning of the 1970s, because this is when Indonesian public sector management reform was first initiated (Harun, 2012). Thus, the historical approach was useful in enhancing our understanding of

the contextual factors shaping Indonesian budgeting reform during the ‘new order’ period.

As previously mentioned, this thesis follows Macquarie University’s thesis by publication format, which includes three individual research papers, written in publication format but not necessarily published, that together constitute a specific research project. Details of the three papers are outlined in Table 1 below:

**Table 1. Research Outline**

<b>THE ROLE OF PERFORMANCE-BASED BUDGETING IN THE INDONESIAN PUBLIC SECTOR</b>		
<b><u>Paper 1:</u></b>  A Conceptual Framework for Budgetary Reform within Public Sector Organisations	<b><u>Paper 2:</u></b>  The Transformation of Indonesia’s Central Governmental Budgetary System	<b><u>Paper 3:</u></b>  The Implementation of Performance-Based Budgeting within Indonesian Local Government
<b><u>Research Questions:</u></b>  1. When and why did public sector organisations within nation states implement PBB in their budgetary reforms? 2. Which reform drivers and institutional arrangements helped shape the decision by various governments to implement PBB? 3. What and why did public sector organisations and governments encounter barriers to PBB implementation during the budgetary reform process?	<b><u>Research Question:</u></b>  How and why did the Indonesian Central Government focus on implementing PBB as the new budgeting system from 2003 to 2010?	<b><u>Research Question:</u></b>  How and why did Indonesian local governments reform their budgeting system using PBB during 1999–2010?
<b><u>Design/methodology/ approach:</u></b>  <ul style="list-style-type: none"> <li>• Lüder FMR model (Lüder, 2002).</li> <li>• Secondary data material obtained from public sector journals and literature, OECD publications and reports, international organisational publications and reports, and archival material including government legislation and promulgations.</li> </ul>	<b><u>Design/methodology/ approach:</u></b>  <ul style="list-style-type: none"> <li>• NIS on isomorphism and institutional pressure for budgetary reform (DiMaggio, 1983; Meyer, 1977).</li> <li>• Primary data material obtained through interviews and archival material including government reports and regulations, international organisational publications, foreign project reports, and academic literature.</li> </ul>	<b><u>Design/methodology/ approach:</u></b>  <ul style="list-style-type: none"> <li>• Lüder FMR model (Lüder, 2013).</li> <li>• Primary data material obtained through interviews and archival material including government reports and regulations, international organisational publications, foreign donor project reports, and academic literature.</li> </ul>

**Paper 1 A Conceptual Framework for Budgetary Reform within Public Sector Organisations** provides an historical examination of the evolution of PBB, as part of public financial management reform, across a number of countries from 1949 to the late 1980s. This period was known as the era of 'old PBB' (Shah and Shen, 2007; Jones and McCaffery, 2010). This paper contributes to the literature through its utilisation of the Lüder FMR model (2002) within a budgetary reform (evolution of PBB) perspective, as prior researchers (see Jorge, 2003; Abushamsieh, 2013a; 2013b; Lüder, 2002) have used the model primarily within the context of accounting reform.

**Paper 2 The Transformation of Indonesia's Central Governmental Budgetary System** examines the history of the adoption and implementation of PBB as a budgeting system within the Indonesian central government. This paper contributes to the literature on institutional theory, specifically with regard to institutional pressure in the embedding of PBB in Indonesia, and the Indonesian central government's response to these pressures.

**Paper 3 The Implementation of Performance-Based Budgeting within Indonesian Local Government** enhances our understanding of the motives, reform drivers and institutional arrangements that facilitated the decision by Indonesian local government to implement PBB. This paper also contributes to the literature regarding the utilisation of the Lüder FMR model (2013) within a developing country budgetary reform (evolution of PBB) perspective.

In summary, the three papers focus on the motives behind the adoption and implementation of PBB within government, particularly within central and local government in Indonesia. Investigating the motives for PBB adoption and implementation is critical in understanding the degree to which budgeting reform can be externally imposed as opposed to emerging organically within organisations. This allows a better understanding of the factors that enable or inhibit the permeation of reform through an organisation and through levels of government. Whether PBB is merely given lip service or whether it is genuinely perceived,

understood and implemented effectively, often depends on localised factors unique to each country, despite international pressure for adoption (Robinson, 2007). Indonesia, as a developing country undergoing political, economic and social transition at national, provincial and local levels, represents a unique setting in which to understand how budgetary reform occurs.

## **1.2 Public Sector Budgetary Reform**

This section reviews literature that examines the traditional (previous) budgetary system, and critiques of its implementation in the public sector, and the nature of PBB as a new budgeting system and its application as part of budgetary reform. This is fundamental in order to study how and why PBB developed as a replacement for traditional budgeting across countries, and in particular, in the Indonesian public sector at the national and local level. This literature review outlines the definition and model of PBB and its implementation within countries.

For over a century, governments in many countries – including the United States of America (USA), the United Kingdom (UK), Australia, New Zealand, and the Netherlands – utilised a traditional approach to budgeting, due to its simplicity and stability, when deciding on policy outcomes (Jones and McCaffery, 2010, Schick, 1998). However, the traditional budgeting format, including annual, line-item and incremental budgeting, has been the subject of criticism. In several countries (e.g. USA, Singapore, Malaysia, Philippines, Sri Lanka, New Zealand) these budgeting forms were seen as inefficient and ineffective, failing to focus on the demands for governmental management practices in a modern competitive environment (see Hope and Fraser, 1999; Mascarenhas, 1996; Jones and McCaffery, 2010; Dean, 1986a; 1986b; 1986c; Schick, 1998; McNab and Melese, 2003). These budgeting forms have been criticised for being irrational given that they focus merely on organisational resource (staff, material, money and equipment) utilisation instead of the achievement of organisational objectives (Kelly, 2003; Wildavsky, 1978). Furthermore, the traditional budget only formulates and forecasts budgets for a

single year (annual budget), which results in fragmentation of budget appropriations that are not matched with organisational programs that extend beyond 12 months (Wildavsky, 1978). Thus, traditional budgets result in problems in controlling the budget allocations of longer-term government programs. Consequently, budget duplication and overlapping are difficult to control because of their fragmentation and annual estimations, which create budget inefficiencies (Caiden, 1982).

Other traditional line-item budgeting criticisms relate to revenues and expenses that are separated into specific items, including wages, maintenance and travel (Schick, 1966). These categories are a carryover from historical practice, rather than being based on contemporary logic, as there is a lack of analysis as to whether each item is necessary as a line item, and/or whether the proposed expenditure or revenue in each item is allocated efficiently. Under traditional line-item budgeting the reallocation of funds within items is forbidden, which leads to inefficiencies and ineffectiveness as unused funding will be lost or reduced in the following budget year. The implication is that government managers will seek to spend all budget line items to ensure that each item is retained at the same level in the following budgetary year (Robinson, 2007; Osborne, 1993).

Although incremental budgeting is the easiest way to forecast a budget's movement by increasing and/or decreasing revenue and expenditure based on the previous year's budget (Kelly, 2003), this form has been criticised as being unable to provide a comprehensive review of activities. As funding is allocated based on line items in the previous budgetary year, not current activity requirements, budget allocations for new activities are difficult to decide if similar budget allocations occur every year. A conservative mindset is inherent in this practice. It does not support risk-taking and results in public budgets being ineffective (Bragg, 2013; Wildavsky, 1978; Khan and Hildreth, 2002).

The literature reviewed above supports the argument that traditional budgeting contributes to both inefficiencies and ineffectiveness within public financial management. To address and eliminate these problems using performance information, PBB emerged as a new budgeting form in many countries (see Dean, 1986a; Jones and McCaffery, 2010; Ho, 2011).

There is no single definition of PBB, nor is there a distinct model of PBB. The Organisation for Economic Co-operation and Development (OECD) suggests three categories of PBB: presentational performance budgeting, performance-informed budgeting and direct-performance budgeting (Curristine, 2005). A detailed explanation of these categories is given in paper one. The OECD also argues that PBB is a form of budgeting that links the allocation of funds to measurable results (Anderson, 2008). Additionally, Carter (1991) argued that performance budgets use mission statements, goals and objectives to explain how funds are disbursed and the approach used to allocate resources in order to achieve measured outcomes. However, the implementation of PBB refers to the integration of performance information into the annual budget process or to the allocation of resources (Aristovnik & Seljak, 2009).

Studies examining the implementation of PBB post-1980 have largely occurred within OECD member countries, including New Zealand, Australia, Denmark, Sweden, the USA, the UK, Mexico and Greece. According to Curristine (2005), the implementation of PBB in OECD countries varies in both technique and form. For instance, New Zealand was the first OECD member to successfully implement PBB, largely through contracts negotiated between the government or the minister and the relevant departments or agencies. The contract specifies that the government or ministry will provide a budget allocation, and the department will perform services as outlined in the budget (e.g. the provision of road services, health services and early childhood education). In the contract format, the government acts as the purchaser of departmental products. The department or other entities act as suppliers, and every year, hundreds of contracts are assigned (Pallot, 2002; Schick,



1998). Based on the Public Finance Act in 1989, New Zealand implemented the corporate accounting framework within its government finances to improve performance measurement, which constitutes part of the PBB implementation process. The success of PBB in New Zealand is attributed to being able to measure outputs and outcomes and capitalising on their links to inputs (Schick, 2001b).

In the Netherlands, PBB was implemented as a form of *Van Beleidsbegroting tot Beleidsverantwoording* (the policy budgeting to policy responsibility) that improves budget transparency and accountability, and makes the policy more results-oriented. As a consequence, the policy and the budget are more tightly interconnected (Van Nispen & Posseth, 2006). Sweden and Denmark employ a non-formal approach to the utilisation and development of performance information in budget negotiations with their Ministries of Finance (MoF) (see Blöndal & Ruffner, 2004). Denmark employs resource-based contract management that contains three aspects: target setting, contract development and annual reporting. One of the critical success factors for Denmark was considerable political support, as there was no direct intervention by politicians in the budget negotiation between the government and its agencies. Furthermore, the success of PBB implementation in Denmark is due to a strong alignment between resource allocation measurement and performance management (Ginnerup et al., 2007).

In Sweden, the government required performance information as a foundation for budget allocations, and as a basis for both demanding accountability from government agencies and for control. Contracts exist between the government and agencies to deliver health, preschool, police and educational services. In addition, agencies implement performance information as a part of their internal control (Küchen & Nordman, 2008; Wehner, 2007). Australia's form of PBB uses integrated performance information in the budgetary process. The implementation is supported by agreements for resource allocation and distribution between the Commonwealth's Finance and Administration Department and other relevant departments or agencies. One advantage of this form is that the government has

better access to performance information for the decision-making phase of the budget. This form also ensures that interrelationships between performance and the other aspects of the financial, political, accountability and management environment are maintained (OECD, 2007).

Despite the abovementioned widespread implementation of PBB, problems associated with its implementation have been documented in several countries. For instance, Danish PBB implementation was hampered by a lack of performance data from the National Board of Statistics (Ginnerup et al., 2007; Blöndal & Ruffner, 2004). The Swedish government experienced difficulties due to few links between performance management and financial and budgetary control. A long process relating to budget revision at the legislative level reduced coordination of performance management efforts in government offices (Küchen & Nordman, 2008; Wehner, 2007). In addition, some problems were encountered during PBB implementation in Australia, including difficulties in gaining access to performance information, contributions to output, and limited evidence as to which information outputs and outcomes contributed toward managerial decision-making (OECD, 2007).

Several developing countries experienced difficulties in PBB implementation. In Mexico problems emerged around 2005, including a failure to measure the outputs, outcomes or impacts performance, and an overall weakness in being able to evaluate performance indicators in decision-making (OECD, 2009). Greece failed to implement PBB because of ineffective implementation of budgetary policy due to the financial crisis, and because of gaps between PBB principles and methodologies (Karkatsoulis, 2010).

Given the problems identified during PBB implementation in the countries above, Aristovnik and Seljak (2009) argued that the PBB reform process requires considerable time due to administration weaknesses (such as budget processes and staff shortages) and a lack of institutional support and guidance to middle and lower

levels of public organisations (including regulation support and bureaucracy). Furthermore, Robinson (2002) asserted that preconditions for PBB implementation should include a good performance information system, performance indicator formulation, management accounting system, and analytical and evaluation tools. Robinson (2007) claimed that the model of PBB evidenced in industrial countries, cannot be fully transposed to developing countries due to differing characteristics and constraints of receptor countries (e.g. public servant demographics, cultural elements, low wages, nepotism), as well as a lack of enforcement or sanctions. These problems imply that the PBB model should be adapted prior to implementation, and environmental factors that support favourable PBB implementation should be in place.

Gibran and Sekwat (2009) suggested that in order to understand the problem of PBB implementation, a theoretical understanding of how, when and why the government implements a specific budgetary model is needed. It is not clear from the literature why many countries decided to use PBB as part of their budget reform as opposed to more traditional formats. Previous research concerning PBB has focused primarily on PBB implementation and practice, rather than its development, including the reasoning for adopting the PBB model within countries. Consequently, given the difficulties in understanding public budgeting, a theoretical model is needed to explain the development of budgeting and budget behaviour. The views of Gibran and Sekwat (2009) are consistent with Kelly (2003) who also suggested that PBB development should be more theoretically advanced to understand budgetary reform within the public sector, which is inherently influenced by the political process. A theoretical framework allows better understanding of the problems of PBB implementation. Hence, this study used the Lüder FMR model (Lüder, 2002; 2013) as a conceptual framework and institutional theory as theoretical frameworks.

In the case of Indonesia, despite international scepticism relating to PBB being able to improve control, efficiency and performance in public sector budgeting, the Indonesian government decided to implement PBB as its budgeting system both at

the central/national and local government level. As a transitioning and developing country, and the most populous country in South-East Asia, Indonesia reformed its political system (authoritarian and centralised for 30 years) into a more democratic government in 1999. This resulted in fundamental changes to governmental financial management, including the adoption of PBB as the principal budgeting system. In the Indonesian Minister of Finance's speech at the 2007 Annual Meeting of the International Monetary Fund (IMF) and World Bank, it was indicated that PBB implementation in Indonesia was in the early stages (Lienert, 2007). However no indication was provided as to whether PBB implementation in Indonesia was problematic or successful, and no documentary evidence has detailed how the PBB implementation process occurred (Lienert, 2007; Salim and Eckardt, 2008). Consequently, this research sought to address this gap in knowledge about the process and outcomes of PBB implementation in Indonesia.

Given the conflicting literature on PBB implementation and its development within countries, this research endeavoured to obtain a deeper understanding of public sector management reform, with particular focus on the history and development of PBB globally, and within the Indonesian public sector specifically. As outlined above, there is a paucity of research or documentary evidence about the extent to which PBB implementation in Indonesia has been successful. Previous research in Indonesia has studied the implementation of decentralisation, democracy, new public management, accounting reform (accrual and double entry systems) within an institutional theory perspective and performance measurement report in the local government, rather than PBB implementation specifically (Djamhuri and Mahmudi, 2006; Djamhuri, 2009; Green, 2005; Guess, 2005; Hadiz, 2004; Mimba et al., 2013).

### **1.3 Research Methodology**

This study aimed to understand and analyse the motives and factors that underpin the development and implementation of PBB within government, and in particular

the Indonesian Government. This research utilised qualitative research methodology for data collection.

For paper one, archival research was undertaken to systematically examine motives that underpin PBB evolution and its adoption within government from an historical perspective. Data was collected from archival documents (e.g. government acts, laws, other relevant reports and publications) related to PBB, as well as OECD publications on PBB. This data was used to provide both background and context to the history of PBB. Data was analysed through a chronological tracking of relevant documents and events using the Lüder FMR Model (2002) as a conceptual framework in order to understand the influencing factors for the development of PBB.

Papers two and three examine both Indonesian central and local government as case studies in order to understand governmental budgeting reform through PBB implementation. A case study is a method of studying an individual or institution through the use of documents, archival records, interviews, direct or participant observations, and physical artefacts (Yin, 2008; Ormrod & Leedy, 2005). Paper two involved utilising the NIS perspectives developed by Meyer and Rowan (1977) and DiMaggio and Powell (1983) to evaluate Indonesian budgetary reform during 2003–2010, particularly the history and implementation of PBB. This study also examined the occurrence of institutional pressures and the Indonesian central government's response to these pressures during the institutionalisation of PBB in Indonesia. Research for paper 3 employed the Lüder FMR model (2013) as a conceptual framework for understanding PBB as a budgeting reform within Indonesian local government during the period 1999–2010.

Data in papers two and three were obtained using semi-structured interviews (see Bryman, 2001) with Indonesians intricately involved in the early stages of PBB implementation and archival documents from Indonesian government reports and regulations, international organisation (the World Bank and the IMF) publications,

foreign donor projects in Indonesia, and newspaper articles. The design of the interview guide for paper two followed the main themes of this research, namely the three institutional isomorphic pressures (coercive, mimetic, and normative), the history of the Indonesian Public Sector (1990s to 2010), and the nature of PBB and its implementation. While the interview guide for paper three was an adaptation of Lüder's FMR model (2013) framework, original questions for each of the main sections were constructed based on a review of relevant literature. Open-ended questions were used in the interview guide to permit the interviewer and participants to probe, explore and ask questions to clarify a particular subject or issue (Patton, 2005).

Primary data collection occurred from November 2013 to January 2014. Interviews were undertaken with 20 participants affiliated with Indonesian government bodies including the Indonesian MoF, Ministry of Home Affairs (MoHA), Indonesian local government association, and the *Ikatan Akuntan Indonesia* (IAI – Indonesian Institute of Accountants). The 20 participants included several key persons from Indonesia involved as consultants for the IMF, the World Bank, and donor/ex-donor organisations, including the United States Agency for International Development (USAID), Canadian International Development Agency (CIDA) and the *Deutsche Gesellschaft für Internationale Zusammenarbeit* (German Organisation for Technical Cooperation – GTZ). Participants were selected because of their historical understanding of the Indonesian government's budgetary system, and their involvement in the formulation of regulations related to PBB implementation in the Indonesian government or PBB implementation more broadly (see Table 2).

Participants were chosen using a snowball sampling method, allowing the researcher to identify other respondents based on the initial respondent's information (Lewis-Beck et al, 2004). The research method is detailed in each paper.

**Table 2. Number of Participants by Institution**

No.	Institution	Number of Interviewees		Total Interviewees*
		Paper 2	Paper 3	
1.	Ministry of Home Affairs (MoHA)	3	4	4
2.	Ministry of Finance (MoF)	3		3
3.	World Organisations (IMF and World Bank)	2		2
4.	Foreign Donor Program	2	3	3
5.	Indonesian Institute of Accountants (IAI)	2	2	2
6.	Universities	3	3	3
7.	Local Government Association		3	3
	Total	15*	15*	20*

[\* = A total of 20 participants were involved in this thesis. Of those, 15 informants were used for paper 2, and also 15 respondents for paper 3.

The following sections discuss the theoretical framework applied in this study to understand the development of PBB within government systematically, and examine the history and motives behind the adoption and implementation of PBB in the Indonesian government budgeting system.

#### **1.4 Conceptual and Theoretical Framework**

The purpose of this section is to provide an understanding of the Lüder FMR as a conceptual framework and NIS as a theoretical framework in this study. The Lüder FMR has been useful in identifying the contextual factors and key players within budgeting and accounting reform (see Lüder, 2002, 2013), while NIS has been broadly applied to examine management accounting reform (see Covalleski and Dirsmith, 1988a, 1988b). The next section discusses the Lüder FMR model that was applied in this study.

#### **1.4.1 *The Lüder Financial Management Reform Process (FMR) Model***

This section explains why this study adopted the Lüder FMR model as a conceptual framework to analyse budgetary reform with a particular emphasis on the evolution of PBB across countries, and as a basis for analysing the Indonesian local government budgeting reform process.

The Lüder FMR model originated in 1992 as the “Lüder Contingency Model (LCM)” (Lüder, 1992), and was revised by Lüder in 1994 (Lüder, 1994). As an extension of the classical contingency theory approach, the Lüder model (both LCM and FMR) assumes a specific configuration of institutional components that influences the attitudes and behaviour of various participants (in public life, politics and administration) (Lüder, 1992, p.108) in the reform process. The Lüder LCM and FMR models have been used in previous research to examine governmental accounting reform in many countries under the Comparative International Governmental Accounting Research (CIGAR) network.

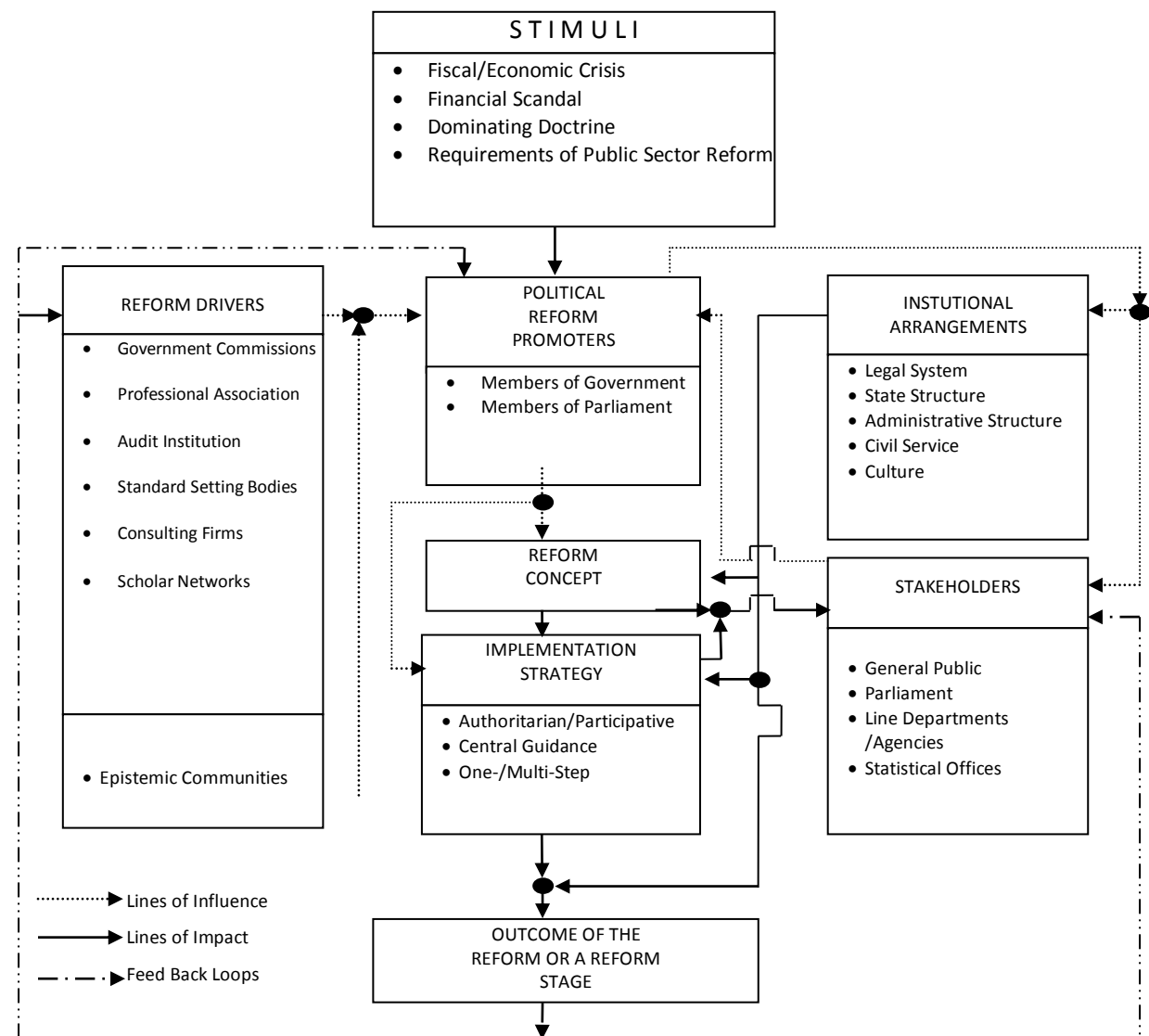
The Lüder model provides a contextual framework for explaining the transition from a traditional government accounting and budgeting model to a more informative system through the interaction of various social, political and administrative factors as institutional components (Lüder, 1992). This contextual framework, like any model, is “skeletal” in concept, and requires empirical detail to provide validity (Laughlin, 1995).

Specifically, the Lüder FMR model (2002) was designed to address the limitation of the previous LCM model that emphasised “context over behaviour” (Chan, 1996, p. 11). This limitation resulted in the LCM model focusing on contextual variables (such as stimuli and political and administrative structures) as opposed to behavioural variables, including changes by an actor or actors behind the reform. As key actors undertake the reform or innovation, the Lüder FMR model (2002) (see Figure 1) places emphasis on analysing the behaviours and attitudes of these key



reform actors (promoters, reform drivers, and stakeholder). Furthermore, the Lüder FMR model (2002) established a feedback mechanism (as part of the dynamic model) to allow for the possibility that the reform occurred over many stages (reform process) based on analysis of the results by key actors (Lüder, 2002).

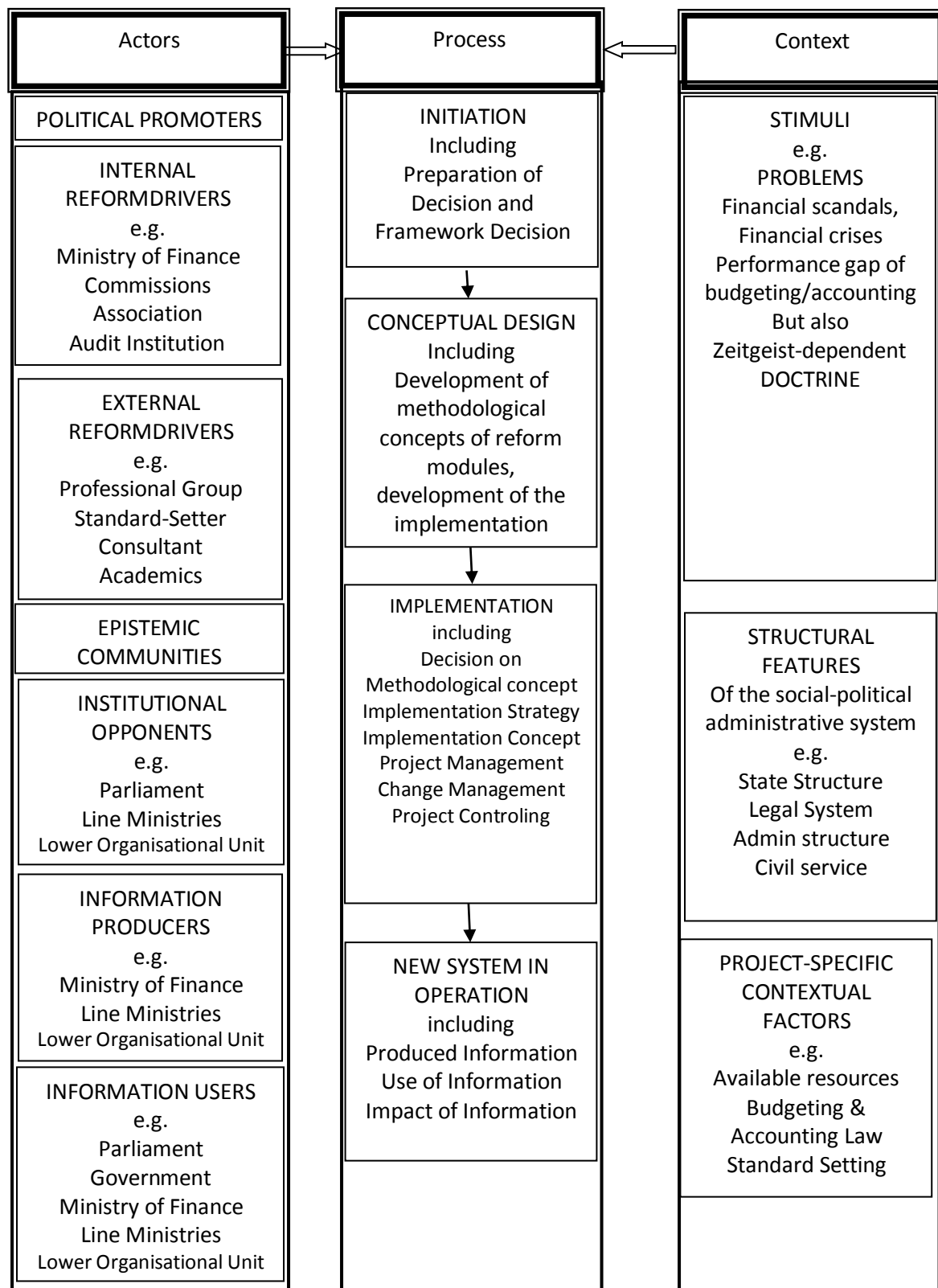
Figure 1 indicates the composition of the Lüder FMR model. It consists of stimuli, reform drivers, political reform promoters, institutional arrangements, stakeholders, the reform concept, and implementation strategy variables (Lüder, 2002). These variables are discussed in more detail in paper one.



**Figure 1. Financial Management Reform Process Model (Lüder, 2002)**

A further modification of the Lüder FMR model occurred in 2013. The 2013 model was used in the comparative analysis of budgeting and accounting reform in the case of the New South Wales (NSW) government in Australia and Hessian State in Germany. Based on analysis of relevant documents and publications as well as face-to-face interviews with 23 respondents, the Lüder FMR model (2013) was developed to analyse several factors influencing budgeting and accounting reform. This latest model, termed the 'actor-process-context model' (see Figure 2) consists of seven actor modules, namely political promoters, internal reform drivers, external reform drivers, epistemic communities, institutional opponents, information producers and information users. The three contextual modules are stimuli, structural features and project-specific contextual factors, and four reform process modules are initiation, conceptual design, implementation, and new system in operation.

The 2013 Lüder FMR model included an increased focus on the role of each module in influencing the reform, with particular emphasis on changes in key actor behaviour. In this model, reform drivers were divided into internal and external reform drivers to distinguish their intention and direction in influencing reform. Furthermore, the stakeholder variables in the Lüder FMR model (2002) were re-categorised into internal reform drivers and institutional opponents. Later, epistemic communities were separated from reform drivers, as in some cases these modules significantly influenced reform (Lüder, 2013). However, unlike the previous FMR model, this Lüder FMR model does not provide a feedback system that allows for the process of reform to occur across stages, and Lüder (2013) did not provide any clear explanation regarding this matter.



**Figure 2. The Financial Management Reform Process Model (Actors – Process – Context modules) from Lüder (2013)**

The Lüder FMR model (2002) is used in paper one (Chapter 2) to collect more contextual variables (such as stimuli and political and administrative structures) for the countries that adopted PBB as their budgeting system during the “old PBB” phase (1949 – 1980s). As suggested by Lüder (2002), this model has better explanatory power when examining the dynamic reforms that occur within countries that implemented PBB. Furthermore, paper three (chapter 4) used the Lüder FMR model (2013) with particular emphasis on changes in key actor behaviour, to gather harmonisation information and other financial management reforms, to assess Indonesian PBB implementation. In order to better understand the 2002 and 2013 Lüder FMR model, a more detailed application and discussion has been provided in papers one (Chapter 2) and three (Chapter 4).

The following section discusses NIS, particularly isomorphism (the degree in similarity of processes and structure between organisations), which is used as the interpretational framework in paper two. Brignall and Modell (2000) suggested that institutional theory is an appropriate basis upon which to explore the successful implementation of performance measurement and management in public sector research. Given that PBB encompasses elements of performance measurement and management, the NIS leads to the utilisation of PBB in this study.

#### ***1.4.2 New Institutional Sociology Theory***

The purpose of this section is to provide an overview of NIS as a framework for understanding the complexities of budgetary reform with particular emphasis on the adoption and implementation of PBB.

NIS is a new stream of new institutional theory that has frequently been applied in management accounting research to explain how rules, norms, structures and belief systems reshape the organisation (Scott, 2008; Burns and Scapens, 2000). This theory can be used to examine the relationship between management accounting practice in a social organisation and its institutional environment (Covaleski and Dirsmith,

1988a). This theory was developed from the premise that an institution is influenced by pressures beyond its control (DiMaggio and Powell, 1983). NIS was introduced by Meyer and Rowan (1977) and focuses on how social structures surrounding resources and meanings embody specific cultural rules and have important consequences within an organisation.

In NIS, the organisation is dynamic and ever-changing. In order to survive, it needs to conform to the rules, norms, structures and belief systems within its volatile environment; this process is called institutionalisation (Scott, 2008). The purpose of institutionalisation is to create homogeneity among organisations. That is, they become similar (isomorphic) in response to institutional pressures (DiMaggio, 1983). This process of becoming similar is called isomorphism, which emphasises how the organisation tends to adopt (conform to) other structures and procedures that are valued in their social and cultural environment in order to achieve legitimacy (Ribeiro and Scapens, 2006). Institutional theorists argue that isomorphism and/or legitimacy embodies the central forces elucidating why and how practices, such as management accounting, are developed and reformed (DiMaggio and Powell, 1983; Meyer and Rowan, 1977). For them, it is not only competitive advantage that drives improvement in new systems, but rather to seek social legitimacy as key. Hence, it is important to distinguish between competitive and institutional types of isomorphism, as opposed to purely seeking social legitimacy (DiMaggio and Powell, 1983, p. 150). Competitive isomorphism is focused on gaining efficiency, and certain budgetary practices are implemented in order to ensure best practice, economy and efficiency (Greenwood and Hinings, 1996). Institutional isomorphism, conversely, reflects the social forces that impose certain pressures to improve practices (DiMaggio and Powell, 1983).

DiMaggio and Powell (1983) argued that institutional isomorphism originates from coercive, normative and mimetic isomorphism. Coercive isomorphism occurs when an organisation is forced to adopt a new structure due to regulation, licensing or accreditation. The regulatory mechanism places emphasis on obtaining justification

for the implementation or adoption of a specific system or organisational practice. Normative isomorphism occurs when an organisation adopts a model because of professional body pressures. Normative mechanisms ensure that the systems are consistently maintained and modified within or across the organisation over time, not because of economic considerations or adherence to laws, but because they believe that the system is the norm (custom), which should be followed voluntarily. Mimetic isomorphism occurs when an organisation replicates another organisation's model because of uncertainty in the environment. Mimetic isomorphism means that the organisation will copy and implement the system or practice from another organisation, although it may have originated from a different culture (Scott, 2008; DiMaggio, 1983).

Institutional isomorphism views the organisation as passive as opposed to proactive in responding to institutional pressures (Powell, 1985, Oliver, 1991, Scott, 2008). A successful institutionalisation process incorporates a general level of acceptance by members of the organisation of the values, concepts and changes introduced. The higher the level of acceptance, the easier it is for new values to saturate the organisation (Scott, 2008). Hence, institutional pressure allows the organisation to conform to the requirements of its environment by either accepting or resisting pressure in the most effective way (Meyer and Rowan, 1977; Siti-Nabiha and Scapens, 2005).

As a response to institutional pressure in both public and private organisations, Oliver (1991) presented five types of strategic responses by organisational members dealing with institutional pressure: acquiescence, compromise, avoidance, defiance, and manipulation. She proposed that the type of institutional pressure applied affects organisational member responses to institutionalisation. Oliver (1991) suggested organisations follow an acquiescence strategy and passively respond to institutional pressures when the degree of coercion is high. Otherwise, organisations can accept a compromise strategy as more active responses to institutional pressures that often conflict with internal organisational demand. The organisation could also

apply an avoidance strategy in attempting to buffer it from institutional pressure, or seek to escape from institutional norms to rule. More active organisational responses include a defiance strategy to resist institutional pressure when internal organisational objectives conflict or diverge dramatically from institutional pressures or requirements. The most active response is manipulation, whereby the organisation actively resists by exerting power to actively change institutional pressure, which occurs when the organisation attempts to co-opt, influence, or control institutional pressures and evaluations.

As budgeting is part of management accounting practice (Scapens, 1990), it can be viewed as routine and, given it is endorsed and reproduced through time, can become 'institutionalised' (Burns and Scapens, 2000). In the public sector, several scholars (Covaleski and Dirsmith, 1988a; Modell, 2001; De-Araujo et al., 2009) have examined the institutionalisation of budgeting systems and found the existence of institutional pressure in the budgetary reform process. Covaleski and Dirsmith (1988a) found that the institutionalisation process of the budgetary system occurred through self-interest from within the organisation as well as being influenced by other organisations. In related research they found that isomorphism occurred in the institutionalisation of the budgetary system in the case of the University of Wisconsin (Covaleski and Dirsmith, 1988b). Modell (2001) found the existence of both economically rational motives (efficiency) and legitimacy-seeking from senior management in response to performance management institutionalisation within the Norwegian health care sector. This finding is consistent with Oliver (1991), who hypothesised that organisations conform to institutional pressure by using compliance responses as motives to seek legitimacy and achieve efficiency. In Portugal, the institutionalisation of the new budgeting system (PBB implementation) occurred as institutional pressure from the European Union, the OECD and the European Public Administration Network (EUPAN). However, the reform was adopted only as a formality – a resistance response from Portuguese bureaucracy (De-Araujo et al., 2009).

The research findings above relate to NIS, which explains how and why public sector organisations accept a particular rule, norm, structure, belief system or method. It is considered appropriate for this study as a theoretical framework for explaining budgeting reform, particularly the adoption and implementation of PBB.

## **1.5 Overall Introduction**

This section outlines the structure of this thesis, which consists of five chapters (including this one). This thesis follows the thesis by publication format, consisting of three papers centralised around an overall theme of budgeting in Indonesia. Each paper examines different aspects of the theme, but has similar intentions in delivering an understanding of the historical evolution of PBB and its implementation within nation states. The thesis provides further understanding of PBB history and implementation in the Indonesian public sector.

Chapter two presents the first research paper, titled *A Conceptual Framework for Budgetary Reform within Public Sector Organisations*. Using the Lüder FMR model (2000), this paper addresses the history of PBB and its implementation within countries from the 1940s to the 1980s. The Lüder FMR model is also used to examine factors influencing PBB adoption and implementation across countries. Data was collected from archival documents (government acts, law, reports and publications) related to PBB, public sector management literature, management accounting literature, and OECD publications on PBB, to support an examination of PBB history during this period. An earlier version of paper one was presented at the *Fourth Biennial Global Accounting and Organizational Change Conference*, 17-20 November 2014 at the American University of Sharjah, in the United Arab Emirates.

Chapter three presents the second research paper, titled *The Transformation of Indonesia's Central Governmental Budgetary System*. This paper employs NIS as the interpretational framework of an examination of budgetary reform within the Indonesian central government from 2003 to 2010. This study focused on the history



of PBB adoption and implementation during the aforementioned period. Data was gathered from interviews and archival documents (Indonesian government reports and regulations), international organisation (e.g. the World Bank and the IMF) publications, the publications of foreign donor projects in Indonesia, and newspaper articles.

Chapter four presents the third research paper, titled *The Implementation of Performance-Based Budgeting within Indonesian Local Government*. This paper used the Lüder FMR model (2013) to investigate the motives that underpinned the development of PBB and factors influencing its implementation within Indonesian Local Government during the period 1999–2010. Data was gathered from interviews and archival documents (e.g. Indonesian government reports, publications, laws, decrees and other regulations), newspaper articles, international organisation (e.g. World Bank, OECD and IMF) reports and publications, foreign donor project reports and publications, public sector management literature, management accounting literature, and newspaper articles.

Chapter five concludes the thesis, delivering an integrated summary of the three papers and providing implications for the broader field of public sector budgeting reform in developing countries, particularly Indonesia.

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## **2. Paper 1: A Conceptual Framework for Budgetary Reform within Public Sector Organisations**

### **2.1 Abstract**

**Purpose:** This paper systematically examines the motives that underpin the development of Performance Based Budgeting (PBB), and the history and factors that influenced early PBB development across countries.

**Design/methodology/approach:** This study uses a qualitative research methodology, by historically reviewing the evolution of PBB as a new public budgeting model from approximately 1949 to 1989.

**Findings:** PBB was first implemented in the United States (US) in 1949 and expanded to developing countries through and United Nations (UN) funded projects. Using the Lüder FMR model (2002), the primary motive underpinning implementation in the US was the rise in demand from the public sector for more informative and efficient budgets. This finding has been supported by subsequent research in the United Kingdom (UK), Australia and Denmark. Furthermore, influence from the US and UK budgeting systems has been the primary stimulus for PBB implementation across the globe. This study found that the outcome of budgetary reform varies among countries, from that of a single format involving traditional budgeting, to 'old PBB', to a dynamic approach involving multiple stages that resulted in PBB modification.

**Research limitations/implications:** Limitations exist in using the Lüder FMR model (2002) to examine budgetary reform across various countries based on the historical approach. Effective use of the Lüder FMR within an historical context requires more chronologically detailed data to perform a deeper analysis relating to events across countries. Alternatively, the Lüder FMR model can be applied across countries using comparative research without an historical overview.

**Originality/value:** The originality of this study lies in the utilisation of the Lüder FMR model (2002) to study the evolution and early global development of public sector PBB. This paper contributes to PBB research in the broader management accounting and public sector literature.

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American University of Sharjah, in the United Arab Emirates, for comments on earlier versions of this paper.

**Keywords:** performance-based budgeting, historical research, Lüder FMR model.

## **2.2 Introduction and Purpose**

This study sought to reveal the motives that underpin the development of PBB and the factors influencing its implementation. It involved an application of the Lüder Financial Management Reform (FMR) model (2002) as a conceptual framework for understanding budgetary reform, the history of performance-based budgeting (PBB) implementation, and whether similar factors influenced early PBB development across countries. The results of the study enhance our understanding of the utilisation of the Lüder FMR model (2002) within public sector management accounting, specifically with budgetary reform and in relation to the evolution of PBB.

Using the Lüder FMR model (2002), this research sought to address several questions:

1. Why and when did public sector organisations within nation states implement PBB as part of their budgetary reform?
2. Which reform drivers and institutional arrangements helped shape the governments' decision to implement PBB?
3. What and why did public sector organisations and government specifically, encounter barriers to PBB implementation during the budgetary reform process?

This paper reviews the evolution of PBB from an historical perspective, as part of public financial management reform, across nine countries from the approximate period 1949 to 1989 to gather detailed information on initial PBB implementation. This period was known as the era of 'old PBB' (Shah and Shen, 2007, Jones and



McCaffery, 2010). Historical research is an appropriate method for tracing the systematic development of a new organisational management system or organisational change (Christensen, 2002, Khumawala, 1997). It is a method of studying major events influencing humanity or organisational change utilising documents, oral history and archives (Ormrod & Leedy, 2005, Salkind, 2012).

Data was gathered from public sector management literature, management accounting literature, Organisation for Economic Cooperation and Development (OECD) publications on PBB, and archival documentary evidence related to the history of PBB. Data were then analysed through a chronological tracking of relevant documents and events within the Lüder FMR model (2002) framework in order to understand the factors influencing the development of PBB.

## **2.3 The Budgetary Context**

Since the early 1990s, the international trend in public sector budgeting has been dominated by the implementation of PBB as a tool for measuring performance (Aristovnik and Seljak, 2009; Schick, 2007). Several researchers argue that PBB was developed to replace traditional budgeting (e.g. Joyce, 2011; Curristine, 2005; Melkers and Willoughby, 2001). In theory, PBB links funding and resource allocation to measurable results in the form of outputs and/or outcomes that achieve specific objectives based on program goals (OECD, 2007; Anderson, 2008). It is argued that PBB is a budget type that has a clear linkage from funding to outputs/outcomes using performance information within the budget document. Governments and budgetary committees use this performance information to assess each budget (Robinson, 2007)<sup>1</sup>. Carter (1991) described PBB as a budget that uses mission

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<sup>1</sup> PBB, has two budget process steps. The first is budget formulation, which requires agencies and departments to submit their budget for review and analysis by government (executive arm). Agencies and departments compete to have their programs funded by providing performance information to government for assessment. This step results in a budget draft document. Second, in a process termed budget enactment, the MoF presents the draft budget to the legislature (budget committee) for review and approval based on performance information provided in the draft budget (Robinson, 2007).

statements, goals and objectives to explain how government money is spent, and contributes toward enhancing performance measurement in the public sector.

There has been recent debate concerning the “relevance” and “real use” of PBB in the public sector. Many authors argue that performance information and performance measurement portrayed in budget documents influence the budget approval process, as mentioned above (Curristine, 2005; Joyce, 2011). For example, Berry and Flowers (1999) examined the case of Florida State Agencies and found that PBB had a positive impact on decision-making that related to performance measurement and budget result accountability. Additionally, research on the US Department of Agriculture and Department of the Interior demonstrated an important link between cost, performance measurement and output, and/or outcomes for these programs (Juszczak, 2009b; 2009a). PBB aims to improve control, efficiency and performance in public sector budgeting and enhance the capacity of departments or agencies within government to compete for budgetary allocations using performance information (Walker, 2002). In summary, PBB is perceived as an appropriate and powerful budgeting tool in the public sector.

Nevertheless, the implementation of PBB has been the subject of criticism. Lu (1998) and Moynihan (2006) indicated that connections between performance information and budget assessment in the budgeting process were often unclear. Moreover, evidence shows that budget committees rarely use performance information and measurement in the budget approval process. For example, performance information depicted in the budget document is rarely considered when parliament approves government budget proposals (Melkers and Willoughby, 2001; Andrews, 2004). Karkatsoulis (2010), Lee (2009) and Jordan and Hackbart (2005) found that difficulties in assessing the outcomes of management and budgetary processes are due to inaccurate performance data associated with the lack of performance measurement capacity of public sector organisations. Others (Kelly, 2003) are not convinced that traditional budgeting is problematic for public sector budgeting and that the perceived problems associated with traditional budgeting warrant the use of

PBB. In fact, despite PBB having been implemented as a new budgetary measure in several countries, including the US and Greece, line-item and incremental budgets (traditional budgeting formats) were still being used in conjunction with PBB (Schick, 2001; Andrews, 2004; Karkatsoulis, 2010; Aristovnik and Seljak, 2009). The research problem arises from the fact that we do not know the historical context in which PBB developed from traditional budgeting, and why various countries decided to implement PBB.

Sterck (2007) and Van Reeth (2002) suggested the use of a theoretical framework in order to understand budgetary reforms, hence, this study used the Lüder FMR model (2002). Klaus Lüder proposed the model as a theoretical framework for understanding and identifying the factors influencing budgetary reform.

The Lüder FMR model and its precursor, the Lüder contingency model (LCM), have been used within public sector literature, specifically the Comparative International Governmental Accounting Research (CIGAR) network, to understand the transition from traditional governmental accounting to a more informative accounting system (Lüder, 2002). Several researchers argue that the Lüder FMR model (2002) is an appropriate model for understanding governmental accounting reform and the factors that influence the reform process. For instance, Jorge (2003) found that the Lüder FMR model (2002) could be used as an interpretative framework to predict several factors, influencing governmental accounting reform in the case of Portuguese local government. Furthermore, Abushamsieh (2013a) used the modified Lüder FMR model to analyse obstacles and difficulties that occurred during accrual accounting reform in the Gulf Cooperation Council (GCC) Countries – Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates. The Lüder FMR model has also been applied to examine the divergence of certain aspect of technical accounting in an inter-governmental study of France, Germany, the UK, and the USA (Jones et al., 2013).

There has been little application of the Lüder FMR model in other areas of financial management reform, including budgeting, financial reporting and auditing. Some researchers have used the Lüder FMR model to explain the factors that influence accounting and budgeting reform in countries such as France, Germany, the UK, the USA, Italy, and Portugal. However, these studies examined the factors influencing broader accounting reform rather than budgetary reform (Bruno, 2014; Jorge, 2003; Abushamsieh, 2013a; 2013b; Lüder, 2009).

This paper is structured as follows. The next section explores the notion of various reforms within the public sector, including budgetary reform, budgeting in the public sector, and the concept, definitions and types of PBB. The section continues with a description of the Lüder FMR model (2002) and the justification for its use in this study. The following section examines the evolution of PBB implementation for the approximate period 1949 to 1989, applying the Lüder FMR model (2002). The final section summarises the findings in relation to the history of PBB implementation, the implications and the limitations of the research, and makes recommendations for future research.

## **2.4 What is Reform?**

Reform refers to a variety of transformations, which can range from the very minor to fundamental adjustments in organisational ownership, governance and managerial arrangements. Within an academic context, these forms describe the range of processes of organisational innovation that increases an organisation's ability to deliver service to the customer (European Commission, 2009). They include privatisation in its many forms, public sector reform, public sector management reform, public financial management reform, accounting reform and budgeting reform.

### **2.4.1 Public Sector Reform**

The public sector is concerned with government authority and services. Nonetheless, the nature of public sector organisations can vary among countries, depending on their historical context. In most countries the public sector consists of three arms of government that constitute the ‘separation of powers’ model: the executive (the administrative government of the day), the legislature (parliament or congress) and the judiciary (the various court systems). Government consists of statutory bodies and services, including defence and/or the military, police, health, road and transportation, and education (The European Commission, 2009).

Public sector reform seeks to improve the efficiency and effectiveness<sup>2</sup> of public sector organisations in order to promote better delivery of public goods and services. Public sector reform is designed and implemented based on a country’s social, economic, political and cultural context (European Commission, 2009). These objectives are achieved through actions including democratisation (Sedara and Öjendal, 2007; Hadiz, 2004), political reform (O'Brien, 1994; Bratton and Van de Walle, 1992), organisational restructure (Hawkins, 2000; Treisman, 1999; Chapman and Boyd, 1986), the improvement of human resource management and training, public sector management enhancement, strengthened measures for public participation, transparency, the combating of corruption (The United Nations, 2006), and public management reform (Pollitt and Bouckaert, 2011; Guthrie et al., 2005; Hood, 1991). Whilst broader public sector reform has existed since government was invented (Woodward and Clark, 1962), specific public sector management reform became more prominent in the 1950s (Pollitt and Bouckaert, 2011).

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<sup>2</sup> Efficiency refers to public sector organisations delivering their best service with minimum expense, time and effort, and is therefore concerned with ‘doing things in the right manner’. Effectiveness is about how public sector organisations achieve their objectives, and is therefore concerned with ‘doing the right thing’ (Australian Government, 2013).

### 2.4.2 *Public Sector Management Reform*

Pollit and Bouckaert (2011) defined public management reform as the innovation<sup>3</sup> of public sector organisational structures and processes, with the objective of enhancing operational efficiency and effectiveness. Organisational structural reform can refer to the amalgamation or separation of organisations, whilst process reform involves systems, quality standards, and capacity-building enhancement.

In the 1980s, public management reform became more widespread internationally with the objective of making government more 'business-like'. This concept became known as new public management (NPM). NPM reform consists of four aspects: (1) finance, including budgeting, accounting and auditing; (2) personnel, including recruitment, staff posting, remuneration, security of employment; (3) public sector organisation, including specialisation, coordination, scaling and decentralisation; and (4) performance measurement systems, including content, organisation and utilisation (Guthrie et al., 2005; Pollitt and Bouckaert, 2011).

Despite NPM having been implemented in some form by many countries throughout the latter half of the 1990s and early 2000s, its adoption has not been comprehensive nor has it become the dominant model (Guthrie, 1998; Pollitt and Bouckaert, 2011). This is primarily due to cultural, ethical and political factors that influence the degree of implementation (Dunleavy and Hood, 1994; Dunleavy et al., 2006). Furthermore, the socio-political environment of the developing countries was not particularly accommodating for NPM (Turner et al., 2015). NPM was an abbreviation that was largely seen as just another administrative model, adopted more broadly across OECD countries that had a government reform agenda (Hood, 1991). Therefore, whilst the NPM concept has become a success in some countries, this has not been the case elsewhere. Each country has sought to develop its own

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<sup>3</sup> Innovation is the implementation of new ideas or changes that have the potential to contribute to organisational objectives (Schroeder et al., 1989). Incremental innovation occurs in most public management reform, as change involves improving the existing model (Ettlie et al., 1984).

model and concept of NPM (Dunleavy and Hood, 1994; Dunleavy et al., 2006; Pollitt and Bouckaert, 2011;).

Research has explored NPM reform in various countries and regions, including Norway (Pettersen, 2001), New Zealand (Newberry, 2005) and Southeast Asia (Turner, 2002), and has illustrated the influence of NPM on budgeting and accounting in public management reform. Researchers, including Christensen (2002) with respect to the state of New South Wales (NSW), Australia, and Khumawala (1997) with respect to the Indian government, have used theoretical frameworks such as the LCM model to observe factors that influence reform. Most research that relates to NPM reform has focussed predominantly on public financial management reform (Guthrie, 2005).

#### ***2.4.3 Public Financial Management Reform***

Public Financial Management (PFM), later termed New Public Financial Management (NPFM), reform has focused primarily on financial and accounting systems (The World Bank, 2012). NPFM is a part of the NPM concept that concentrates primarily on accounting and financial aspects, as opposed to broader institutional reform. Focusing on financial management, Olson et al. (1998) identified five different elements of NPFM: 1) market-oriented management system development; 2) budgeting system development; 3) performance management systems development within government entities; 4) government financial reporting system reform; and 5) public sector audit mechanism reform.

Research in NPFM reform has been undertaken for over a decade in Australia (English et al., 2005), Italy (Mussari, 2005), New Zealand (Newberry and Pallot, 2005), Spain (Pina and Torres, 2005), and within Eastern European nations (Vagnoni, 2005). However, most of this research focuses on the study of accounting and budgetary reform rather than on other elements of NPFM. Accounting and

budgetary reform have become more prominent within financial management reform studies.

#### **2.4.4 *Accounting Reform***

For over 30 years, research on accounting reform has been a part of NPFM reform studies (Guthrie et al., 2005). Recent research on accounting reform has focused on the implementation of accrual accounting as a replacement to the cash accounting system. This is based on the premise that accrual accounting improves public sector accountability and assists users by providing information for decision-making (Hyndman & Connolly, 2011).

However evidence has illustrated that accrual accounting has several problems when adapted from the business environment to the public sector, including issues regarding asset definition and valuation, as well as the matching concept (Ezzamel et al., 2005). Further, Pollitt & Bouckaert (2011) argued that expenditure figures based on accrual accounting led to confusion among parliamentarians in Sweden and New Zealand. Debate has largely focused on whether business accounting concepts and practices, including accrual accounting, are indeed applicable in the public sector.

Several scholars have studied the development of accrual accounting within government in Australia (Guthrie, 1998), Indonesia (Harun and Robinson, 2010), New Zealand (Pallot, 2001), Sweden (Paulsson, 2006), the Netherlands (Peter van der Hoek, 2005), and the European Union (Pina, 2009). In order to examine the contingency factors that influence accounting reform, theoretical frameworks such as the LCM and the Lüder FMR model have been used to examine federal government operations in Malaysia (Saleh, 2007) and the United States (Chan, 1994), and also accounting reform in Gulf Cooperation Countries (Abushamsieh et al., 2013a), Palestine (Abushamsieh et al., 2013b), and Portugal (Jorge, 2003). Although this research has placed emphasis on accounting reform, some studies have also



explored budgetary reform and found evidence that several factors – including stimuli, reform drivers, and political reform promoters – influence accounting and budgetary reform.

#### **2.4.5 *Budgetary Reform***

As part of public sector management reform, budgetary reform refers to budgeting system change within government. Government budgets involve the financial planning of public money that consists of revenue and expenditure estimation for a specific period (Schiavo-Campo and Tommasi, 1999). There are many reasons for government budgetary reform. Several researchers have argued that as government activities in the modern era expanded and diversified, the role of government budgets has also become more complex in order to address them. Thus, reform is needed because traditional budgeting systems inadequately address the needs of modern government (Curristine, 2005; Joyce, 2011). Other researchers have argued that reform occurs as a result of the influence of new budgetary systems from other countries (Aristovnik and Seljak, 2009; Karkatsoulis, 2010).

Several studies have examined budgetary reforms within countries and various budgeting formats; for instance, PBB in Sri Lanka (Dean, 1986b), program budgeting and PBB in Malaysia (Dean, 1986c), planning, programing, budgeting system (PPBS) in the USA (Page, 1967), program budgeting in OECD countries (Kraan, 2007), and zero-based budgeting (ZBB) in the USA (Wetherbe and Dickson, 1979). However, these studies, and most budgetary reform research, lack any theoretical framework(s) for interpreting the factors influencing budgetary reform (Sterck, 2007; Van Reeth, 2002). Thus, the examination of public sector budgeting in its various forms and a corresponding theoretical framework are needed to understand the history of budgetary reform in the public sector, in particular the evolution of PBB. The next section examines budgeting in the public sector, including traditional formats and their limitations, and several contemporary budgeting forms that have replaced traditional budgeting.

## 2.5 Budgeting in the Public Sector

Before the emergence of PBB, global public sector organisations utilised traditional budgeting as part of their budgetary process (Jones and McCaffery, 2010). Traditional budgeting focuses solely on the utilisation of inputs or organisational resources; for instance, labour, money, materials, and equipment. Traditional budgeting has been used in many countries, including the USA, New Zealand, India, Singapore, and Slovenia, for over a century because of its simplicity and stability when deciding on policy outcomes (Kelly, 2003; Aristovnik and Seljak, 2009; Chowdhary, 2001; Schick, 1998). However, traditional budgeting does not consider information regarding the performance of an organisations' programs and activities when assessing resource allocation (Wildavsky, 1978). Thus traditional budgeting contributes to both inefficiency and ineffectiveness within public monetary management (Osborne, 1993). There are several forms of traditional budgeting:

- **Annual budgeting**, which requires expenditure and revenue to be formulated and forecast annually, for a single year (short-term). Budgets are often not in line with organisational programs and are fragmented in the budget appropriation and decision process (Wildavsky, 1978). As the annual budget lacks long-term vision, there are problems in controlling budget allocations within long-term government programs. Examples include infrastructure development programs that require a cycle of three years or more to complete, where it is difficult to control budget duplication and overlapping because of fragmentation and annual estimations. This results in inefficiency and ineffectiveness within public budgeting (Caiden, 1982).
- **Line-item budgets** involve revenues and expenses being separated into specific centres including wages, supplies and travel (Schick, 1966). Although this budgeting has benefits for public sector managers in that it has a simple format and is easy to manage (Kelly, 2003), it is also problematic as it does not facilitate analysis as to whether each item is necessary as a line item, and/or whether the

proposed expenditure or revenue in each item is allocated efficiently. Furthermore, in this form of budgeting, public sector managers are not allowed to reallocate funding between items. This inflexibility impacts upon budget efficiency and effectiveness as funding for each line item will be spent in the current budget year, otherwise it is lost or reduced in the next accounting period (Robinson, 2007; Osborne, 1993). As a consequence, public sector managers tend to fully utilise the monetary allocation on each line item to preserve their budget in the following year.

- **Incremental budgets** formulate the current year's budget by increasing/decreasing revenue and expenditure based on the previous year's budget (Wildavsky, 1978). The incremental budget has benefits of simplicity, stability and permeability in the political system, because it provides the easiest way to forecast a budget's increase and/or decrease (Kelly, 2003). However, this budgeting form is inefficient and ineffective with respect to public expenditure accountability, as prior budgets lack comprehensive review. Budget allocation is not based on an established public need, and merely preserves the previous budget and/or activities (Khan and Hildreth, 2002). Furthermore, similar to line-item budgets, the incremental budget nurtures the public sector manager's attitude of "use it or lose it", as if expenditure is not used in the current period it will reduce in subsequent periods. Furthermore, in regards to maintaining preferred budgetary slack, incremental budgeting forces public sector managers to deflate revenue and inflate expenditure, giving the impression that managers are improving performance. Furthermore, since the budget is assigned the same allocation every year, it is difficult to decide funding allocations for new activities. Thus, incremental budgeting maintains a conservative mindset and does not support risk-taking (Bragg, 2013).

These forms of traditional budgeting are not mutually exclusive and could take place at once (Wildavsky, 1978; Khan and Hildreth, 2002). However, as the purpose of public sector budgeting reform is to increase efficiency and effectiveness, modern

public sector budgeting that uses any of the traditional aforementioned budget types face problems. PBB was introduced to alleviate the problems caused by traditional budgets (For example see Dean, 1986a; Jones and McCaffery, 2010; Ho, 2011; Allen and Radev, 2006).

To address and eliminate these problems, several contemporary public sector budgeting approaches have emerged that are similar to PBB. These budgets also use performance information to evaluate government budget documents. They include:

- **Program/Programme budgeting**, which focuses on the expected results of government programs and classifies public sector expenditure based on government objectives. Thus, programs with common objectives are considered together (Carlson, 1969). This budgeting also emphasises the achievement of longer-term community-wide goals that relate to revenues and expenditures of multi-year programs (Novick, 1967).

In general, program classification closely follows the organisational structure of the line ministry, hence every Director-General is made responsible for one or more program line items. There are no overlapping responsibilities between programs and/or Director-Generals (Kraan, 2007). Therefore, as program budgeting focuses on the expected results of the program and long-term vision, it alleviates the limitations of traditional budgeting that include orientation toward inputs and line items and the possible overlapping across multi-year programs. Program budgeting can be seen as an early variant of PBB, and has been used in conjunction with PPBS (Robinson, 2007; McNab and Melese, 2003).

- **Zero-based budgeting (ZBB)** is defined by the Chartered Institute of Management Accountants (CIMA) as:

*.. a method of budgeting which requires each cost element to be specifically justified, as though the activities to which the budget*

*relates were being undertaken for the first time. Without approval, the budget allowance is zero. (Scarlett, 2005, p. 216)*

In the context of the public sector, each government department/agency proposes decision-packages that contain annual budget and performance information. Moreover, the budget committee evaluates each decision-package and approves it based on government requirements (McGill, 2001).

Zero-based budgeting has many advantages that eliminate traditional budget weaknesses, especially in relation to incremental budgets. Firstly, ZBB allocates resources more efficiently as the budget is formulated based on organisational needs and benefits rather than from previous-year approaches. Moreover, as it is public sector managers who allocate expenditure to activities in this budgeting form, it is nearly impossible for them to inflate or deflate expenditures and revenues. Further, this budgeting coerces public sector managers into improving their operations by identifying and excluding inefficient and outdated operations. ZBB coerces public sector managers into deciding which activities are valuable to the organisation. Thus, they can eliminate non-valuable activity and improve organisational efficiency and effectiveness (Bragg, 2013). However, in the USA, ZBB faced difficulties during early implementation due to increased paperwork in the budgeting process and a lack of performance information needed for analysis (United States General Accounting Office, 1997).

- **Planning Programming Budgeting System (PPBS)** was initiated in the USA in the 1960s, and is designed to facilitate budget decision-making within government departments/agencies by utilising better program categories (Page, 1967).

*Proponents of PPBS believed that efficiencies and improvements in government operations could be achieved through a common approach for (a) establishing long range planning objectives, (b) analysing the costs and benefits of alternative programs which would meet these objectives, and (c) translating programs into budget and legislative*

*proposals and long-term projections. (United States General Accounting Office, 1997, p. 35).*

When PPBS was first implemented it was known as output budgeting, and was identical to program budgeting. PPBS was promulgated in many countries, including France and Malaysia, as part of the international program of the United Nations (UN), the International Monetary Fund (IMF) and the World Bank (Robinson, 2007). Thus, similar to program budgeting, PPBS seeks to address several limitations of traditional budgeting, especially for annual and line-item budgeting, including changing orientations from inputs to outputs, transforming budget accounts from line items to program based, and accommodating a long-term vision that reduces inefficiency in multi-year programs (Schick, 1966). Nevertheless, many problems arise in PPBS implementation, for instance, the increased paperwork within the budgeting process, difficulties in measuring the costs and benefits of programs, and complexities in linking programs with budgetary structures (United States General Accounting Office, 1997).

These contemporary public sector budgeting approaches outlined above were categorised by some researchers as different to PBB (Dongsung, 2005; Ho, 2011; Shah and Shen, 2007; Schick, 1966). However, other researchers consider these modern budgeting techniques to be variants of PBB, because of the utilisation of performance information within the budgetary document (Kraan, 2007; Van Nispen and Posseth, 2006; Robinson, 2007; McGill, 2001). Robinson (2007) classifies program budgeting as an early variant of PBB. As PPBS is identical to program budgeting, this technique could also be classified as a variant of PBB.

## **2.6 What is Performance-Based Budgeting?**

This section provides an outline of the evolution of PBB and a discussion about its variations. It is important to answer several questions: What is PBB? How and why

is PBB different from other budgeting techniques? Why did certain countries choose to adopt and implement PBB?

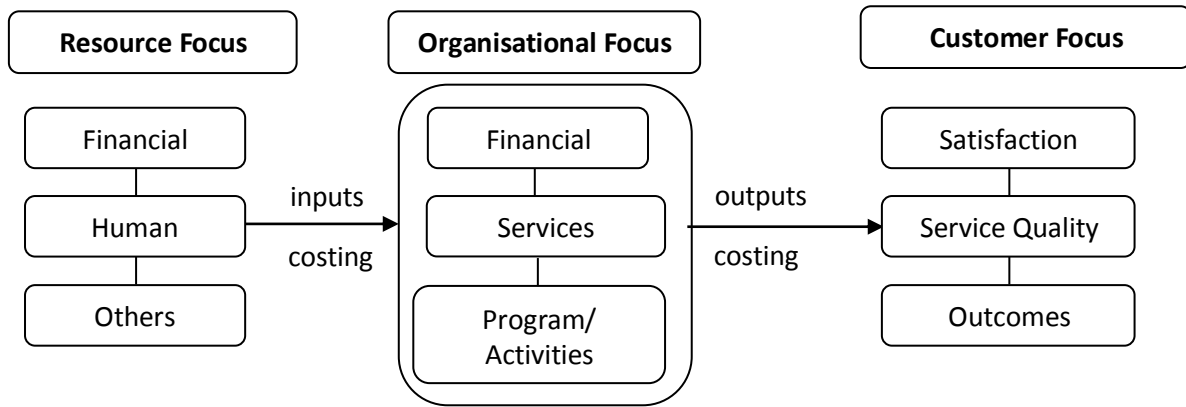
While there is no single agreed definition of PBB, an early definition can be found in the US Budget and Accounting Procedure Act 1950, where it is described as being based on performance and program cost information by organisational unit. Furthermore, PBB is used to identify and emphasise programs and/or activities performed based on organisational, functional, and project/activity formats (United States Congress, 1950). Additionally, PBB has been defined as:

*...a system of budgeting that presents the purpose and objectives for which funds are required, costs of programs and associated activities proposed for achieving those objectives and outputs to be produced or services to be rendered under each program. (Shah, 2007, p. 5)*

*...designed to strengthen the linkage between funding and results (outputs and outcomes), through the systematic use of formal performance information, with the objective of improving the allocated and technical efficiency of public expenditure. (Robinson, 2007, p. 1).*

In summary, PBB is a budget model that focuses on resource allocation based on performance information within a program and/or activity. This performance information is used to approve each program and/or activity over an organisational unit in order to provide public services.

Shah and Shen (2007) argued that the history of PBB implementation can be divided into two periods: (1) 'old PBB', which originated in 1949 and continued until the late 1980s, and focused on organisational structure, and; (2) 'new PBB', commencing in the 1990s, where greater emphasis was placed on the linking of input/resources with results. This different emphasis of PBB is also distinguished by Dongsung (2005) based on their performance measurement focus, as explained in Figure 3.



**Figure 3. Focus of budgeting: performance measurement type (Dongsung, 2005)**

According to Dongsung (2005), there are three types of performance measurement orientations within budgeting: resource-focused, organisation-focused and customer-focused. *Resource-focused* means that government budgets only measure input resource performance (e.g. financial, human, or other resources), which is the basis for traditional budgeting. *Organisation-focused* measurement means that the government budgets also focus on the performance of organisational processes and outputs, including finance, services and programs and/or activities. This performance type retains certain characteristics from the old PBB, and is also recognised as a characteristic of program budgeting. Finally, *customer-focused* measurement means that government budgets emphasise customer performance measures (satisfaction, service quality and outcome), which is a characteristic of the new PBB (Dongsung, 2005). Therefore the performance focus of old PBB (1949–1980s) was organisation-focused, whereby the new PBB (1990s–present) focuses on customer orientation.

The customer-oriented performance measurement focus inherent within PBB is in line with the principles of NPM, which also places emphasis on customer orientation (see Dunleavy et al., 2006; Diefenbach, 2009; Dunleavy and Hood, 1994). NPM aims to reorganise public sector organisations by aligning their management, accounting and reporting methods to those of the private sector, with the aim of improving



government's public administration system, with citizens also being customers (Denhart and Denhardt, 2000; Dunleavy and Hood, 1994).

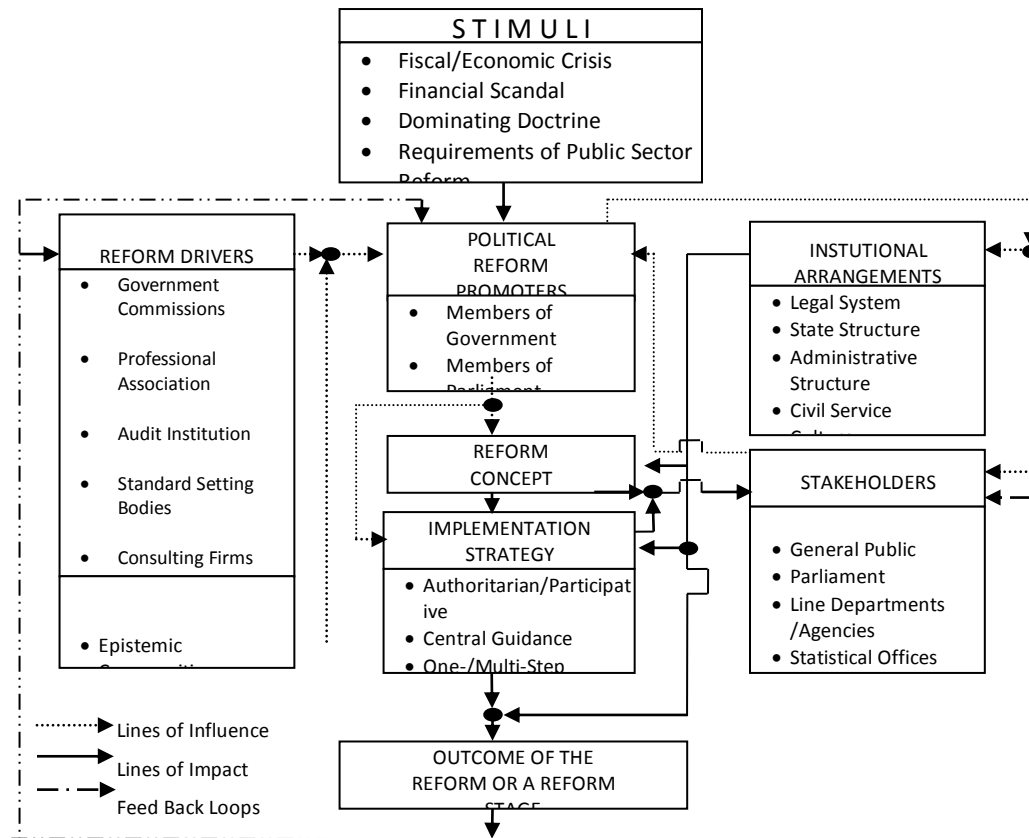
These PBB categories have several advantages in being able to solve the problems of traditional budgeting. Firstly, in contrast with traditional budgeting that only focuses on inputs and/or resource utility, PBB focuses on resource allocation to achieve outputs and outcomes. Therefore, PBB may achieve more efficient resource allocation processes as it is based on program and/or activity performance information (Dongsung, 2005). Secondly, PBB offers flexibility to reallocate money between programs based on performance achievement that reduces inefficiencies caused by unspent budgetary allocations. Moreover, as PBB places emphasis on programs and/or activities rather than expenditure items, it reduces the incentive for public sector managers to increase expenditure or decrease revenue (Dongsung, 2005, Curristine, 2005). Furthermore, similar to program budgeting and PPBS, PBB provides long-term vision to accommodate multi-year programs as part of a modern organisational strategy. Finally, PBB provides more informative performance in each program for executive assessment and legislative approval.

Although PBB is generally regarded as superior to traditional budgeting, there is a need for more understanding of its history and its initial implementation across different geographical contexts. Therefore, this study sought to establish how and why the PBB model was introduced, and used the Lüder FMR model (2002) to examine the historical development of PBB implementation.

## **2.7 The Lüder Financial Management Reform Process Model**

The Lüder FMR model is a conceptual framework (see Figure 4) developed by Professor Klaus G. Lüder in 2002. It originated in 1992 as the "Lüder Contingency Model (LCM)" (Lüder, 1992). The Lüder FMR Model is used in this thesis as it focuses on public financial management reform, which covers budgeting and accounting reform. Other models, such as the Public Management Reform Model

(Pollit and Bouckaret, 2011) focus more broadly on public management reform or a Diffusion-Contingency Model for governmental accounting (Godfrey et al., 2001), which emphasizes governmental accounting reform.



**Figure 4. Financial Management Reform Process Model (Lüder, 2002)**

Figure 4 illustrates how the Lüder FMR model (2002) consists of various stimuli including reform drivers, political reform promoters, institutional arrangements, stakeholders, reform concepts, and implementation strategy variables (Lüder, 2002) which are discussed later in this paper/ chapter.

As Appendix 1 illustrates, the Lüder FMR Model and its original model/parent, the LCM, have been applied to examine governmental accounting reform in many countries (Chan, 1994; Budaus and Buchholtz; 1996; Godfrey et al., 1995; 1996; Christensen, 2002; Lüder, 1994; Mäder and Schedler, 1994; Mellemvik and Monsen,

1995; Mussari, 1995; Pallot, 1995; Jorge, 2003; Jones et al., 2013; Bruno, 2014; Abushamsieh et al., 2013b; 2013a; Lüder, 1992; Montesinos and Vela, 1996; Yamamoto, 1999). As the latest version to be improved, the Lüder FMR model has been applied far less often in than the LCM model; thus, there remains much potential in extending the application of the Lüder FMR model. The following section explains how the FMR model variables in Figure 4 have been used in previous research.

### **2.7.1 *Stimuli***

Stimuli are defined as the events that exist in the early phase of FMR that indicate the need for a new financial management system. These stimuli affect expectations and behaviours and promote reform, and can include fiscal and/or economic crisis, financial scandals, and the dominating doctrine from a superior power (Lüder, 1992; 2002).

A fiscal and/or economic crisis occurs when public debt increases and creates liquidity problems. This can force the public to demand a more informative financial management system (Lüder, 1992). Previous research found that fiscal crisis was an important stimulus in public sector accounting reform in Canada, Denmark, Sweden, the USA, Germany, and the UK (Lüder, 1992; Chan, 1994). Fiscal crisis stimuli strongly influenced governmental accounting reform in other European countries, including Italy, Switzerland, Spain, Finland, Sweden and Portugal (Lüder, 1994; Paulsson, 2006; Jorge, 2003; Budaus and Buchholtz, 1996; Mäder and Schedler, 1994; Khumawala, 1997; Godfrey et al., 1996). However, weak influence from this stimulus occurred in accounting reform in Japan as no significant fiscal stress or economic crisis occurred within that country, with the exception of small events in the late 1970s and 1980s (Yamamoto, 1999).

A financial scandal stimulus refers to negligence in relation to governmental financial management that has consequences for the taxpayer. This type of scandal

can occur due to problems in a traditional system. For instance, federal governmental accounting reform in the US occurred as a result of the failure of the financial management system within the US Department of Housing and Urban Development in the late 1980s. This scandal resulted in billion-dollar losses and triggered the passage of the Chief Finance Officers Act and the formation of the Federal Accounting Standards Advisory Council (FASAB) in 1990 (Chan, 1994). Further, this stimulus provoked accounting reform in India with government financial scandals resulting in the loss of bureaucratic control (Khumawala, 1997).

Dominating doctrine from a superior power is also a stimulus. Examples include governmental accounting innovation in Australia (state of NSW) being influenced by the NPM concept (Christensen, 2002). Furthermore the dominance of Anglo-Saxon accounting and the doctrine of power of commercial accounting have been the main stimuli in the European community and countries including Spain, New Zealand, the Netherlands, Finland, Tanzania, Kenya and Uganda (Budaus and Buchholtz, 1996; Godfrey et al., 1996; Montesinos and Vela, 2000; Lüder, 1994). International public sector accounting standard doctrine has also prompted accounting reform in Portugal, Palestine and Qatar (Jorge, 2003; Abushamsieh et al., 2013a; 2013b).

Public sector reform, inclusive of accounting systems, is often initiated within the public sector to address the limitations of existing accounting systems (Lüder, 2002). This stimulus has influenced accounting reform in the United States, India, and Portugal (Chan, 1994; Khumawala, 1997; Jorge, 2003).

### **2.7.2 *Reform Drivers***

Reform drivers are the recognised institutions or professionals that act as motivators for accounting reform. These drivers could be government commissions, professional associations, audit associations, standard-setting bodies, consulting firms, scholarly networks or epistemic communities (Lüder, 2002).

Researchers have pointed out the impact of these reform drivers. Lüder (1992) provided examples of; (1) the role of standard-setting bodies, including the Public Sector Accounting and Auditing Committee of the Canadian Institute of Chartered Accountants, which has standard-setting responsibility for all three levels of Canadian government, and (2) the Governmental Accounting Standards Board in the United States, which has standard-setting responsibility at the local and state level. Other examples of reform driver influence are found in government accounting reform in Italy (the National Association of Accountant being the official standard setter) and Spain (Commission for Accounting Standards) (Bruno, 2014; Montesinos and Vela, 1996). Furthermore, Government Commissions, Professional Associations, Standard Setting Bodies, and Scholars Networks, were present as drivers for accounting reform in Portugal. However, these drivers did not form epistemic communities (Jorge, 2003). Conversely, government accounting reform in India has not been evidenced by any reform drivers (Khumawala, 1997).

### **2.7.3 Political Reform Promoters**

Political reform promoters include executive members of government or parliament who are impacted by stimuli and who initiate and influence reform. These include the Prime Minister, Minister of Finance, or members of parliament and/or congress who play a key role in government (Lüder, 2002).

Political reform promoters have a significant role in governmental accounting reform. In the USA, the General Accounting Office, the Office of Management and Budget (OMB), Treasury, and the Office of Personnel Management, are key actors on FASAB (Chan, 1994). Furthermore, in Portugal, Qatar, Germany, France, and the UK, the respective MoFs were important political reform promoters that supported accounting reform (Jones et al., 2013; Jorge, 2003; Abushamsieh et al., 2013a; 2013b).

The significant role of members of parliament in governmental accounting reform has been evidenced in Spain, the USA, Germany, Portugal, Sweden, the UK, Italy

and Canada (see Lüder, 1992; Chan, 1994; Mellemvik and Monsen, 1995; Jorge, 2003). However government in India – where there is little political transparency – has shown weak support for reform, and likewise in Italy, where government is strongly dominant over parliament (Khumawala, 1997; Bruno, 2014).

#### **2.7.4 Institutional Arrangements**

Institutional arrangements influence stakeholders and in turn are influenced and shaped by political reform drivers. Institutional arrangements consist of five variables. The *legal system* refers to the basis of law in the Roman-Germanic tradition (comprehensive and detailed systems of statute law/civil/code law) and the English tradition (limited in quantity and precedent-based common law). Within countries under the Roman-Germanic tradition, including Germany, Italy, Portugal and France, procedure

s and principles are stipulated and detailed in codified law within rigid systems that have less flexibility for judgement. Within countries that have British colonial heritage, including the UK, the USA, Canada, India, Australia and New Zealand, the common law system allows for greater flexibility in being able to implement new systems. Thus, countries and jurisdictions with a common law foundation are better able to support accounting reform than jurisdictions with a civil/code law foundation (Lüder, 2002; Lüder, 1992).

Secondly, state structure relates to the structure of the government, being unitary or federal, cooperative or competitive federalism, unicameral or bicameral legislature, or a combination of any of these. A combined unitary structure and a unicameral legislature with strong executive power can be conducive to supporting government initiated reform, as was the case with accounting reform in Portugal (Jorge, 2003). However legislatively induced reform might be better supported by a more balanced division of power such as a federal structure with a two-chamber (bicameral) parliamentary (congress) based system, such is the case with accounting reform in

the USA (Lüder, 1992). Thus, favourable reform support from the state structure is dependent upon who induces reform.

Thirdly, administrative structure relates to the authority of central/federal government regarding decision-making. Decision-making could be centralised or decentralised administratively. It could be concentrated or fragmented within financial management, or it could be found within a central organisational unit. A decentralised structure with financial management functions concentrated within powerful central units could be particularly supportive toward government accounting reform. This has occurred with respect to accounting reform in Canada, Sweden, Denmark and Portugal (Lüder, 1992; Jorge, 2003; Lüder, 2002).

Fourthly, the qualifications of the civil service, refers to the capability of governmental staff to implement reform. Lack of staff capability can result in a failure of the reform process. The lack of professional training for accounting personnel has impeded accounting reform in India (Khumawala, 1997), whilst training for accounting staff has improved accounting knowledge in Portugal and assisted in reform (Jorge, 2003).

Finally, 'culture' refers to the readiness for facing risk and uncertainty, and the social, administrative and political makeup of a society; that is, whether a system is risk-taking or risk-averse, individualist or collectivist, and its degree of openness and responsiveness (Luder, 1992; 1994). Godfrey et al. (1996) found strong influence of the merit culture between residual culture (tribal) and national culture in East and North Africa, which influenced accounting reform, and which may encourage or discourage innovation in governmental accounting.

### **2.7.5 Stakeholders**

Stakeholders are the people or institutions positively or negatively influenced by reform, but the term excludes those who are reform drivers and political reform

promoters. Stakeholders could be the general public/citizens, parliament (non-political reform promoters), the administration (line department and agencies), and statistical officers (Lüder, 2002; Pollitt and Bouckaert, 2011). Reform success also depends on stakeholders receiving or abandoning the new model. Stakeholders can expedite or postpone reform, affecting the success of the implementation strategy and the outcomes of the reform (Lüder, 2002). In Portugal, parliament has an important role in governmental accounting reform, not only as a promoter, but also a stakeholder. Furthermore, the US Congress has provided significant support to the governmental accounting reform process through their support of the OMB (Chan, 1994). However, weak support occurred in Germany after the central government accounting reform project was abandoned by the *Bundestag* (Germany constitutional and legislative body) in 2006 due to lack of funds (Lüder, 2013).

#### ***2.7.6 The Reform Concept***

The reform concept represents full or modified accrual accounting. The reform concept includes all or some features related to the accrual-based accounting system. Reform could include the choice of valuation bases, three financial statements (statement of financial position, operating statement and cash flow statement) as well as consolidated financial statements. For example historical cost valuation is used in many countries, including Germany, Spain, Italy, The Netherlands and Sweden (Lüder, 1994; Montesinos and Vela, 1996), but the UK uses current cost valuation (Lüder, 1992), and merit cost (historical and current) valuation is used in Switzerland, France and Finland (Mäder and Schedler, 1994; Budaus and Buchholtz, 1996).

#### ***2.7.7 Implementation Strategy***

An implementation strategy is a process of implementing reform. It could be authoritarian or participative; involve centralised or decentralised guidance; be with or without a pilot model; comprise one or multiple steps in implementation; include



considerable or minimal user discretion; vary in duration; and include or exclude systematic staff training (Pollitt and Bouckaert, 2011; Lüder, 2002). Previous research has indicated that the implementation strategies vary across countries. Accounting reform in Switzerland is centrally guided, with a short implementation period and a single stage (no pilot model). However, the UK has central guidance with longer implementation periods, multiple transition stages, and a parallel operation with high-intensity staff training. France has central guidance with a short implementation period, a single-stage transition model and parallel operations (Mäder and Schedler, 1994; Budaus and Buchholtz, 1996; Lüder, 1992).

### **2.7.8 *Outcome of the Reform***

The outcomes of the reforms are the result of the process of accounting innovation. The Lüder FMR model allows for the possibility of multiple stages of reform. If there is a need to change the outcome of the reform, it will 'loop back' to the political reform promoters to restart the reform process as a dynamic flow model (Lüder, 2002).

This study used the Lüder FMR model to analyse budgetary reform, with a clear link between each instrument variable discussed previously (stimuli, reform drivers, political reform promoters, institutional arrangements, implementation strategy, stakeholders, reform concept and outcome of the reform). These variables are needed to analyse the development of PBB implementation as part of budgetary reform. Furthermore, this model proposes a feedback loop that allows budgetary reform to be examined in multiple stages. The next section addresses the historical development of PBB.

## **2.8 The Historical Development of Performance-Based Budgeting**

This section investigates the historical development of PBB and provides a brief description of environmental factors that influenced the first period of PBB

implementation (old PBB) across countries that implemented PBB as their new budgeting system. This study found nine countries had sought to implement PBB in the period between the 1940s to 1980s. For a more detailed understanding of its historical development, PBB history is examined by periods commencing from the 1940s to 1960, then the 1960s to the late 1980s.

### **2.8.1 1940s–1960**

The year in which PBB was first introduced is still contested. Evidence has found that the model of PBB was initiated at approximately the same time as the idea of performance management, and was prepared by the International City/County Management Association (ICMA)<sup>4</sup> in the United States from the mid-1930s to 1943. This budgeting type arose in response to several problems. These included perceived budgetary abuse at the local government level (e.g. in New York City), the great depression of the 1930s, and an unstable economic situation before and immediately after World War II (Jones and McCaffery, 2010).

In 1949 the US Commission on Organisation of the Executive Branch of Government, known as the “Hoover Commission” issued the National Security Act (NSA). This constituted the first wave of PBB model implementation proposed by the ICMA. This act implemented PBB in the US Military (Department of Defence) to manage the increased cold war budget after World War II (Dongsung, 2005; Anderson, 2008). The NSA 1949 outlines the clear and simple basic principles of PBB: “all costs which are related to the logical and identified program must be included in the project or budget program” (United States Congress, 1949, p. 3).

In 1950, the US government issued the Budget and Accounting Procedure Act (BAPA), which mandated the implementation of PBB in all government

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<sup>4</sup> ICMA is an association representing professionals in local government management, based in Washington, D.C., USA.

organisations (federal, state and local/city/county) and greater scrutiny of line item expenditure (Jones and McCaffery, 2010; Dongsung, 2005; Schiavo-Campo and Tommasi, 1999; United States Congress, 1950). Its implementation focused on full cost measurement, evaluation of workload, and unit costs (Schiavo-Campo and Tommasi, 1999). Similar to the 1949 NSA, the BAPA focused on measuring program costs and the results and outcomes of various programs (United States Congress, 1950). This implementation phase used a pilot system model that meant the first implementation was in only a few departments (e.g. US Department of Defence and US Department of Building, Safety and Library) to ensure that the model was effective, before being expanded to others (Jones and McCaffery, 2010).

The first PBB implemented in the USA was integrated with program budgeting and focused on the organisational structure, including mission statement, organisational goal/objectives, and core/sub-service and activities (Schick, 2007; Shah, 2007). It therefore focused on how activities with the same objectives were classified in the same program (United States Congress, 1950). However, the first implementation of PBB within the US was considered a failure; for two reasons. First, there was an overemphasis on how budget was allocated to the activities/programs at the expense of creating a link between program inputs and outputs (McGill, 2001). Second, a conflict of interest was found among government organisations that had similar objectives (Dongsung, 2005).

Although difficulties in implementation were found at federal, state and local government levels (cities/counties), there are examples (Los Angeles and Sunnyvale in California) in which PBB was implemented continuously from the 1950s until the present. Benefits achieved include increased budgetary control by the city administrator, and an increase in the quality of program planning which led to better decisions and results (Jones and McCaffery, 2010; Dongsung, 2005). Although the first wave of PBB implementation was not widely successful, the United States did promulgate the idea of PBB to other countries, often via US foreign missions and projects including the Bell Mission, Manhattan and UN projects. PBB

implementation in the US was the first implementation within a developed country. This was later expanded to other countries but with contextualised innovations and modifications based on local customs and the local environment (Jones and McCaffery, 2010).

The Philippines was the first country to implement PBB after the USA. Based on the recommendation of the Truman Economic Survey Mission, the Daniel Bell Mission<sup>5</sup> was launched to provide aid based on an analysis of the economic situation in the Philippines post-independence (Jenkins, 1951). The Bell Mission resulted in the emergence of an agency, the Philippine Council for United States Aid, which was responsible for delivering PBB assistance to the Philippines government (Parsons, 1957). The agreement between the US and the Philippines government forced the issuance of the Republic Act 992, known as the Revised Budget Act, on the 4th June 1954. This Act provided the basic rules for PBB implementation and used a program, activity and projects (PAP) format that was developed under the first PBB model in the US ((Yoingco and Guevara, 1984; Pedro, 1963). However, this format lacked adequate information about performance measurement funding (Parsons, 1957).

In the first PBB proposal, the Philippines legislature enthusiastically supported reform because of the need for more information about budgetary performance. However, after two budget periods the legislature had difficulties in reading and scrutinising the budget given the absence of line item categories. Strategic executives, including ministers, bureau chiefs, agency budget officers, and legislative members, did not understand PBB (Yoingco and Guevara, 1984). Until 1969, there was a disagreement between the Philippines legislature and executive regarding PBB implementation. Moreover, the legislature even argued that PBB implementation was just a “propaganda job” from their ex-colonial power, the United States (Dean, 1986a, p. 5). It meant that the implementation of PBB in the

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<sup>5</sup> Daniel Wafena Bell was a former under-secretary of the United States Treasury (and acting director of the Bureau of the Budget), authorized by President Truman to oversee the mission for the provision of US aid to the Philippines government after WW2.

Philippines, during the first wave, was merely a formal paper report for their donor (the US) without serious consideration as to its intended benefits (Jenkins, 1951; Dean, 1986a).

India was the second non-US country to implement PBB, and similar to the Philippines, followed the trend of budgetary reform that occurred in the US. PBB was initiated by the Estimates Committee in Lok Shaba<sup>6</sup> in its 1957–1958 and 1958–1959 reports. However, although the Indian parliament was interested in this new budgeting form, no substantial action relating to PBB implementation occurred until 1964 (Thimmaiah, 1984; Toye, 1981).

### **2.8.2 1960s–1980s**

Although the first iteration of PBB had spread to other countries, the US government did not pursue PBB because of the difficulties mentioned. Modifications to the first iteration of PBB were made in the 1960s. In 1965, PPBS was introduced as a modification to PBB (Dongsung, 2005). Nonetheless, in 1971 this budgeting system was terminated due to program complexities. Program approvals had become difficult because of the impact of political decisions. However, evidence illustrates that the Department of Defence still continued to implement PPBS under a new name – the Planning, Programming, Budgeting and Execution system (Jones and McCaffery, 2010).

Management by Objectives (MBO) was initiated in April 1973 to replace the PPBS. The MBO model formally linked the federal departments' objectives to their budgetary proposals. The MBO model sought to hold departmental managers responsible for agreeing upon outputs and outcomes. It was intended to centralise goal-setting decisions while at the same time allowing managers to choose how to achieve goals. MBO focused on tracking progress toward goals previously agreed

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<sup>6</sup> Lok Shaba is the Indian lower house of parliament.

upon between a supervisor and subordinate (United States General Accounting Office, 1997). However, difficulties occurred in separating budget formulation processes from political overtones. For instance management of the departments/agencies might approach the White House directly for budget approval purposes. Furthermore, many significant stages of implementation were not attained, as too much focus was placed on setting goals as opposed to actual plan implementation (McGill, 2001; Denhardt and Denhardt, 2008; Tomkin, 1998). As a result of the difficulties experienced with MBO implementation, ZBB was launched in 1976, but it also proved challenging due to difficulties during implementation, including increased administrative burden for federal managers, lack of performance accuracy, and a lack of quantifying decision-packages (McGill, 2001).

In India, PBB preparation continued in 1964 through the preparation of a PBB manual by a group of financial administrators. Formed by the Administrative Reform Commission (ARC)<sup>7</sup> this group was supported by the UN, whose study recommended the implementation of PBB across all central government departments. In 1965, the Indian Government Planning Commission Committee on Planned Projects sought to implement PBB in a pilot project. However, due to the lack of a prepared PBB manual, implementation actually began in early 1970, involving several pilot projects across several ministries and departments including the MoF and the Central Public Works Department. PBB then spread to all ministries and departments over the next eight years (Toye, 1981; Dean, 1986a; Thimmaiah, 1984).

Although the implementation of PBB occurred within all Indian central government departments, little progress was found in several departments at the state level, including public works, public health and irrigation and waterways (Parashar, 2003). Impediments to implementation included the fact that most of the budget

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<sup>7</sup> ARC is an Indian Government committee appointed to both review and provide recommendations about public administration.

documents in all departments were too descriptive and lacked output performance information. Performance information tended to focus on the financial and physical targets (input focus). This occurred due to difficulties with performance indicator development in the programs and activities (Thimmaiah, 1984). Initial experience of PBB implementation in India was similar to that in the US, which primarily focused on the combination of PBB and program budgeting.

Another impediment to PBB implementation in India was the lack of trained staff who understood it, and could prepare the performance budget document. Moreover, although PBB needs performance data for program and activity performance analysis in each department, such information was either inadequate or unavailable. Furthermore, there was confusion surrounding PBB implementation as the budgets were still annual; this did not allow any monitoring of multi-year programs and hindered long-term performance forecasts (Khumawala, 1997). Nevertheless, slow progress continued beyond 1975 as the number of trained staff and states implementing PBB grew, until the economic crisis, which occurred in India in early 1990 (Thimmaiah, 1984).

The old PBB approach also influenced budgetary reform in Sri Lanka, which started at the end of the 1960s with UN support. PBB was introduced through various seminars via the Institute of Chartered Accountants of Ceylon (now Sri Lanka) (ICAC) in 1963 (Dean, 1986b). This PBB version was similar to the PBB model based on the UN Manual of 1965<sup>8</sup>, which established the utilisation of program budgeting and PBB. This system comprised the classification of expenditures based on programs, projects and activities. The UN also supported its implementation by providing UN staff to support the program budget unit in Ceylon's MoF. The first implementation phase in 1969 used a pilot system across three ministries: Education; Health; and Land, Irrigation and Power (Dean, 1986b).

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<sup>8</sup> The 1965 UN Manual on PBB provides guidance on how to implement PBB.

Implementation continued with the establishment of a new budgetary system, which involved issuing PBB guidelines, staff seminars and training, and objectives, programs and performance measurement refinement (Dean, 1986a). However the United Party Government of Prime Minister Sirimavo Bandaranaike, which had been in power since 1970, was defeated in the 1977 election by the United National Party (UNP), led by J.R. Jayewardene, and PBB implementation stalled. A constitutional amendment allowing Jayewardene to become President saw Ranasinghe Premadasa from the UNP become Prime Minister in 1978, and despite a lack of focus, the new Sri Lankan government sought to continue PBB implementation, despite difficulties including insufficient legislative support, little use of performance data in budget reviews, difficulties in accurate program and performance cost determination, and a restructuring of the MoF and its agencies (Dean, 1986b). These problems affected the ability to identify new objectives and performance measurements within the new government structure.

In 1967 and 1968, Malaysia, with support from consultants from the Ford Foundation and the Harvard Advisory Group, sought to implement PBB, aiming to improve the system of managing and controlling resource allocation and utilisation (Dean, 1986c). Treasury Circular No. 5 was issued in 1968 as a regulation that amended the implementation of PBB, now called “programme and performance budgeting (PPB)” (Dean, 1986c, Government of Malaysia, 1968). The 1968 Circular identified two PBB components. The first was programme budgeting, which focused on the program and its cost. The second was performance budgeting, which focused on performance measurement with costs being linked to prior program objectives (Government of Malaysia, 1968). However, several implementation difficulties such as securing appropriate staff, lack of top commitment, and information problems occurred. Another problem persists, between program budgeting and PBB (Dean, 1986c). Even though program budgeting and PBB have similar terminology, there is a different focus regarding implementation. Program budgeting focuses on expenditure by cluster of activities that support common objectives whereas PBB focuses on a present result-based chain (input, output, and outcome) to achieve



specific objectives (Shah and Shen, 2007). The PPB implementation process used a pilot phased system (Dean, 1986c) and focused on how similar activities were collected and classified in the same program, how the goals of the program should be related to the agency's mission, and the total reclassification of expenditure within the program (Chien, 1972). Even though PBB was implemented across several agencies, this appeared to be purely fulfilling instructions from senior management. Implementation tended to lack support from treasury and senior management (Dean, 1986c; Chien, 1972).

PPB implementation in Malaysia continued with the issuance of Circular Treasury No. 3 in 1981 that instructed all agencies to adopt PPB in their budget submissions. However, this circular also faced several difficulties that finally resulted in the decision to change the budgetary model to a new PBB model, namely the Modified Budget System (MBS) in the late 1980s (Dean, 1986c). However, evidence suggests that PBB implementation in Malaysia was constrained by a lack of commitment on the part of agency steering committees, budget officers and managers in the implementation unit (Dean, 1986c).

In 1969, Philippines President Ferdinand Marcos announced the implementation of a PBB variant as an effective method of budgetary control. This variant was similar to the implementation of PPBS in the US, and was termed an integrated budget system (IBS). IBS implementation continued with the issuance of martial law in 1972 that instructed all agencies to implement PBB despite rejection by the legislature (Laya, 1980). PBB implementation in the Philippines was therefore strongly dominated and driven by the executive branch, which ignored the views of legislators. Other constraints included inadequate performance data within government budgets and a lack of trained staff (Yoingco and Guevara, 1984). In 1979, the Philippines implemented a variant of PBB, the Management Audit and Improvement Program. This budgeting form required all agencies to use performance indicators to set up objectives for their achievement. These objectives were used as a standard to monitor the achievement of each agency (Dean, 1986a). This illustrates that although this

model still adopts the principles of PBB, variation and modification exist based on local interest, including approaches to performance measurement, budgetary form and valuation.

PBB has also been adopted in the Netherlands. In the mid-1970s, budgetary reform resulted in the replacement of the input budget with an output budget through new provisions in the Financial Law (*Comptabiliteitswet*). This law required Dutch ministries to provide performance information in the budget process. However, performance information was only provided in the budget appendix as opposed to the main document. Further, the budget composition did not change and the format was in many respects similar to previous budgets (Van Nispen and Posseth, 2006). The idea of PBB also influenced UK financial management reform in the late 1970s through the Financial Management Initiative (FMI). However, this approach had the wider focus of improving accountable management in government as a part of an efficiency strategy, rather than merely in a budgetary context (Gray and Jenkins, 1986). Similar to the UK, Australian budgeting reform commenced in 1983 but focused on management accountability using the Financial Management Improvement Program (FMIP)<sup>9</sup>, which emphasised that managers use clear objectives and performance measures to improve their financial management system (Hawke, 2007).

In Denmark, budgeting focused on using management-oriented performance information to improve efficiency and provide value for the taxpayer. The Danish program first focused on program modernisation in the 1980s with a later introduction of performance-based contracting in the early 1990s. Similar to Denmark, financial management reform in New Zealand occurred in the 1980s after the enactment of the Public Finance Act 1989. Focusing on accounting and budgetary reform, it was fully implemented during the 1990s (Mascarenhas, 1996).

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<sup>9</sup> The FMIP was the initial program designed to enhance financial management which included planning, budgeting and accounting as part of a broad ranging public sector reform strategy. The program emphasised program-based planning, and reporting on cash movements (Hawke, 2007).

The next section applies the Lüder FMR model (2002) as a conceptual framework to examine the factors influencing the implementation of PBB from approximately 1949 to 1989.

## **2.9 The Lüder FMR Analysis**

### **2.9.1 *The Stimuli***

The stimuli for the first iteration of PBB implementation differed across countries. For instance, stimuli in the USA included fiscal stress and financial scandals (Dongsung, 2005; Jones & McCaffery, 2010; McGill, 2001; Schiavo-Campo and Tommasi, 1999), the identification of which then led to greater measurable performance in the budgetary process of government organisations. In turn, this led to budgetary reform, with the implementation of PBB replacing the traditional budgeting model. However, the stimuli for PBB implementation in other countries, including the Philippines, India, Malaysia, Sri Lanka and the Netherlands, emanated through dominant US doctrine via aid programs, which ‘overvalued’ the success of PBB implementation within these developing countries at the time, even though the US had experienced problems relating to PBB implementation (Dean, 1986a).

### **2.9.2 *Reform Drivers***

A variety of reform drivers influenced PBB implementation internationally. The ICMA, led by Clarence Ridley, was the reform driver for the US, which developed PBB. From 1927 until 1950 ICMA promoted the concept of performance measurement. In the case of the Philippines, the reform driver for budgetary reform was the US consultant under the Daniel Bell Mission that assisted PBB capacity building within the Philippines government (Parsons, 1957; Pedro, 1963; Dean, 1986a). As previously noted, the ARC was the main reform driver that forced the implementation of PBB in India. This commission had an important role in ensuring PBB implementation was implemented on schedule. Similar to the Philippines

experience, US doctrine also significantly influenced PBB implementation in India. Several academics from ICAC were important drivers for PBB implementation in Sri Lanka, together with several UN consultants (Dean, 1986b).

### ***2.9.3 Political Reform Promoters***

In some countries, including the US, UK, the Philippines, India and Sri Lanka, both legislative and executive members supported PBB implementation. In the US, examples were the President's Bureau of Budget and the US Congress (Dongsung, 2005; Jones, 2010; Schiavo-Campo and Tommasi, 1999). In India the MoF and members of parliament (Khumawala, 1997) supported PBB, whilst in the Philippines it was the President, the Minister of Finance and the legislature. However, in the Philippines the legislature withdrew its support for implementation after two years. This withdrawal of support occurred because the legislature had difficulty understanding PBB and felt that the new budgeting model was an attempt to weaken their role in the budgetary approval process (Parsons, 1957; Pedro, 1963; Dean, 1986a). Furthermore, in Malaysia, the Treasury was the only agency that promoted and forced the implementation of PPB, which included creating the budget divisions and Financial Management System Units for PPB implementation and guideline development (Chien, 1972).

### ***2.9.4 Institutional Arrangements***

The institutional environments within countries that implemented PBB between 1949 and 1989 were mostly both conducive to and supportive of it. Firstly, the legal system in these countries often had its origins within precedent and case law based on the English legal system. This legal system is flexible and simple, and is not codified, thus providing favourable conditions for PBB implementation that requires flexibility to manage budgets. However, the Netherlands, Denmark and many countries follow a continental legal system, which is often unfavourable to PBB implementation (Dean, 1986a; Van Nispen and Posseth, 2006). Secondly, several

countries (including the USA, India, and Malaysia) that use a federal/state and decentralised administrative structure have given more flexibility to local decision-makers to manage their budgetary system (McNab and Melese, 2003). However, very few countries (e.g. the UK and USA) have sufficient skilled government employees able to effectively implement PBB. Poister and Streib (1999) found more than 80 per cent of US federal government staff had the necessary skills to analyse the data on performance measurement. The necessary culture of openness and transparency supporting implementation was only found in certain countries (again, the UK and USA).

In summary, institutional arrangements were influenced by political reform promoters and stakeholders, who built pressure around the concept of reform and its associated implementation strategy. Therefore, the readiness of institutional arrangements was an important factor that influenced PBB implementation, in addition to a legal system based on English common and case law tradition that provided the necessary flexibility. Moreover, unskilled staff who lacked the necessary capabilities were a barrier to PBB implementation.

### **2.9.5 Stakeholders**

In countries such as the UK, USA and the Netherlands, congress or parliament, and the wider public as stakeholders, had a positive influence on PBB implementation. Strong public awareness of budget transparency, as the embodiment of a developed country, provided support for PBB implementation (Dongsung, 2005; Van Nispen and Posseth, 2006; Gray and Jenkins, 1986).

Different stakeholder characteristics existed in developing countries. In the Philippines, the parliament as a stakeholder had a positive influence on the first budget reform. However, because budgetary reform progress was slow, weak parliamentary influence appeared to be a barrier to implementation (Parsons, 1957; Dean, 1986a). The Indian parliament had a positive influence in relation to budget

reform as it needed better measures of performance in the budget. However, the general public had a weak influence on PBB implementation (Toye, 1981). This characteristic was also found in other developing countries such as Malaysia and Sri Lanka (Dean, 1986a), because PBB was implemented soon after independence. Thus, access to information by stakeholders was still poor due to a lack of developed communication channels.

### ***2.9.6 Concepts of Reform***

The concept of reform varied across countries depending on the approach to PBB implementation. In the US, the focus was on categorising program or project costs for the first phase of PBB implementation. In the second reform phase, emphasis was on developing a planning and programming budgeting system, which then led to more efficient oriented ZBB (Dongsung, 2005). Similarly, the Philippines commenced reform using the PAP format, whilst Malaysia used PPB that was similar to the first phase (old) PBB model in the US. In the second reform phase, the Philippines used a concept of budgeting that focused on the effectiveness of budget control. Moreover, budgeting reform continued in the third phase, focusing on management audits to enhance performance information. However, in the second reform, Malaysia enhanced the reform concept by focusing more on performance measurement. On the other hand, India and Sri Lanka's concepts were influenced the first implementation of PBB in the US that focused on government programs and project classifications for cost allocation (Dean, 1986a). The concept of reform in other countries, including the UK and Australia, places emphasis on the wider aspects of financial management that contain reforms not only to budgeting but to accounting and management accountability (Sharifi and Bovaird, 1995; Hawke, 2007).

### ***2.9.7 Implementation Strategy***

A variety of PBB implementation strategies were employed. For instance, in the first implementation phase, the US used the Budget and Accounting Procedures Act of

1950 for central guidance; engaged stakeholder participation in every stage; and used a pilot phased and multi-step reform process (Dongsung, 2005). The Philippines also used central guidance based on the Republic Act 992. They used a pilot system across many phases, which was generally perceived as authoritarian in nature (Yoingco and Guevara, 1984). Similarly, Sri Lanka's implementation strategy used a pilot phased system, with early implementation perceived as having good progress; however, implementation became stagnant after a change in government leadership (Dean, 1986b). A change in agency structure in Malaysia and errors in staff transfers resulted in slow implementation (Siddiquee, 2006).

### **2.9.8 Outcome of the Reform**

The process of budgetary reform across several countries continually evolved toward a 'best practice' model. For instance, the implementation of PBB in the US government changed from old PBB, to PPBS, to MBO and then to ZBB (Jones and McCaffery, 2010). Furthermore, in 1990 the budgeting model returned to a newer version of PBB. Thus, although the old PBB faced implementation difficulties, it resulted in fundamental concepts of budget reform being preserved, which continued into subsequent PBB variations and modifications. Budget reform in the Philippines had a similar outcome that resulted in a change to a new phase of PBB modification; however, this change did not alleviate efforts to find a more appropriate budget model in line with local conditions in the Philippines. Active reform was also noted in Malaysia, where reform was quick and required only thirteen years from the launch of the first model of PBB to the launch of the second reform (MBS). In contrast, up until the 1980s, India had only one experience with budgetary reform, that being based on the US's old PBB. However, in the 1990s it modified and revised the original format of PBB through a re-evaluation, which saw dynamic change that reflected better PBB practices that included local content. Sri Lanka continued to experience delays in PBB implementation because political reform was not in line with budgetary reform, and PBB implementation stagnated accordingly. These outcomes experienced across countries are evidence that

dynamic reforms are needed in order to achieve the objective of creating better budgeting systems (Dongsung, 2005; Jones and McCaffery, 2010; Dean, 1986a).

## **2.10 Conclusions**

This review of the historical development of PBB implementation leads to several conclusions.

First, the motive underpinning the first implementation of PBB was the rise in public sector community demand for more informative and efficient budgets that would overcome and highlight fiscal stresses and financial scandals. However, these stimuli only occurred in the first PBB implementation phase in developed countries such as the US, the UK, Australia and Denmark. In several developing countries, the motive for PBB implementation was the influence of a dominant budgeting system from a larger country that had prior colonial or donor program influence, which provided the necessary stimulation for these countries to reform their budgetary model. This is evident from the findings of several US and UN donor programs regarding PBB implementation in many developing countries. This external influence was the main underlying reason why there were difficulties implementing PBB in developing countries in the initial phase as there was lack internal motivation and commitment in PBB implementation.

Second, environmental factors such as legislative support, executive action, and public sector community support are important for successful PBB implementation. Thus, this finding is consistent with the proposition in this paper that environmental factors within the Lüder FMR model (2002) are also applicable within a budgeting reform context.

Problems in the first phase of PBB implementation occurred for four reasons:

- resistance within organisations to received PBB as their budgeting system;



- there was a lack of information about PBB, and that information should have been transferred to all stakeholders involved in PBB before implementation;
- too few trained staff who understood the PBB model and how it was to be implemented; and
- the limitations of various information systems during the first phase.

These findings are consistent with Dongsung (2005), who argued that different levels of implementation success between old and new PBB lies in the rise of computer technology and management applications to assist the process. Robinson (2002) also argued that good performance information systems, performance indicator formulation, management accounting systems, and analytical and evaluation tools should be in place before PBB implementation.

On the other hand, the budgetary reform problems within several countries occurred because they were not part of other governmental reforms, such as accounting, auditing, and political reforms. This finding is consistent with Ho (2011) and Melkers & Willoughby (2001) who argued that to fully comprehend the significance of PBB, complementary reforms are necessary.

There are limitations in using the Lüder FMR model (2002) to examine research on budgetary reform within an historical perspective. Effective use of Lüder within an historical context requires more chronologically detailed data to examine deeper levels of analysis relating to events across countries. Therefore the Lüder FMR model (2002) can be more appropriately used when examining budgetary implementation from an historical perspective using a single case study country to obtain greater detail on the events that shape changes in the budgetary process, and a deeper level of analysis of the underlying meaning underpinning why events occur, and why actors and stakeholders act in the way they do. Alternatively, the Lüder FMR model (2002) can be applied across countries using comparative research without an historical overview.

Based on the outcomes of this paper, two suggestions for future research are proposed. First, there is a need for the use of the Lüder FMR model (2002) within a single country analysis for a deeper understanding of how reform occurs, with the ability to draw upon more context-specific data and the reasoning underlying specific actions through interviews with key stakeholders in the change process. Second, based on evidence relating to isomorphism and decoupling in the implementation of budgetary reform in several countries that has been outlined in this paper, and the role that various actors play in the reform process, it is necessary to examine specific country reforms using institutional theory as a lens by which to interpret events.

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### 3. Paper 2: The Transformation of Indonesia's Central Governmental Budgetary System

#### 3.1 Abstract

**Purpose:** This study investigated how and why the Indonesian central governmental budgetary processes changed from traditional to performance-based budgeting (PBB) in 2003. Furthermore, this study examined the extent to which isomorphism was evident during PBB implementation in Indonesia. Indonesia is a developing country currently experiencing the early stages of PBB implementation.

**Design/methodology/approach:** This study was motivated by Timoshenko and Adhikari's (2009) call to examine the institutionalisation process surrounding budgetary reform. Primary data was obtained through interviews, an examination of reports and other documentation from governmental bodies and international agencies, donor agency reports, and academic literature.

**Findings:** The change to the budgetary system was a consequence of the Indonesian central government's institutional environment. Two phases of PBB implementation occurred within the Indonesian central government. In the initial period (1990s), most of the impetus for change originated from Indonesian technocrats (internal governmental officers and academics) who proposed PBB after their participation in an international public sector workshop. During the second period (2003), pressure to implement PBB emanated from the IMF and the World Bank, and the Indonesian central government responded with moderate coercive pressure, albeit with an avoidance strategy. This avoidance response, coupled with the occurrence of weak mimetic and strong normative (from Indonesian technocrats) pressure in the institutionalisation of PBB, is evident from the modified form of PBB used across the Indonesian central government. Further, this avoidance strategy appears to be the reason the Government sought legitimacy from the international community rather than the rational motive of improving efficiency.

**Research limitations/implications:** The research involved a small number of respondents with a central role in the Central government's budgeting reform, hence caution should be exercised in interpreting the results as a perfect representation of the Indonesian central government's PBB implementation.

**Originality/value:** The originality of this study lies in the utilisation of new institutional sociology theory as a lens to examine the implementation of budgetary reform using PBB within a developing country.

**Keywords:** Institutional theory, performance-based budgeting, government, Indonesia

### **3.2 Introduction and Purpose**

Performance-Based Budgeting (PBB) has been implemented across developed and developing countries since 1949, as part of a public sector reform process that sought to embed 'good performance' measurement within public sector organisations (see Franklin, 2006; Aristovnik and Seljak 2009; Schick, 2007). Several researchers (see Curristine, 2005a; Joyce, 2011; Robinson, 2007; Ho, 2011) have suggested that PBB is a budgeting system that links resource allocation to outputs and outcomes using performance information within the budgetary documents. Furthermore, performance information and its measurement as depicted in the budget documents are believed to significantly influence a legislature's budget approval (see Curristine, 2005a, Joyce, 2011, Robinson, 2007). However, despite the implementation of PBB across various countries, some problems have become apparent.

Firstly, difficulties associated with performance information measurement and its relevance to the budgeting process are evident during PBB implementation. For instance, the lack of valid performance data and difficulties in measuring performance (input, output and outcome) are common (see also Küchen & Nordman, 2008; Blöndal and Ruffner, 2004; Van Nispen and Posseth, 2006; OECD, 2009; Karkatsoulis, 2010). Secondly, it seems that the principal reason for several developing countries' (India, Malaysia, Sri Lanka and Philippines) implementation of PBB budgetary reform is institutional pressure from a 'superior' country (e.g. the United States of America), and international organisations (e.g. the United Nations) (Dean, 1986a; 1986b; 1986c; Pedro, 1963; Chowdhary, 2001). Thus, the motivation for budgetary reform is one of organisational legitimacy rather than a fundamental operational improvement within the organisation (Covaleski and Dirsmith, 1988), leading to the proposition that new institutional sociology (NIS) theory can provide a lens through which to explain institutional pressure for budgetary reform.

Timoshenko and Adhikari (2009) suggested that further research on the institutionalisation process of accounting and budgetary reform in a central government context is warranted. These authors used NIS to argue that the institutionalisation of new budgetary processes in the Russian central government were infused within organisations through coercive power, and classified as an effort by the Russian government to seek legitimacy from stakeholders, thereby facilitating the portrayal of the government as modern. The usefulness of NIS in this study was further supported by Meyer and Rowan's (1977) argument that organisations, which are influenced by phenomena in their operational environment, tend to become isomorphic through technical and exchange interdependencies. Isomorphism is referred to as a homogenisation of organisations that reflects how they adopt and embed other organisational structures and procedures in response to international pressure (DiMaggio and Powell, 1983). Evidence of institutional pressure for budgetary reform through PBB implementation across several developing countries previously mentioned, is evident within the literature (Dean, 1986a; 1986b; 1986c; Pedro, 1963; Chowdhary, 2001). Given these problems confounding our understanding of the utilisation of PBB in developing countries, this research sought to examine how and why the Central Governmental budgetary processes in Indonesia changed to PBB. This research focused on the implementation of PBB across Indonesia's systems from 2003 to 2010 and the government's motivation for doing so.

This research paper had four objectives, to:

1. evaluate the institutional processes of the Indonesian central government's budgetary reform;
2. examine the historical events leading up to PBB implementation within the Indonesian central government, through the enactment of Law No. 17/2003 on State Finances (*Undang-undang (UU) No. 17 Tahun 2003 tentang Keuangan Negara*);
3. explore the factors influencing the Indonesian central government's decision to implement PBB; and

4. scrutinize the extent to which the Indonesian central government has implemented PBB.

This study applied NIS for evaluating Indonesian budgetary reform, particularly the history and implementation of PBB. This study also examined the occurrence of institutional pressures and the Indonesian central government's response to these pressures in the institutionalisation of the PBB system in Indonesia.

The remainder of the paper is structured as follows. The next section explores the literature regarding PBB, its development in public sector budgeting, and why it is important to study its implementation in Indonesia. The third section explains how the theoretical framework (NIS) has been applied within a reform context. The fourth and fifth sections respectively examine the research method and the Indonesian budgetary reform analysis using NIS. The final section summarises the findings in relation to the institutionalisation of PBB in the Indonesian central government, the historical development of and factors influencing PBB implementation in Indonesia, and the extent to which the Indonesian central government has implemented PBB. Furthermore, this final section examines the implications and the limitations of this research, and gives recommendations for future research.

### **3.3 Performance-Based Budgeting**

Since the 1980s PBB has dominated budgetary reform internationally; it focuses on measuring performance, integrating performance reviews with budget submissions, and allocating costs within programs and activities (Curristine, 2005; Moynihan, 2006). Governmental budgetary reform involves a change of the budgeting system within government that not only allocates scarce resources to activities, but fulfils society's demand for the management of public budgeting through the allocation and utilisation of resources in a responsive, efficient and effective manner (Wildavsky, 1961; Schiavo-Campo and Tommasi, 1999). Moreover, some researchers

believe that PBB has the ability to address the flaws of traditional budgeting – flaws that inhibit the maintenance of an efficient and effective competitive environment for modern public sector management (see Hope and Fraser, 1999; Mascarenhas, 1996; Jones and McCaffery, 2010; Dean, 1986c; Schick, 1998; McNab and Melese, 2003). Additionally, traditional budgeting has been criticised for reducing public transparency, and being irrational because it emphasises organisational resources (personnel, material, money and equipment) utilisation instead of achievement of an organisation's goals (Kelly, 2003; Wildavsky, 1978).

The OECD (2007) suggested that there are three categories of PBB: presentational performance budgeting, performance-informed budgeting and direct-performance budgeting. **Presentational performance budgeting** incorporates performance information within the budget or other government documents, the purpose of which is to improve budget accountability of agencies and departments. However, government and budget committees rarely use presentational performance budgeting information for resource allocation decisions because this information constitutes primarily background information, such as a governmental department's vision, mission, goals and objectives (Curristine, 2005). Therefore, presentational performance budgeting information is not related to historical or planned future expenditure, and often does not reflect an organisation's real performance, and there is no link between performance information and results. Presentational performance budgeting was found in the first wave, that is the old era (1949–1980s) of PBB implementation in several countries, including the USA, the Philippines, India and Malaysia (Dongsung, 2005; Dean, 1986a).

**Performance-informed budgeting** is a budgeting approach that uses performance information in the budget process to distribute funds. Whilst performance information is used significantly in the budgetary decision-making process, and has a role to play in budget accountability and organisational planning, it does not address issues or challenges surrounding resource allocation (Sterck and Scheers, 2006). The reason for this is the lack of suitable information being used within a

strategic plan for performance measurement and in the allocation of cost (Joyce, 2011; OECD, 2007), meaning the relationship between performance information and budget decisions is indirect. Performance-informed budgeting was predominant throughout the second wave (1990s–present) of PBB implementation across developed countries including the USA, Finland, Spain, Australia and the Netherlands (Joyce, 2011; Van-Nispen & Posseth, 2009; OECD, 2007).

**Direct or formula performance budgeting** involves allocating resources, both in the budgetary proposal and decision process, that is, it presents a budget estimation that is directly related to output and outcome. It directly and explicitly associates performance results with funding, which improves budget accountability and resource allocation (OECD, 2007). Additionally, this form of budgeting sets clear and explicit output measures linked to unit cost information; thus, it requires appropriate information about strategic direction, results measurement and cost allocation. Direct or formula performance budgeting is also known as advance budgeting, and has been implemented within the health and education units in the public sectors of Norway and New Zealand (Anderson, 2008).

The three categories of PBB mentioned above are also known as the steps constituting PBB implementation, commencing from the initial category (presentational performance budgeting) and moving toward an advanced category (direct performance budgeting). It means a country that has implemented direct performance budgeting is more advanced in PBB implementation than one that has implemented performance-informed budgeting or presentational performance budgeting. These categories are beneficial in understanding the extent to which a country has implemented PBB.

PBB seeks to provide a more efficient and effective approach to resource allocation within government, which is part of the notion of New Public Management (NPM) (Osborne, 1993; Anderson, 2008; Shah and Shen, 2007; USA Congress, 1950). NPM became a new philosophy for the public sector, and has been a tool to guide

governmental structural reform, to ensure that government as a service provider delivers the necessary accountability to its citizens (Pollitt and Bouckaert, 2011), and that governmental management practices emphasise efficiency and effectiveness (Dunleavy & Hood, 1994). Pollitt and Bouckaert (2011) argued that NPM reform has four aspects: (1) finance and budgeting, (2) personnel management, (3) public sector organisation (e.g. specialisation, coordination, scaling and decentralisation), and (4) performance measurement systems. NPM has been applied in developed countries including the United Kingdom (UK), the USA, the Netherlands, Singapore, Australia and New Zealand, and also in developing countries including Malaysia, Mexico, Thailand and India ((Dongsung, 2005; Pollitt and Bouckaert, 2011).

As part of NPM reform, organisations including the IMF, the World Bank, the UN, the OECD, and developing country donor programs such as the United States Agency for International Development (USAID), Canadian International Development Agency (CIDA) and the German Organisation for Technical Cooperation (GTZ) (Shah and Shen, 2007; Schick, 2007; Ayeni, 2002; Binnendijk, 2000), were instrumental in promulgating PBB globally throughout the 1980s. However the implementation of PBB has been subject to criticism. Research (see Melkers and Willoughby, 1998; Wang, 2000; Moynihan, 2006; Ho, 2011) has questioned whether PBB can influence both performance measurement and improve the ability to support decision-making concerning the allocation of resources. Further, Dongsung (2005) found that US federal and state governments experienced difficulties in measuring the extent to which some PBB programs contributed toward specific outcomes in subsequent years. Moreover, several researchers (see Melkers and Willoughby, 1998; Melkers and Willoughby, 2001; Joyce and Tompkins, 2002; Jordan and Hackbart, 2005) found weak linkages between performance and resource allocation at the state level in the USA. Similar difficulties occurred in other countries, including Malaysia, Bolivia, Thailand, Chile, Tanzania, Canada and Finland (Shah and Shen, 2007; Curristine, 2005b; Siddiquee, 2006). In several developed (e.g. Canada and France) and developing countries (e.g. Bolivia, Tanzania, South Africa and Thailand), line-item forms (as a component of traditional



budgeting) are still used in conjunction with PBB implementation (Shah and Shen, 2007; Curristine, 2005b).

Regardless of the scepticism related to PBB being able to strengthen the links between the inputs, outputs and outcomes of public spending, the Indonesian central government decided to implement PBB as its budgeting system. As a developing and transitioning country, Indonesia experienced transformation from an authoritarian and centralised system to a more democratic government system in 1999, resulting in fundamental change to governmental financial management, specifically the budgeting system. Thus, this study evaluates why and how the Indonesian central government implemented PBB. Further, the aforementioned implementation difficulties found in other countries may have significance for this research in that the Indonesian central government may have encountered similar implementation problems.

Previous research on Indonesian reform was focused on governmental structure and political, accounting reform, and performance measurement reporting in local government (see Harun and Robinson, 2010; Djamhuri and Mahmudi, 2006; Djamhuri, 2009; Hadiz, 2004; Guess, 2005; Hadiz, 2013; Mimba et al., 2013). However, there is no extant research investigating how and why changes in the Indonesian central government budgetary system took place in the period after the enactment of Law No. 17/2003 on State Finances (*UU No 17 Tahun 2003 tentang Keuangan Negara*) to 2010. Law No. 17/2003 is a fundamental regulation that officially required the Indonesian central government to reform its financial management by adopting accrual accounting and a PBB system. Thus, there is a need for further in-depth exploration of the Indonesian central government budgetary system, particularly relating to the implementation of PBB, in order to gain a better understanding of why the Indonesian central government considered (and continues to consider) PBB superior to the traditional budgeting system. This study also evaluated the reason why the Indonesian central government budgetary system changed from traditional budgeting to PBB in 2003.

Several researchers (Djamhuri and Mahmudi, 2006; Djamhuri, 2009; Harun et al., 2012; Harun and Robinson, 2010; Hadiz, 2004; Hadiz and Robison, 2013) have used institutional theory to examine Indonesian governmental (political and accounting) change. Hadiz (2004) and Hadiz and Robison (2013) argued that global organisations such as the IMF, the UN, the Asian Development Bank (ADB), the World Bank, other countries outside Indonesia, and the central government itself have a significant impact (institutional pressure) on democratisation and decentralisation within the Indonesian government. More specifically, Djamhuri and Mahmudi (2006), and Djamhuri (2009) found that coercive isomorphism manifested through IMF pressures and legal obligations (regulations) occurred when implementing NPM reform and accrual accounting within Indonesian local government. Harun (2012) argued that the institutionalisation of the accrual accounting system within Indonesian local government was one of coercion through the IMF, the World Bank and government regulation, which then garnered normative support through technocrats<sup>10</sup> within government. Harun (2012) also found that Indonesian accrual accounting practices tend to mimic those of Australia and New Zealand.

Given that previous research (i.e. Djamhuri and Mahmudi, 2006; Djamhuri, 2009; Harun et al., 2012; Harun and Robinson, 2010; Hadiz, 2004; Hadiz and Robison, 2013; Harun, 2012) has identified the influence of international and regional organisations and regulations in the institutionalisation of democracy, decentralisation and the accrual accounting system in Indonesia, it is relevant for this paper to examine the nature and outcomes of institutional pressures on Indonesian central government budgetary system reform, particularly the implementation of PBB from a NIS perspective. The changes from a traditional to a PBB budgeting system within the Indonesian central government appear to be shaped by the environment, including influence from the superior country donor project (e.g. the United States Agency for

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<sup>10</sup> 'Technocrats' as outlined in Harun (2012) constitute a group of Indonesian scholars and government officers, particularly from the Ministry of Finance that had an idea to reform the political system and public sector practices in Indonesia.

International Development (USAID), Canadian International Development Agency (CIDA), the Australian Agency for International Development (AusAID), Japan International Cooperation Agency (JICA), and the *Deutsche Gesellschaft für Internationale Zusammenarbeit* (German Organisation for Technical Cooperation – GTZ)), international organisations (e.g. the IMF, the World Bank, and the ADB) and government regulations. Research has also found that institutional pressure from the US and UN campaigns (coercive), as well as professional/standard body initiatives (normative), influenced PBB implementation in the Philippines, Malaysia, India, and Sri Lanka (see Dean, 1986a; Dean, 1986c; Dean, 1986b; Pedro, 1963; Chowdhary, 2001).

The next section discusses NIS as the framework for this study, including its usefulness in analysis of Indonesian budgetary reform with specific reference to the implementation of PBB.

### **3.4 Theoretical Framework**

The purpose of this section is to provide an overview of NIS as a framework for understanding the complexities of budgetary reform. An initial overview of the theory is provided, followed by a brief discussion on the associated isomorphic pressures, then a review of extant public sector research to promote understanding of budgetary reform within this sector.

NIS is one of the prominent perspectives within New Institutionalism (Hall and Taylor, 1996). It is unique because it places emphasis upon culture, social belief and values as a basis for influencing organisational behaviour (Meyer and Rowan, 1977). Lounsbury (2008) stated that social structures influence organisational behaviour. NIS does not suppose that organisational behaviour is driven by individual characteristics. This is supported by DiMaggio and Powell (1983), who implied that organisational behaviour is not influenced solely by any one individual, but rather is dependent upon the ‘supra-individual unit’ or institutional factors.

Furthermore, NIS opposes the perspective that the motives that stimulate individual and organisational group behaviour are based on rational choice assumption. Rational choice assumption is evident within market-based accounting theory, and is based on the premise that economic actors are considerate and seek to use the most efficient means by which to achieve economic goals (Carruthers, 1995 p. 317). NIS rejects the assumptions of methodological individualism and individual rationality. In that way, it embraces the prominence of culture, in particular how the social world is created and cognised by social actors. Furthermore, this theory considers “that people live in a socially constructed world that is filled with ‘taken-for-granted’ values and procedures. Action is then neither on purpose nor conscious, but is undertaken unconsciously and as a matter of routine” (Carruthers, 1995, p. 315).

NIS is based on the principle that organisational structure and behaviour is shaped by the social environment, including social belief and value, and also culture (Carruthers, 1995). Thus, from an NIS perspective, organisations reform their structures and processes to adapt to external outlooks about what is deemed acceptable or legitimate (Hoque, 2005, p. 370). Covalleski and Dirsmith (1991) argued that the general theme of NIS is one of organisational survival. In order to survive organisations must obey social norms of acceptable behaviour, which might not be compatible with achieving high levels of production efficiency. This process is both cultural and political, and focuses on legitimacy and power as opposed to efficiency alone (Carruthers, 1995). Many aspects of an organisation's formal structure, policies, and procedures conform to institutionalised rules, which assist in its ongoing legitimisation within society (see Scott, 2008; Meyer and Rowan, 1977).

NIS provides analytical tools to develop explanations for how public sector reform can be legitimised (Pettersen, 2001). Over the years, social scientists have developed multiple definitions of legitimacy. Legitimacy refers to an evaluative process whereby an organisation is justified by other organisational, public or superordinate systems, and bestowed rights to exist (Suchman, 1995). Accordingly, legitimacy connotes "congruence between the social values associated with, or implied by

[organisational] activities, and the norms of acceptable behaviour in the larger social system" (Parsons, 1956, p.175). Suchman (1995) defined legitimacy as a generalised perception or assumption that "the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (p. 574). Legitimacy is part of the public perception of an organisation, yet it is subjective. It reflects the degree to which an organisation's particular claim is respected and given social acceptance and value by respondents. An organisation might deviate:

*....dramatically from societal norms yet retain legitimacy because the divergence goes unnoticed. Legitimacy is social constructed in that it reflects a congruence between the behaviours of the legitimated entity and the shared (or assumedly shared) beliefs of some social group; thus, legitimacy is dependent on a collective audience, yet independent of particular observers (Suchman, 1995, p.574).*

NIS reinforces the central tenet of legitimacy, which means that that organisational success and survival depends on how the organisation adopts 'institutional templates' or 'myths' that most organisations have successfully implemented in their environments (Ryan, 2002). NIS is sociological in origin, emerging from cognitive psychology theory, cultural studies, phenomenology and ethnomethodology (Scott, 2008); it has been increasingly applied in the study of public sector management reform and is the prevailing theory for examining internal changes within public sector organisations (Greenwood and Hinings, 1996). NIS holds that in order to achieve legitimacy, all organisations will adopt similar procedures, systems, and values. When legitimacy leads to congruence, this is referred to as isomorphism, which has direct implications for an entity's survival (Hoque, 2005). DiMaggio and Powell (1983) label isomorphism as the procedure by which organisations embrace the similar structures, methods, philosophies and practice, which is also referred as homogenisation.

Scott (2008), DiMaggio and Powell (1983), and Covaleski and Dirsmith (1988a) argued that institutional pressures can lead to similarities in organisational practices.

Within NIS the adoption of organisational values, beliefs and methods are usually the result of three pressures: coercive, stemming from political influence; mimetic, resulting from standardised responses to uncertainty; and normative, associated with professionalisation (Djelic and Quack, 2008; Meyer and Rowan, 1977; DiMaggio and Powell, 1983; Frumkin and Galaskiewicz, 2004). These three pressures are discussed below.

#### **3.4.1 Coercive Pressures**

Coercive pressures reflect “formal and informal pressures exerted on organizations by other organizations, upon which they are dependent and by cultural expectations in the society within which the organizations function” (DiMaggio and Powell, 1983, p. 150). Examples of coercive pressures on organisations include a government regulation, a public sector organisation adopting a new accounting and budgeting system to conform to new doctrine from superior organisations, and non-profit reporting entities engaging accountants in order to comply with new financial reporting regulations. Coercive pressures result from power relationships and politics. At an analytical level, this type of isomorphism is linked to the environment surrounding the organisational field (Frumkin and Galaskiewicz, 2004, p.285).

#### **3.4.2 Mimetic Pressures**

A second source of isomorphic organisational change is mimetic pressures, whereby an organisation reproduces or uses a similar model to another organisation that has successfully implemented a particular value or practice (Frumkin and Galaskiewicz, 2004; DiMaggio and Powell, 1983). Modelling, as Meyer and Rowan (1991) used the term, is a response to uncertainty. Mimetic pressures arise primarily from uncertainty. Under conditions of uncertainty, organisations often replicate peers that are apparently positive or significant (Boxenbaum and Jonsson, 2008); accordingly, mimetic isomorphism occurs (Greenwood et al, 2008). Models can be diffused unintentionally, or indirectly through employee transfer or turnover (DiMaggio and Powell, 1983, p. 151).

### **3.4.3 Normative Pressures**

Normative pressures that lead toward isomorphic change stem primarily from professionalisation. Professionalisation is interpreted as the collective struggle by members of an occupation to attain a certain level of qualifications and competence, including fulfilling their conditions of employment. Attaining a certain standard of professional competence is essential in achieving legitimacy that perpetuates and reinforces occupational autonomy (Meyer and Rowan, 1991; DiMaggio and Powell, 1983). Normative pressures are often associated with professions because this includes education and training that infuse the professional values expected in all organisations (Boxenbaum and Jonsson, 2008). Normative isomorphism occurs because organisations are inherently competitive and are motivated to achieve respect and legitimacy from society (Greenwood et al., 2008; Frumkin and Galaskiewicz, 2004).

### **3.4.4 NIS and Public Sector Organisations**

The concept of institutional isomorphism has not been without its critics, as it appears to view the organisation as a passive adaptor to institutionalisation rather than adopting a proactive response to institutional pressure (Powell, 1985; Oliver, 1991; Scott, 2008; Modell, 2001). The success of the institutionalisation process is dependent upon the degree to which member organisations accept the values, concepts and changes that are introduced; the higher the degree of acceptance, the more easily the new value becomes 'saturated' within organisations (Scott, 2008). The degree of isomorphism is therefore dependent upon the extent to which organisations accept or resist surrounding environmental pressures. The organisation might adopt a 'tightly coupled' response when institutional pressure is accepted without doubt. Such behaviour would occur when the organisation was highly dependent on others. Alternatively, isomorphism (institutionalisation) could be low if the organisation adopts a loosely coupled (decoupled) response and is resistant to change. Decoupling occurs when the actual organisation's activities

diverges from its vision (Meyer and Rowan, 1977; Siti-Nabiha, 2005; Scott, 2008; Frumkin and Galaskiewicz, 2004)

As a response to institutional pressure in private and public sector organisations, Oliver (1991, p. 151) delineated five ways that organisational members respond when dealing with institutionalisation. These are acquiescence (compliance), compromise, avoidance, defiance and manipulation. Oliver proposed that organisational member response to institutionalisation is affected by the type of pressure implemented. Oliver (1991) hypothesised that organisational members will actively resist when social legitimacy is perceived to be low and there are rational economic motives present. Further, a high degree of resistance from organisational members will occur when a low degree of coercive pressure exists. She also hypothesised that the larger the possibility of organisational resistance to pressure, the less consistency in institutional norms and the bigger the level of discretionary constraints imposed by the institutional pressure. Moreover, a high degree of resistance by the organisation occurs when the uncertainty level and interconnectedness of the organisational environment is low.

Several scholars (e.g. Covalleski and Dirsmith, 1988a; Modell, 2001; De-Araujo et al, 2009; Timoshenko, 2009) have found examples of institutional pressure within the budgetary reform process. Covalleski and Dirsmith (1988a) found that the institutionalisation process of the budgetary system and design occurred as a result of self-interest from within the organisation, and was externally influenced by other organisations. They also found, using the University of Wisconsin as a case study, that isomorphism occurred through the institutionalisation of a new budgetary system (Covalleski & Dirsmith, 1988b). Modell (2001) found senior managers sought legitimacy and displayed economically rational motives (efficiency) in response to the institutionalisation of performance management in the Norwegian health care sector. This finding supported one of Oliver's (1991) hypotheses relating to compliance responses to institutional pressure that sought to determine legitimacy and efficiency motives. Timoshenko and Adhikari (2009) found the motive underpinning Russian government accounting and budgeting reform was to pursue



legitimacy from the viewpoint of external parties and stakeholders rather than achieving rational motives. In Portugal, the institutionalisation of a new budgeting system (PBB) was in response to institutional pressure from the European Union, the OECD and the EUPAN. However, as a resistance response from the Portuguese bureaucracy, PBB implementation was viewed only as a formality (window dressing) in seeking legitimacy from the community, and PBB was not implemented in any substantive way (De-Araujo et al, 2009).

The abovementioned research findings were produced using NIS, which informs us why public sector organisations adopt a particular value, belief or method. It therefore provides a reasonable starting point to help explain why the Indonesian central government adopted PBB as its budgeting system. Frumkin and Galaskiewicz (2004) found that public sector organisations are more vulnerable to all three types of institutional pressure (isomorphism) than private sector organisations. Given that Indonesian budgetary reform, through PBB, was influenced by institutional pressure from the external environment, NIS is an appropriate framework to analyse the institutionalisation of PBB within the Indonesian central government. The following section examines the research methods used in this study.

### **3.5 Research Method**

This research examined governmental budgeting reform through the implementation of PBB, using Indonesia as a case study. A case study is a method used to study an individual or institution through the use of documents, archival records, interviews, direct or participant observations, and physical artefacts (Yin, 2008; Ormrod & Leedy, 2005). A case study approach to governmental reform, specifically to explain the implementation of new systems in public sector organisations, was used by Khumawala (1997) and Christensen (2002). Khumawala (1997) analysed the factors affecting the transition of accounting in the Government of India from an ineffective bureaucratic system to that of an informative decision-making tool. This case study demonstrated that a lack of strong political support,

insufficient trained staff and an authoritarian and centralised administrative culture were factors detrimental to successful accounting reform in the Government of India. Christensen (2002) used a case study approach to analyse accrual accounting change within the New South Wales (NSW) Government. He found a strong influence of internal promoters (e.g. the NSW Premier and Treasurer) and external drivers (e.g. consultants and accountants) on the NSW accrual accounting reform team.

This research used a case study approach to examine the Indonesian central government's budgetary reform process between 2003 and 2010, particularly with respect to the implementation of PBB. It employed NIS perspectives developed by Meyer and Rowan (1977) and DiMaggio and Powell (1983), and Oliver's (1991) conceptualisations of organisational strategic response to institutional pressure.

Data for this study was obtained from semi-structured interviews<sup>11</sup> (see Bryman, 2001) and archival documents including Indonesian government reports and regulations, international organisation (the World Bank and the IMF) publications, foreign donor projects in Indonesia, and newspaper articles. The design of the interview guide occurred using the main themes of this research, namely the three institutional isomorphic pressures (i.e. coercive, mimetic, and normative), the history of the Indonesian Public Sector (1990s to 2010), and the nature of PBB and its implementation. Original questions for each of these main sections were constructed based on a review of the relevant literature. However, open-ended questions were included to allow the interviewer and participants to probe, explore and ask questions to clarify a particular subject (Patton, 2005). The original interview guide was developed in English. Following Behling and Law (2000), the interview guide was translated into *Bahasa* Indonesia, as all participants used *Bahasa* as a first language.

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<sup>11</sup> The semi-structured interview is a method that refers to a context in which the interviewer has a series of questions that are in the general form of an interview schedule but is able to vary the sequence of questions (Bryman, 2001).

Primary data collection occurred between November 2013 and January 2014. Semi-structured interviews were undertaken with 15 Indonesians involved in the early stages (2003 to 2010) of PBB implementation. Some participants were affiliated with Indonesian governmental bodies, including the Indonesian Ministry of Finance (MoF) (n=3) and Ministry of Home Affairs (MoHA) (n=3). The participants also included members of The *Ikatan Akuntan Indonesia* (Indonesian Institute of Accountants - IAI) (n=2) and university staff (n=3). Other participants included several key Indonesians involved as IMF and World Bank consultants (n=2), and donor/ex donor projects, including the USAID, CIDA and the GTZ (n=2)<sup>12</sup>. Participants were selected because of their historical understanding of the Indonesian central government budgetary system, and their involvement in the formulation of regulations related to PBB implementation in the Indonesian central government or PBB implementation more broadly.

Participants were chosen using a snowball sampling method, allowing the researcher to identify the next respondent based on a prior respondent's information (Lewis-Beck et al., 2004). The first participant, a member of the team who formulated the Indonesian regulations that related to PBB and its implementation, has an informal relationship with the researcher. Based on an informal discussion with this participant, during which a brief overview of this research was provided, they indicated their knowledge of other key actors and potential participants. They indicated that these actors had significant knowledge of the history of the Indonesian central government's budgetary system, and they were involved in the formulation of regulations related to PBB implementation in Indonesia.

The interviews ranged between 60 and 90 minutes in duration, and were conducted in the participants' offices or homes in several cities in Indonesia. Interviews were audio-recorded with participants' permission. Interviews were conducted in *Bahasa Indonesia* and transcribed from the audio record by the researcher. To preserve the confidentiality of the participants, they were not identified by name. Interview

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<sup>12</sup> These people worked for more than one organisation each.

transcriptions were later translated into English by an Indonesian professional English translation service based within an Indonesian university to confirm the quality of translation. A re-translation from English to *Bahasa Indonesia* by a staff member at Macquarie University's linguistic department, who was also a staff member of an Indonesian State University, using five randomly chosen interview transcripts, confirmed the validity of the translations.

Following the work of Huberman and Miles (2002), interview data was analysed and interpreted using a thematic framework (themes and codes) to categorise patterns across the data. These themes and codes were based on NIS theory developed by Meyer and Rowan (1977) and DiMaggio and Powell (1983), the history of the Indonesian Public Sector (1990s to 2010), and the nature of PBB and PBB implementation (see Appendix 2). Finally, as per Yin (2008), interview results were supported and supplemented by a review of archival documentary evidence from the Indonesian government (e.g. government reports, publication, laws, decrees and other regulations) and newspaper articles, international organisation (e.g. World Bank and IMF) reports and publications, outputs from foreign donor projects (e.g. USAID and CIDA), OECD publications, public sector management literature, and management accounting literature. This supplementary information ensured the capture of different dimensions of PBB implementation in Indonesia and maximised the validity of the results. The following sections contain the findings of this research in terms of an historical overview of Indonesian public sector budgeting in order to understand the history and motives for the adoption and implementation of PBB within the Indonesian central government budgeting system.

### **3.6 An Historical Overview of Indonesian Public Sector Budgeting**

This section relates to the second research objective of this chapter – to examine the historical events leading up to PBB implementation within the Indonesian central government, through the enactment of Law No. 17/2003 on State Finances (*UU No. 17 Tahun 2003 tentang Keuangan Negara*). The implementation of PBB within the

Indonesian central government should be considered in an historical context in order to be able to contextualise the findings of this research and enhance our understanding of the government's budgetary reform process. Based on interview data analysis and archival document reviews, this historical context includes financial, political and structural reform.

Indonesian central government budgeting systems have been a legacy of Dutch colonial regulations since the country's independence in 1945.<sup>13</sup> Primary budget use has been on an annual and balanced budget basis<sup>14</sup>, categorised as 'traditional budgeting'. Accordingly, Indonesian central government budgeting has only recognised projected cash flow for a maximum of one lead year. This traditional form of budgeting was confusing for producing financial reporting as it operated on a cash basis rather than accrual accounting. Thus, cash inflows from debts or taxes were recorded as revenue, and cash outflows for capital expenditures (building, road and bridge) or routine expenses (wages, maintenance, supplies) were recorded as expenditure (Chowdhury and Sugema, 2005). Consequently, as there was no difference between the cash inflow from taxes or government's debts from other parties, when taxes collected remained relatively stable and cash outflow increased, government debt would increase. The consequence of this practice was not easily understood by the government, and the large amount of debt that eventually matured was believed to be one of the factors that led to the Indonesian economic crisis in 1997 (Tarmidi, 1999). Budget transparency and duplication also significantly affected budget inefficiency and therefore accountability. These weaknesses were

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<sup>13</sup> Legal regulations included: (i) *Indische Comptabiliteitswet* (ICW) Stbl. 1925 No. 448, (ii) *Indische Bedrijvenwet* (IBW) Stbl. 1927 No. 419 jo. Stbl. 1936 No. 445, and (iii) *Reglement voor het Administratief Beheer* (RAB) Stbl. 1933 No. 381 (The Government of Indonesia, 2003)

<sup>14</sup> Annual budgeting is a budget that requires expenditure and revenue to be formulated and forecast for a single year (short-term); which occurs annually. Budgets are often not in line with organisational programs and are fragmented in the appropriation and decision process (Wildavsky, 1978). A balanced budget requires the revenue and expenditure side in a balanced position (Chowdhury & Sugema, 2005).

found in the traditional budgeting form, evidence of which is seen through interviewee transcripts below:

*We know that the traditional budget has some weaknesses, for example, our prior budgeting system was not transparent as the budget document [was not made] public. Further, it is difficult to measure... accountability [as] there is no accountability mechanism [to the] public; even we can't control...budget performance. As we use balance[d] budget[s],...we received money and then spent it. It is simple, but hard to measure. Thus, it is also difficult to measure...government money. How much did it spend? For what purpose is it? Where is it?...and so forth. (Interviewee No. 15 – university lecturer)*

*[Budget] duplication...is one problem because our budget structure [was] overlapping within departments that impacted [on] budget inefficiency. (Interviewee No. 7 – ex-senior consultant for an international organisation)*

These weaknesses highlighted the importance of budgetary reform, as part of overall financial management reform, in Indonesia. Furthermore, the motive for budgeting reform is inherent within the explanation section of Law No 17/2003 on State Finances (*UU No. 17 Tahun 2003 tentang Keuangan Negara*)<sup>15</sup> passed by the Indonesian central government that relates to the government's need for budget accountability and transparency (The Government of Indonesia, 2003).

Within the Indonesian government, the concept of PBB and double-entry bookkeeping was introduced in 1992 after a World Bank funded delegation of Indonesian central government officers and university academics attended a local government finance course provided by The University of Birmingham (Mardiasmo, 2002; Halim, 2004):

*We [several government officers and academics] sought to reform Indonesian financial management after [we came] back from [a] financial management workshop in the UK [in] 1992. Therefore, this decision to implement PBB was, in fact, initiated in the 1990s (Interviewee No. 1 – A senior officer in MoHA).*

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<sup>15</sup> The explanation section of the Law No 17/2003 "... an effort to improve budgeting process in the public sector by an implementation of performance based budgeting."

PBB within Indonesia gained further prominence following the enactment in 1993 in the US of the Government Performance and Result Act (GPRA). This prompted Indonesia to formally adopt a public sector performance management model that led to the establishment of the *Sistem Akuntabilitas Kinerja Instansi Pemerintah* (SAKIP) [Government Agency Performance Accountability System] in 1996 (Ruswandi, 2005). This early performance management model was later used by the *Lembaga Administrasi Negara* (LAN) [State Administration Office] in formulating the *Laporan Akuntabilitas Kinerja Instansi Pemerintahan* (LAKIP) [Government Agency Performance Accountability Report] in 1999 (The Government of Indonesia, 1999a; 1999c).

The onset of the Asian economic crisis in July 1997 saw a rapid devaluation in many East Asian currencies following years of high foreign debt-to-GDP ratios. Indonesia's currency (the rupiah) experienced severe devaluation following the country's move from a managed floating exchange regime to a free-floating exchange rate arrangement (Liddle, 1999). This crisis resulted in the closure of 16 insolvent banks. Companies faced higher debt costs in US dollars due to the devaluation of the rupiah, and the increase in the Indonesian unemployment rate led to many employees being retrenched from crisis-affected firms (Djiwandono, 2000). In an attempt to stabilise the currency and alleviate the crisis, between October 1997 and April 1998 the Indonesian central government asked the IMF for aid and signed several Letters of Intent (LoI) to support Indonesia's economic recovery. The important points of these LoI between the Indonesian central government and IMF were that: 1) the IMF program provide a macroeconomic framework to support continued efforts in the restructuring of the financial sector and to achieve progress with these structural reforms; 2) the Indonesian central government adopt several policies on fiscal, monetary and exchange rate reforms, which would affect its external position and financing policy, that would be designed by IMF and Indonesian central government co-operative teams; and 3) Indonesia should review its public expenditure management, eliminate subsidies and restructure tax. With

respect to monetary and exchange policy, several programs for establishing the Indonesian banking system were constructed to support the rupiah on foreign exchanges. Using the IMF supporting program, the Indonesian central government undertook an Indonesian bank restructuring program, and strengthened the legal and supervisory framework for the Indonesian banking system to restructure the financial sector which had essentially collapsed as a result of the economic crisis. Finally, the Indonesian government increased the liberalisation of foreign trade and investment, deregulated domestic activities, and accelerated a program of privatisation (IMF, 1998a; 1997; 1998b).

However the economic crisis, and the consequential high inflationary pressures placed on the economy, had already resulted in political and social unrest among the population. These political and social circumstances led to significant political reform, which culminated in the resignation of President Suharto on 21 May 1998 after 31 years in power. Furthermore, in June 1998, the new government under President Habibie honoured the agreement with the IMF in continuing programs outlined in the LoI that supported Indonesian economic recovery, particularly the government's structural changes (Tarmidi, 1999; Harun, 2007; Harun et al., 2015).

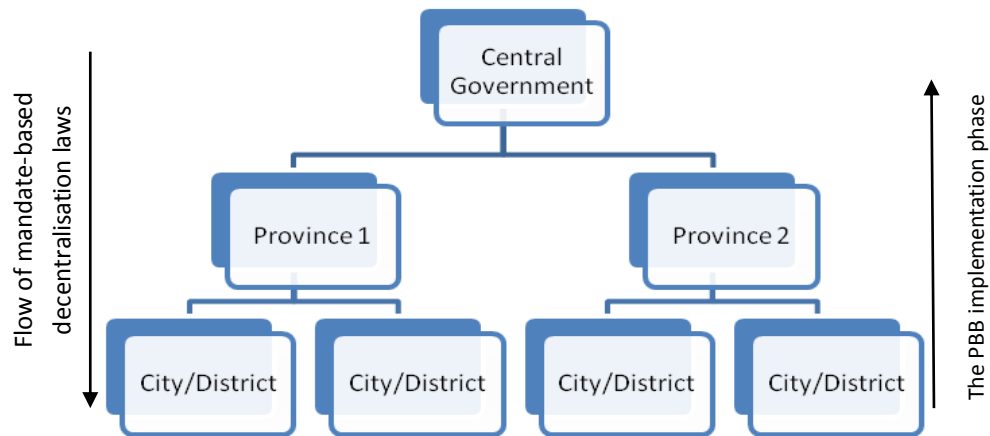
The government's structural reform occurred in 1999, supported by the enactment of decentralisation laws (Law No. 22/1999 on the Local Government (*UU No. 22 Tahun 1999 tentang Pemerintahan Daerah*) and Law No. 25/1999 on Financial Arrangement between Central and Local Governments (*UU No. 25 Tahun 1999 tentang Perimbangan Keuangan Pusat dan Daerah*)<sup>16</sup>. These Laws were fundamental regulations that governed the decentralisation process in Indonesian local governments. As per Figure 5, which depicts the extent of governmental structural reform, these laws mandated that the central government provide more discretion and responsibility to

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<sup>16</sup> These Laws were later amended in 2004 with Law No. 32/2004 on the Local Government [*UU No. 32 Tahun 2004 tentang Pemerintahan Daerah*] and Law No. 33 /2004 on Financial Arrangement between Central and Local Governments [*UU No. 33 Tahun 2004 tentang Perimbangan Keuangan Pusat dan Daerah*].



local government, including both provincial and city/district levels (The Government of Indonesia, 1999). This law resulted in a significant change for local government management system as this change involving the transfer of numerous responsibility and funds from central to local government. (Hadiz, 2004).



**Figure 5. Decentralisation vs PBB implementation in Indonesia**

In addition to stimulating structural reform, decentralisation laws instigated reform of the Indonesian government's financial management system, which included budgeting and accounting systems. At the local government level, financial reform commenced with the enactment of Government Regulation (GR) no. 105/2000 on Local Government Financial Management and Accountability (*Peraturan Pemerintah (PP) No. 105 Tahun 2000 tentang Pengelolaan dan Pertanggungjawaban Keuangan Daerah*), which instructed all local governments (provincial and city/district) to implement PBB, by stating that "local government budgeting is prepared by using performance based budgeting" (GR 105/2000 verse 8). However, financial reform within the Indonesian central government commenced in 2003 with the issuance of Law 17/2003 on State Finances (*UU No. 17 Tahun 2003 tentang Keuangan Negara*). This law regulates financial management (budgeting and accounting) within both central and local government in Indonesia. It also constitutes the rules of the budgeting schedule from preparation to disbursement, financial management and budget principles, the new financial management system (accrual accounting, PBB

and Medium Term Expenditure Framework<sup>17</sup>), financial responsibility, and the relationship between central and local government (The Government of Indonesia, 2003).

When asked why PBB commenced first at the local government level, some participants from MoHA and MoF provided reasons:

*It is because...local governments are [more] ready than the central government. Furthermore local governments' budget management is simpler than the central government. In financial matters local governments manage less money than the central government. (Interviewee No. 1 – A senior officer in MoHA)*

*Financial management [with]in...local government is more established than [within] central government. For instance, before budgeting reform occurred, local government[s] already had several financial systems [in place] such as an asset management and financial management manual, which were not owned by the central government. That is why PBB started [at] the local government [level]. (Interviewee No. 4 – An ex-senior officer in MoF)*

Although Law 17/2003 was enacted in 2003, PBB was applied in 2005 as there was a two-year preparatory period for designing PBB forms, systems and procedures for implementation. These designs were formally enacted in GR No. 21/2004 being the *Formulation of Working Plans and Budgets of Indonesian Central Government Ministries and Agencies* (PP No 21 Tahun 2004 tentang Penyusunan Rencana Kerja dan Anggaran Kementerian Negara/Lembaga) that commended all ministries and departments to implement PBB. Accordingly, several elements such as performance indicators and budgetary structure were strengthened to improve the PBB system. This sought to synchronise the budgeting process with the chart of accounts, as the Indonesian central government had implemented double entry bookkeeping in 2005 using

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<sup>17</sup> The Medium Term Expenditure Framework (MTEF) is a policy-based budgeting approach in which policy decision-making is across more than one fiscal year, and considers the cost-benefit of decisions in the following year. The MTEF seeks to improve the value for money of public spending, in addition to reinforcing fiscal discipline and strategic prioritisation (The Government of Indonesia, 2003).

International Governmental Financial Standards. Thus, in 2007, the Indonesian MoF enacted decree No. 91/PMK.02/2007 regarding the chart of accounts standard (*Peraturan Menteri Keuangan (PMK) No. 91/PMK.02/2007 tentang Bagan Akun Standar*) for budgeting and accounting. Further, in 2010, the Indonesian central government also enacted GR No. 90/2010, a refinement of GR No. 21/2004, that required all ministries and departments to integrate government planning and budgeting (The World Bank, 2012).

The next section presents the results related to the institutional pressures that influenced the adoption and implementation of PBB in Indonesia. It enhances understanding of the reasons why the Indonesian central government adopted PBB as its budgeting system.

### **3.7 Institutionalism of PBB within Indonesian Central Government Budgeting**

This section is related to research objective one (evaluating the institutional processes of the Indonesian central government's budgetary reform) and two (examining the factors influencing the Indonesian central government's decision to implement PBB). Therefore, this section focuses on the findings from the responses to the interview questions, supported by the documentation (see Section 4, Research Method) relating to PBB implementation within the Indonesian central government. This discourse uses NIS as an interpretive lens.

#### **3.7.1 Coercive Pressures**

In order to examine the influence of international organisations such as the IMF and the World Bank, interviewees were asked several related questions. Most responses consistently indicated an indirect influence of the World Bank in Indonesia's decision to implement PBB in the 1990s, and this indirect influence is articulated in greater detail by interviewees below.

*In my opinion, the World Bank and the IMF had indirect influence in the decision to implement PBB [...] we started to think about*

*budgeting reform long before the economic crisis occurred in Indonesia. [...] As I remember, this notion of PBB was in fact discussed in the early 1990s after several friends returned from attending a course in the UK. Inspiration for PBB arose here from the implementation of [the] Government Performance and Result Act in the US in 1993 [...] That is why we developed performance measurement early, [well] before PBB implementation was being suggested by the IMF and the World Bank. (Interviewee No. 5 - senior officer, MoF)*

*After they (several government officers and academics) went back to Indonesia, they pursued to reform Indonesian financial management. It was in the 1990s. [...] However, this process stopped when the economic crisis occurred in Indonesia. [...] my opinion is that the influence of the World Bank and the IMF in the decision to implement PBB was indirect. (Interviewee No. 13 – university professor)*

Thus the idea for budgeting reform, particularly the decision to implement PBB, arose in Indonesia after government employees and academics attended a public sector administration course. The participants were funded by the World Bank as part of a project on Indonesian accountancy development running since 1979 (The-World-Bank, 1996). Although the World Bank's project focused on improving Indonesian central governmental accounting practice, it also sought to improve Indonesia's budgeting system given that "budget allocation should be driven more by future targets than by past performance" (The-World-Bank, 1996, p. 6). Whilst this illustrates early World Bank influence in advocating PBB within Indonesia, it is indirect, as the actual decision to implement PBB rested with Indonesian central government employees, rather than direct coercion through regulatory means.

On the other hand, in their LoI dated July 1998, the IMF suggested that the Indonesian central government reform its management of public expenditure, including a new budgetary system. However, there is no clear statement from the IMF that 'imposes' PBB upon the Indonesian central government budgeting system. Thus, this LoI only 'conveyed the necessity' of improving budgetary revenue performance and expenditure management within the Indonesian central government. In addition, the IMF provided recommendations on enhancing the

management of public expenditure, including the “establishment of spending priorities, more efficient budgetary preparation, cash management controls, and comprehensive, accurate, and timely reporting” (IMF, 1998c, p. 11).

*Improving budgetary revenue performance and expenditure management is essential for the achievement of our short- and medium-term fiscal objectives. A Committee on Fiscal Monitoring has been established by the Minister of Finance to coordinate fiscal and monetary policy, with the participation of BAPPENAS (the State Ministry of National Development Planning) and Bank Indonesia. A public expenditure review was completed with the World Bank in late July. (IMF-Indonesia Letter of Intent, July 1998, p. 11)*

Therefore, because the LoI required technical assistance to enable Indonesian financial management reform, the IMF and the World Bank sent experts to provide checklists to the drafting team during the formulation/ratification of Law 17/2003. The checklist included several concepts such as accrual accounting, PBB, and an MTEF within the new financial law (The World Bank, 2007b). These checklists reflect direct influence from the IMF and the World Bank in the official decision to implement PBB within Indonesian central government. See supportive evidence from the two interviewees’ transcripts below:

*These observers (from the IMF and the World Bank) played their role in supervis[ing] the process of Law 17/2003 ratification [formulation] to ensure their message [adoption of PBB, accrual accounting, and MTEF] was complied with by the Indonesian formulation team. (Interviewee No. 6 – ex-senior officer, MoF)*

*They sent their expert and gave us [a] checklist [that must be] included in Law 17/2003 formulation. (Interviewee No. 4 – ex-senior officer, MoF)*

However, although the IMF and World Bank provided the checklists that included the implementation of PBB, its form and content was modified by the Indonesian regulation team to accommodate the cultural, political and administrative environment of Indonesia (The Government of Indonesia, 2004a; The World Bank, 2007b).

Most interviewees' evidence suggests the influence of global organisations on the Indonesian central government's decision to adopt PBB was indirect. That said, evidence indicated strong influence by the IMF and the World Bank in the formulation/ratification of Law 17/2003, constituting a regulation that provided an official instruction for Indonesian central government to implement PBB as its budgeting system. Thus, their coercive pressure nevertheless existed when the decision was taken to use PBB in Law 17/2003. DiMaggio and Powell (1983, p. 150) argued that coercive isomorphism arises from both formal and informal pressures exerted upon an organisation by other organisations. These pressures could be felt as a force, as persuasion, or as an invitation to collude. Hence, after Oliver (1991), influence from these global organisations on Indonesian PBB implementation can be categorised as moderately coercive.

In this study, most interviewee responses consistently suggested that whilst the IMF and the World Bank indirectly contributed to the process of PBB implementation within the Indonesian central government, this was predominantly from an observation standpoint. They argued that although there were consultants from these international organisations, their role was primarily to observe whether PBB was implemented within the Indonesian central government. Moreover, the influence of these consultants on the format of PBB were not as strong as they were in countries such as the US, the UK or Australia. This moderate influence was evident in the form of Indonesian PBB, which was modified to accommodate the Indonesian team's ideas and perspectives.

*These consultants [from the IMF and the World Bank] played their role as observers in several meetings with the MoF, [which were] held to supervise the process of PBB implementation, however they didn't have much influence in the detailed formulation of PBB formats. (Interviewee No. 7 – ex-senior consultant, international organisation)*

*..... the IMF and the World Bank have also indirect influence on the process of PBB implementation. Although they sent their consultants, this...was just to ensure the dissemination of PBB in the ministries*

*and agencies within the Indonesian central government, not in the detail [regarding] which PBB form...was used in...implementation.  
(Interviewee No. 14 – university lecturer)*

The above suggests that IMF and World Bank consultants, in their roles as supervisors and observers, exercised control over the process of PBB implementation. The fact that these consultants were supervisors and observers is indicative of the application of coercive pressure during the process of PBB implementation. These consultants seemed to broadly observe that the process of PBB implementation was indeed occurring, but they did not appear to have much influence on the form of PBB that Indonesia was implementing. Moreover, that the PBB form was modified to accommodate the Indonesian team's perspective leads one to conclude that PBB implementation within the Indonesian central government was somewhat of a 'window dressing' exercise in order to be 'seen' to be fulfilling the conditions contained within the LoIs. This modified form of PBB was also evidence of the Indonesian government's resistance to foreign (the IMF and the World Bank) detailed concepts of PBB. This was identified by the World Bank (2007a) as a reason for weak Indonesian policy on budgeting, and the public financial management system. Thus, although the Indonesian central government signalled a move to PBB and MTEF through Law 17/2003, this progress was slow (World Bank, 2007a). Thus, institutional pressure from the IMF and the World Bank in the process of implementation was categorised as being one of moderate coercive pressure.

All interviewees consistently emphasised that developed country donor programs<sup>18</sup>, including those of USAID, CIDA and GTZ, did not influence the decision to implement, or the process of implementing, PBB within the Indonesian central government. However, they had an indirect influence in the process of

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<sup>18</sup> In Indonesia, development aid from several developed countries existed, particularly, for delivering aid for local government financial management reform. These included USAID projects through BIGG [Building Institutions for Good Governance] and LGSP [Local Governance Support Program] programs, CIDA through the program of Improved Public Financial Management, and GTZ, through the governance and democracy program.

disseminating PBB in local government, through their coordinating role with the Indonesian MoHA and several local government authorities (province or city or district) (RTI International, 2009; CIDA, 2009). See the quotations from the interviewees below:

*The donor programs from developed countries didn't influence the decision to implement PBB or [affect] the process of implementation within central government. They [did] focus on the implementation of PBB [with] in local governments with the MoHA. (Interviewee No. 6 –ex-senior officer, MoF)*

*... No, I have never heard about their [the developed country donor program] influence within the central government. All I know [is that] USAID was [an] influence on PBB implementation [across] several local governments through the BIGG [Building Institutions for Good Governance] program and LGSP [Local Governance Support Program], as well as CIDA. (Interviewee No. 8 –ex-senior consultant, international organisation)*

*All I know [is that]...donor programs such as USAID and CIDA did not...influence...PBB implementation [with]in the central government. Most of them [were] helping...PBB implementation in the MoHA that...related to...local government PBB dissemination. They also help[ed] several local governments...implement...PBB as a pilot project. (Interviewee No. 11 – IAI representative)*

Additional coercive pressures were attributed to Indonesian financial management regulation. Thus, to understand the influence of this regulation, the Indonesian government's regulatory structure must be understood. Indonesian government administration is based on legal regulations. The hierarchical framework of Indonesian government legal regulations includes: (1) the Indonesian Constitution of 1945, (2) enacted laws, (3) government regulations, (4) presidential decrees, and (5) local government regulations (The Government of Indonesia, 2004b).

Indonesian regulations were seen by participants as having had a powerful influence on the decision to implement PBB. As the Indonesian legal system is based on civil law code that is stipulated, rigid and detailed in codified law (Helmholz, 1990), PBB could not be implemented prior to the related regulation being enacted. Therefore, although the notion of PBB was introduced before 2003, this budgeting system could



only be applied after the enactment of Law 17/2003. Moreover, the implementation of PBB was only effective from 2005 after several attempts to prepare a PBB manual and guidance notes (The Government of Indonesia, 2003; 2004a).

Hence, this study found that the World Bank and the IMF exerted a moderate degree of coercive pressure. However, a significant degree of coercive pressure came from Indonesian regulations (the Law 17/2003 on State Finances (*UU No 17 Tahun 2003 tentang Keuangan Negara*) and GR 21/2004 2004 on the Formulation of Working Plans and Budgets of Indonesian central government's Ministries and Agencies (*PP No 21 Tahun 2004 tentang Penyusunan Rencana Kerja dan Anggaran Kementerian Negara/Lembaga*)), as indicated above. From an NIS perspective, findings in this study are consistent with DiMaggio and Powell (1983) and Frumkin and Galaskiewicz's (2004) explanation of coercive pressures. Further, this finding is consistent with research from other developing countries (Malaysia and Sri Lanka) regarding the institutional processes of PBB implementation, which included influence from the UN (Dean, 1986a). However, this study found weak influence of foreign country donor projects on the decision and process of PBB implementation within the Indonesian central government. This finding is inconsistent with evidence of a direct influence of US donor projects in the decision to adopt PBB and its implementation process within other developing countries (for example, India, Philippines, Sri Lanka and Malaysia). In previous research this direct influence from the US, the first country to adopt and implement PBB, was categorised as strong coercive pressure (Dean, 1986a; 1986b).

### **3.7.2 Mimetic Pressures**

To determine whether mimetic pressures occurred during the implementation of PBB within the Indonesian central government, several questions were asked relating to the PBB type used. Two of the 15 participants claimed that Indonesian PBB mimics models in the US and UK.

*...[the form of] PBB that is used in Indonesia came from the GPRA (Government Performance and Result Act) [the US] and FMI (Financial Management Initiative) [the UK] model. (Interviewee No. 8 – ex-senior consultant, international organisation)*

*Our initial PBB form came from the implementation of the Government Performance and Result Act (GPRA) in the US in 1993. (Interviewee No. 5 - senior officer, MoF)*

However, 13 participants consistently indicated that specific countries were not used as role models for implementation. As noted in the previous section, respondents argued that the PBB used in Indonesia was a modified model, combining elements from developed countries (the UK and the US), international organisations (the UN and the World Bank), and local influence from the LAN (State Administration Office) and the *Badan Pengawas Keuangan dan Pembangunan (BPKP)* (Financial Development and Supervisory Agency) (Ruswandi, 2005; The Government of Indonesia, 1999a). The initial dimensions of performance measurement used in Indonesian PBB were derived from those used in the State Administration Office (*Lembaga Administrasi Negara*) (The Government of Indonesia, 1999a). These were:

1. Input: the number or value of resources used in delivering government activities (services), for example, money, skilled staff, operating equipment and facilities, and electricity.
2. Output: goods or services (products) delivered from one or more jobs from one activity in a ministry or agency. An activity could have one or more outputs with different units or product type.
3. Outcome: everything that reflects the functioning of an activity's output in the medium term. An outcome is a measurement of how much of each product/service meets the public's needs and expectations.
4. Benefit: the usefulness of an output that is beneficial to the people. It could be the availability of public facilities.
5. Impact: a measurement of the multiplier influence of government activity to the social, economic, environmental or other public interest. Impact is also evident in the medium and longer term, as it describes the macro aspects of

program objectives, the purpose of sectoral programs, and coverage at both the regional and national level.

The format of other countries' performance measurement systems, including those for the US and UK governments, provided only three dimensions, that being input, output and outcome (Noman, 2008; Robinson, 2007). However with the case of Indonesia, there are additional performance measurement dimensions, including benefit and impact.

The budgetary structure within Indonesian PBB still embraces the line-item incremental approach as part of traditional budgeting. Thus, expenditure type reflects the economic nature of the item, examples being wages, goods, capital, interest, subsidies, grants and social expenditure (The World Bank, 2007; The Government of Indonesia, 2004a).

*We tried to mix and modify [the form of] PBB...used in Indonesia from [that of] prior models...Some we[re] brought and modified from [the] UK and prior internal regulation[s] in Indonesia. For example, the performance indicators which we used are taken from [those used] by Badan Pengawas Keuangan dan Pembangunan and Lembaga Administrasi Negara that were formulated [between] 1993-1997. Also, the budget[ary] structure...used in the PBB still covers line items and [is] also [an] incremental model. It is because line items [are] still needed to manage how much money that [is] spent on each item. However [unlike] in traditional line items, this new line item allows the department to reallocate funding between items as long as there is substantial reason such as a change of policy. Thus, it still reduces inefficiency that results from traditional line items. [The] incremental approach is still used to control the progress of activities or programs from [the] previous budgeting period. It is different with traditional incremental [budgeting] that is used to control the funding in each item. Thus, this new incremental [approach] is helpful in PBB, [allowing it] to control performance. (Interviewee No. 14 - university lecturer)*

Thus, compared with other developed (the US, the UK, New Zealand and Canada) and developing (India, Philippines, and Chile) countries, which totally removed the line-item and incremental approach (See Dongsung, 2005; Noman, 2008; Schick,

1998; Curristine, 2005), Indonesian PBB retained the line-item and incremental approach and modified certain practices to improve usefulness and assist localised implementation (see Appendix 3 and 4).

Nevertheless, similar to other developing countries, the budget categorisation within Indonesian PBB is based on existing organisational structures. Thus, the budget categorisation follows the structures within the ministries and agencies of Indonesian central government that oversee governmental functions, including general public services, defence, order and security, economy, environment, housing and public facilities, health, tourism, culture, religion, education and social protection (The Government of Indonesia, 2004a; The-World-Bank, 2007b).

From an NIS perspective, according to DiMaggio and Powell (1983) and Frumkin and Galaskiewicz's (2004) explanation of mimetic pressure, the analysis demonstrates weak mimetic pressures in budgeting reform within Indonesian central government. Furthermore, contrary to the Harun et al. (2012) finding that Indonesian accrual accounting mimicked Australian and New Zealand practices, this study found that the format of Indonesian PBB is derived from that practised from several countries (such as the USA and the UK) and world organisations' (e.g. the World Bank and the IMF), in addition to the internal demand for line-item and incremental forms. This contrasting finding might be due to the fact that this study focused on PBB adoption within Indonesian central government including its design, implementation, use and impact, while Harun et.al (2012) focused on accrual accounting adoption.

### **3.7.3 Normative Pressures**

This research considered the extent to which normative isomorphism exists through professional bodies' (KSAP: *Komite Standar Akuntansi Pemerintahan* (GASC) [the Governmental Accounting Standard Committee], consultant organisations and the IAI) influence on the decision to implement PBB. The KSAP focuses on designing

accounting standards, and in 2005 the cash toward accrual (CTA) accounting standard was enacted through GR No. 24/2005 (*PP No. 24 Tahun 2005 tentang Standar Akuntansi Pemerintahan*) (Harun et al., 2012), which was then amended to full accrual accounting (FAA) in 2010 through the endorsement of GR No. 71/2010 (*PP No. 71 Tahun 2010 tentang Standar Akuntansi Pemerintahan*). Thirteen of the 15 respondents believed that the KSAP did not influence the preparation, decision and process of PBB implementation within the Indonesian central government (The Government of Indonesia, 2002a; KSAP, 2014).

*No, the KSAP did not have influence in the decision to adopt PBB as the new budgeting system and its implementation. As [is] my understanding, they have only focused on the implementation of the new accounting system [accrual accounting]. (Interviewee No. 3 – ex-senior officer, MoHA)*

*As the KSAP was established in 2002, while the decision to adopt PBB was taken in the 1990s, thus, KSAP has no influence [on the decision to adopt PBB]. (Interviewee No. 15 – university lecturer).*

However, two interviewees stated that the KSAP had an indirect influence on the process of PBB implementation, as the utilisation of CTA and FAA also impacted on changes to the budgeting chart of accounts.

*Although KSAP does not focus on PBB implementation, their decision had an indirect impact on the process of PBB implementation through the enactment of GR 24/2005 that was [subsequently] amended by GR 71/2010 regarding government accounting standards. In other words, the change [to the] budgeting chart of account[s were] required after those regulations [were] enacted. Thus...budgeting chart of account changes [were twofold]; in 2007 through the MoF decree No. 91/PMK.02/2007 and [in] 2013 through No. 214/PMK.05/2013. (Interviewee No. 9 – ex-senior consultant, foreign donor project)*

*KSAP only [has] influence in the implementation of accrual accounting. However, this implementation [only] indirectly influences PBB implementation through budgeting chart of account design. (Interviewee No. 7 – ex-senior consultant, international organisation)*

Suggestions on how to build an accountable and transparent budget were delivered through seminars provided by a private organisational consultant who occasionally

introduced and delivered consultancy services or technical assistance to Indonesian central government staff to assist in their understanding of the new PBB system (Suara-Merdeka, 2002; The-World-Bank, 2007b). However, some interviewees indicated that the seminars were primarily business-oriented, that is, held to profit from participant attendance:

*Sometimes, these consultant organisations help [in] the introduction of this new PBB system for Ministry staff and officers. As we know, official workshops and technical support that [was] organised by our government were limited. However, in the first PBB introduction and implementation, the technical support [provided by] these consultants were not comprehensive, and [appeared to be just about] profit[ing] from the participants. (Interviewee No. 5 - senior officer, MoF)*

Moreover, Interviewee No. 3 indicated that the IAI had little influence on the process of PBB implementation. The IAI only had an indirect influence over the introduction of the double-entry bookkeeping approach within Indonesian central government, as several KSAP members were also IAI members (The Government of Indonesia, 2004c). As with the organisational consultant, the IAI's public sector accounting division occasionally raised the topic of the implementation of double-entry bookkeeping and PBB in seminars and workshops at which Indonesian central government staff and officers were participants (Suara-Merdeka, 2003; IAI-KASP, 2008). Thus, similar to KSAP and organisational consultants, the IAI influence on PBB implementation within Indonesian central government was weak.

*IAI as [an] organisation also doesn't have a direct influence on the PBB implementation decision in Indonesia. [IAI] sometimes raises the topic of double entry bookkeeping and PBB implementation in seminar[s] and workshop[s] and invites some government officers to discuss. However, some IAI members also act personally or jointly with organisational consultants to help [with] technical assistance in some ministries. (Interviewee No 3 - ex-senior officer, MoHA)*

However, as mentioned earlier in the historical overview of Indonesian public sector budgeting, the decision to adopt PBB was made by Indonesian technocrats (government officers and academics), who began working towards budgeting

reform in the 1990s. Hereafter, these Indonesian technocrats acted as the main promoters of the implementation of PBB through their influence in the discussion, formulation of PBB regulation, and dissemination of PBB across Indonesian central government. Thus, the strong influence of Indonesian technocrats in the Indonesian central government budgeting system is evidence of strong normative pressure.

From an NIS perspective, normative isomorphism is related to “professionalisation” (DiMaggio and Powell, 1983, p.152) and occurs when professionals operating in the organisation are subject to pressures from professional bodies (such as Indonesian technocrats, KSAP and IAI) to conform a set of norms and tenets shaped by them (Abernethy and Chua, 1996, p.574). Consistent with DiMaggio and Powells’ (1983) explanation of normative pressures, this study found strong normative pressure from technocrats in the adoption and implementation of PBB. However, differing from Harun et al.’s (2012) finding that explained the influence of KSAP in promoting Indonesian financial management reform, particularly the implementation of accrual accounting, this study, through a different perspective, identified weak influence (normative pressure) from KSAP, IAI and a professional consultant in the implementation of PBB.

In summary, several rational motives within Law 17/2003 such as promoting accountability, obtaining budget transparency, and enhancing efficiency and effectiveness, underpinned the initial adoption of PBB within Indonesian central government (The Government of Indonesia, 2003). However, as evidence shows, the response by Indonesian central government officers and staff to preserve elements of traditional budgeting, including line items and their incremental form (see Appendix 3 and 4), leads one to conclude that the motives underpinning budgeting reform were ultimately irrational. Indonesian central government officers and staff appear to have resisted full implementation of the PBB model through modification and local adaptation. Christensen (2012) used the term ‘window dressing’ in the context of the public sector and NIS. In this research, the modification and local adaptation of the PBB model is considered to be a window dressing strategy of the

Indonesian central government in the implementation of PBB. Within this strategy, the Indonesian central government presents the IMF and the World Bank with evidence that PBB is being implemented as a new Indonesian budgeting system, but in reality it is only in order to fulfil the LoI. The actual practices of the Indonesian budgeting system were 'decoupled' or loosely coupled with the formal PBB form, as the line-item and incremental approach were still retained as components of the Indonesian form of PBB. "Decoupling enables organisations to maintain standardised, legitimating, formal structures while their activities vary in response to practical considerations" (Meyer and Rowan, 1977, p.357).) Thus, it can be argued that these Indonesian central government strategic responses, which reflect isomorphic pressure, had specific objectives in gaining legitimacy from the international community and support from world organisations such as the IMF and World Bank, although the degree of legitimacy ultimately obtained was low.

This result can be aligned with Oliver's (1991) finding on the response to institutional pressure. She argued that, in response to coercive and mimetic pressures discussed earlier, organisations respond in different ways due to various standards and expectations, ranging from passive cooperation to an active response that involves avoidance, defiance or manipulation. Evidence of low legitimacy and rational motives, and moderate coercive pressure in the institutionalisation of PBB within Indonesian central government, could be categorised strategically as one of avoidance through concealment (Oliver, 1991). This evidence is also supported by the finding of the exertion of normative pressure by Indonesian technocrats who played a central role in the adoption, implementation and modification of PBB within Indonesian central government. This strategy involves engaging in window dressing; ritualism; ceremonial pretence; or symbolic acceptance of institutional norms, rules or requirements (Meyer and Rowan, 1977; Oliver, 1991). Thus, instead of rejecting the notion of PBB and its content, the Indonesian central government went along with this idea, but adjusted its content to incorporate several non-PBB values such as the line-item and incremental approach. Hence, in terms of organisational strategic response, this study supports Oliver's (1991) hypotheses that



the lower the degree to which an organisation seeks legitimacy, or the lower the degree to which the organisation seeks rational motives such as efficiency, the greater the organisational resistance to institutional pressure. Consequently, the exertion of moderate degrees of coercive pressure results in organisational development of a compromise or avoidance strategy.

Beyond this, the responses from the Indonesian central government toward the introduction of PBB point to the uniqueness of its form in Indonesia. This finding is consistent with DiMaggio and Powell (1983) and Meyer and Rowan's (1977) concept of isomorphism – that an organisation may adopt or conform to 'much-used' or 'elsewhere successful' organisational structures and operations in order to avoid critical attention and questions from society. It can be argued that institutional pressure occurred in Indonesian budgetary reform, as suggested by Timoshenko and Adhikari (2009). The following section overviews the implementation, challenge, modification, and enhancement of PBB in Indonesia.

### **3.8 The implementation of PBB within the Indonesian Central Government**

This section is related to the final research objective of this study, outlined in the introduction section of this paper (3.2).

The implementation of PBB within Indonesia in 2003 was based on Law 17/2003 on State Finances (*UU No. 17 Tahun 2003 tentang Keuangan Negara*) and GR 21/2004 Agencies (*PP No 21 Tahun 2004 tentang Penyusunan Rencana Kerja dan Anggaran Kementerian Negara/Lembaga*). This implementation was premised on the NPM concept, which focuses on value for money for public expenditure (RTI-International, 2009).

*As a part of [the] NPM concept, the central idea of PBB is to create value for money. [W]e can measure the budget performance for program[s] and activit[ies], we can also measure the efficiency, effectiveness, and economic [performance] of the organisation. Thus, it is impossible to achieve...efficiency, effectiveness, and also economic [performance] without PBB. (Interviewee No. 3 – ex-senior officer, MoHA)*

As PBB seeks to eliminate the weaknesses of traditional budgeting previously mentioned and evident in interviewees' responses, early PBB implementation focused on eliminating the annual budgetary problem through the introduction of the MTEF and forward estimate concepts. These concepts require the calculation of funding requirements for the next fiscal year, based on the current year, which are planned to ensure a continuity of approved programs and activities. Furthermore, Indonesian PBB focuses on the relationship between inputs and outputs/outcomes and the necessary efficiencies to ensure they are achieved (see Appendix 3) (The Government of Indonesia, 2004a). Therefore, several tools to measure program and activity performance, such as performance indicators, cost standards and performance evaluation, are required (The Government of Indonesia, 2004a).

However, the initial implementation phase was still superficial. Operational problems associated with this form and mentioned by several participants included: 1) resistance to the process of transformation by government staff, 2) a lack of alignment of regulation of PBB implementation with other regulations, 3) an inconsistent approach to the application and utilisation of performance indicators in the budget documents, and 4) inability of MoF staff to utilise and evaluate the information generated through performance measurement.

*The problem of implementation came from [certain] government staff that secretly oppose and refuse to implement PBB [for] several reasons. They said it is not suitable, it is difficult, or it...need[s] time to understand the new budgeting [system]. Regarding this...we tried [to] modify our PBB [by] utilising line item[s] and [modifying] performance indicators. (Interviewee No. 5 – senior officer, MoF)*

*Technical[ly speaking], we also faced some problems regarding the idea of PBB and its regulation relating to PBB [the Law 17/2003]. In my opinion... the regulation of PBB [the Law 17/2003] [is] still not connected with other regulations in Indonesia. For example, our regulations regarding central-local financial balance [Law 33/2004] and government financial reports [GR 24/2005] are still not aligned with Law 17/2003 and PBB implementation. (Interviewee No. 10 – ex-senior consultant, foreign donor project)*

*A critical problem [for] implementation is the interconnection between performance indicators. In some budget documents, performance indicators are sometimes left blank, or [are] put in carelessly. Sometimes indicator measurements are inputted but they forget to measure outputs and outcomes. Moreover, [despite] the MoF staff..hav[ing] responsibility to check performance measurement, sometimes [they] forget to check, and only review the budget amount. [An] increase [in] documents to be reviewed [is] the main reason, as they should learn the new budgeting [format], but training is rare. (Interviewee No. 2 – senior officer, MoHA)*

*The problem of PBB implementation is performance measurement. It is difficult to measure performance information in several ministries as we don't have the data for comparative measurement. Moreover, often, these performance indicators are just for ceremonial display in our budget documents. The people who have responsibility to assess this performance never even check it, so these performance indicators are often useless. (Interviewee No. 13 – university professor)*

Based on the OECD categorisation of PBB, the implementation of PBB within the Indonesian central government is presentational PBB. However, performance information within the government budget, and its subsequent review by budget committees, is flawed and does not consider performance information with respect to resource allocation. Thus, this performance information is primarily a symbol of compliance with the PBB regulation that each department must portray their performance information in the budget document (The Government of Indonesia, 2007). This statement is consistent with the World Bank Report (2007, p.46) that mentioned that the Indonesian government's budget system focuses internal and external scrutiny on compliance rather than improving the efficiency and effectiveness of government spending.

Given the problems with PBB implementation previously identified, the Indonesian central government tried to improve PBB implementation through staff rotation within the Ministry, and providing training and technical assistance for all government staff and officers to maintain implementation according to plan. Additionally, data validity and the integration of planning and budgeting were also improved to strengthen the quality of performance information used in performance measurement.

*That is why we tried to make them understand [through] socialisation, training, [more] information and so forth. However, until the present, there are [still a] few people who [are] resistant [to] this budget[ary] system. (Interviewee No. 5 – senior officer, MoF)*

*We always provide training and workshop[s] for all government staff to [ensure they] understand and [are] ready to implement PBB. It is a very hard job because we still found [long-term] staff [who] cannot understand the critical [nature] of PBB [for] our financial management. Sometimes we should [consider] staff rotation to make the implementation of PBB easier. (Interviewee No. 9 – ex-senior consultant, foreign donor program)*

*Our training is focusing [on] strengthen[ing] performance measurement. Thus, qualified and valid data that include government performance information [is] needed [to] improve measurement. (Interviewee No. 13 – university professor)*

Harmonising budgeting reform with other financial management reform (including accounting and accountability reform) was needed to achieve PBB objectives in allocating resources responsively, efficiently and effectively. Some regulations were formulated to support this objective. For instance, in line with Law 17/2003 on State Finances (UU No. 17 Tahun 2003 tentang Keuangan Negara) that proposed budgeting and accounting reform, two Laws were enacted to cover reform of the Treasury (Law 1/2004 on Treasury (UU No 1 Tahun 2004 tentang Perbendaharaan)) and audit system (Law 15/2004 on State Finances Audit, Management and Accountability (UU No. 15 Tahun 2004 tentang Pemeriksaan, Pengelolaan dan Tanggung Jawab Keuangan Negara)). Thereafter, these three laws (17/2003, 1/2004 and 15/2004) constituted the package of financial reform laws. Hence the implementation of PBB, as a part of broader financial reform, brought benefits to the Indonesian central government. Several interviewees noted that the implementation of PBB within the Indonesian central government resulted in increased performance information and measurement, prevention of budget duplication, and better integration of planning and budgeting for multi-year program controllers.

*In my opinion, PBB [makes] a good contribution [to] our government sector. We have better performance and better accountability. Before budgeting reform, it was easy to steal government money as there was*

*weak accountability for expenditure. (Interviewee No. 4 –ex-senior officer, MoF)*

*By using PBB, we could [obtain] several benefits. For instance: it could prevent budget duplication in the government as there are clear performance indicators between programs and activities. Also, as we use a medium-term expenditure framework [approach] in PBB, there is better planning and budgeting for controlling multiyear programs. (Interviewee No. 6 –ex-senior officer, MoF)*

An examination of some Indonesian regulations (for example, MoF decree No. 91/PMK.02/2007 on the chart of accounts standard for budgeting and accounting, and GR No. 90 /2010 on formulation of government budgeting) indicates several improvements to the form of PBB were made, particularly regarding the integration of the budgeting and accounting process via chart of account standard formulation, strengthening of performance measurement through data availability and reliability, and integration of planning, budgeting and accounting.

### **3.9 Conclusions, Implications and Limitations**

The purpose of this research was to examine how and why the central governmental budgetary processes in Indonesia, a developing and transitioning country, changed in 2003 from traditional budgeting to PBB. Further, this study sought to establish the nature of institutional pressure and organisational responses to this pressure with respect to the implementation of PBB within the Indonesian central government. This research was a response to Timoshenko and Adhikaris' (2009) call for studies of the institutionalisation processes during budgetary reform, and drew on DiMaggio and Powell's (1983) notion of institutional isomorphism. Based on the findings presented above, several conclusions can be made regarding the four objectives of this research.

The first research objective related to the evaluation of institutional processes of the Indonesian central government's budgetary reform. This research found that a line item and incremental approach is still evident in the PBB practices within Indonesian central government. These findings mean that the Indonesian central

government had weak rational motives to achieve efficient and effective budgeting through PBB implementation, as the line item and incremental approach remained as a remnant of traditional budgeting, contributing to inefficiency and ineffectiveness. Moreover, this study revealed the indirect influence of the IMF and the World Bank in the introduction of, and decision to use, the PBB form in the Indonesian central government's budgeting system. However, the World Bank's influence on Indonesian central government budgetary reform occurred earlier (1979) than that of the IMF (1997). World Bank support to Indonesian technocrats had been provided since 1979, stimulating the decision to reform Indonesian central government budgeting in the 1990s. The IMF's influence commenced in 1997, after the Indonesian economic crisis. Thus, the influence of the World Bank on Indonesian central government budgetary reform has been stronger than that of the IMF. Based on this evidence, a moderate degree of coercive pressure from international organisations occurs within Indonesian central government budgetary reform, particularly the institutionalisation of PBB. This study also confirmed that the Indonesian central government followed the expectations of the institutional environment by conforming to international organisational pressure, motivated by the desire to gain legitimacy in the eyes of the international community.

This study also found weak mimetic isomorphism regarding the institutionalisation of PBB within Indonesian central government, as the form of PBB was modified during implementation. However, strong normative isomorphism existed in the adoption and implementation of PBB. This modified form of PBB revealed strong influence from technocrats who were forced to adapt PBB whilst masking its fundamental elements. Indonesian PBB therefore had little substance, but appeared solid in order to gain legitimacy from the international community. The study suggests the Indonesian central government's response to international pressure to change its budgeting system was avoidance and concealment. Thus the first research objective was achieved, as this study discovered evidence of normative and coercive pressure in Indonesian central government budgetary reform.

The second objective was to examine the historical events leading up to PBB implementation within Indonesian central government through the enactment of Law No. 17/2003 on State Finances. This study found that Indonesian technocrats decided to adopt, and prepared to implement (with support from the World Bank), PBB as an Indonesian central government budgetary system in the 1990s to reflect their awareness of a need for a more efficient and effective budgeting system. However, this effort was hindered by the Indonesian economic crisis in 1997. The World Bank and IMF provided support to the Indonesian central government to help them overcome the crisis and implement reforms to financial management including accounting, budgeting and auditing. Financial management reform officially occurred through the enactment of Law No. 17/2003 on State Finances, which mandated PBB implementation within Indonesian central government. Hence, the second research objective was achieved.

The third research objective was to examine the factors or motives underpinning the implementation of PBB within Indonesian central government. Its initial purpose was to increase efficiency and effectiveness in public budgeting, but gaining international legitimacy soon became the goal. This study found the major factor influencing the Indonesian central government's decision to implement PBB was the technocrats' awareness of external demand for more efficient and effective budgeting systems. Another factor influencing PBB implementation was moderate coercion from the IMF and the World Bank, which led to the formulation of regulations that related to PBB implementation within Indonesian central government (Law 17/2003). In revealing these motivations, the third research objective was achieved.

The final research objective for this study was an examination of the extent to which the Indonesian central government has implemented PBB as budgetary reform. This study found that although the implementation of PBB within the Indonesian central government spread across ministries and agencies, its implementation is still in its early stages. Thus, it is too early for this research to conclude that the

implementation of PBB has been successful or unsuccessful. However, this study demonstrated a degree of achievement of PBB implementation within the Indonesian central government, including improvements in the form of PBB undergoing implementation. This includes the integration of the budgeting and accounting process via a standard formulated chart of accounts, strengthening of performance measurement through data availability and reliability, the integration of planning, budgeting and accounting, and the harmonisation of PBB implementation with other financial management reform, such as accrual accounting and MTEF implementation. However, several problems remain, such as the lack of adequate training for government staff, poor regulatory system coordination, and insufficient data of the quality needed for performance measurement.

Problems similar to those described above were found in the early PBB implementation within other developing countries, including India, Malaysia, and the Philippines (Dean, 1986a; Pedro, 1963; Chien, 1972). However the experience of PBB adoption and the associated institutional pressures in Indonesia appear very different from those in other developing countries. This study finds that Indonesia experienced an indirect influence (moderate coercive) from the World Bank and the IMF, while other developing countries experienced strong influence (strong coercive) from a 'superior country' (the US) and the UN (Dean, 1986a). Further, the form of PBB in these developing countries mimics that of the US's PBB practices through the US's donor programs and UN projects. This is evidence of strong mimetic pressure (Dean, 1986a), whilst weak mimetic pressure was found during Indonesian PBB adoption. This finding can be partially explained by the differing time periods for adoption and implementation in Indonesia (since the 1990s, with the new PBB format) and these developing countries (since the 1960s, with the old PBB format). Moreover, this study found that PBB implementation in Indonesia was seen as being partly cosmetic, as it retained the incremental and line-item approach as part of traditional budgeting to improve usefulness and assist localised implementation. This meant that the form of PBB implemented in Indonesia was compromised, and was not fully aligned or compatible with the original form of PBB



that had been intended. Thus, it appears that the Indonesian central government implemented PBB in order to fulfil an IMF and World Bank mandate, as outlined in the LoI between the global bodies and the Indonesian government. This practice differs from those in other developed (e.g. the US, the UK, New Zealand and Australia) and developing countries (India, Philippines, Singapore and Chile), which removed the traditional budgeting format altogether. This examination of the extent to which the Indonesian central government has implemented PBB as its budgetary system shows that the study's final research objective was attained.

In conclusion, this study examined how and why the central governmental budgetary processes in Indonesia, a developing and transitioning country, changed from traditional budgeting to PBB in 2003. It revealed the historical context underlying the motives and factors behind the implementation of PBB within Indonesian central government, and evaluated the institutional processes of the central government's budgetary reform. Moreover, this study found that PBB has been adopted across Indonesian government ministries and agencies, albeit still in its early stages.

This study contributes to the field of management accounting literature on PBB and budgetary reform by utilising a theoretical framework to examine budgeting forms, particularly the development of PBB and its application in Indonesia, using DiMaggio and Powell's (1983) concept of institutional isomorphism. Using this framework, this study analysed the way organisational pressures forced the adoption of PBB within the Indonesian central government, and examined the relationship and response of government to this pressure.

This study provides practical guidance for future policymaking by global organisations such as the OECD, IMF and World Bank. These organisations seek to influence the transparency of national governments of transitioning countries, and the findings of this study identify factors that inhibit full realisation of the policy objectives of these funding organisations, particularly with respect to central

government responses to institutional pressures for reform. Further, given the uniqueness of the Indonesian central government's budgeting reform process, this study makes a practical contribution to the Indonesian central government's policy of strengthening and developing its PBB, given the problems and challenges found during implementation to date. The Indonesian experience of PBB implementation contains budgetary reform lessons for other developing countries that are considering adopting PBB.

The purpose of this study was to examine budgetary reform within Indonesian central government from 2003 to 2010 through a reflective analysis of the archival documents and respondent views and knowledge related to the introduction, decision and implementation of PBB. The voices of respondents are important as their central role in the regulations relate to the early adoption of PBB and its implementation within Indonesian central government. However, this study has limitations with respect to research method, as the interviews were conducted with only 15 respondents. Thus, caution is advised in applying these results more generally to PBB implementation across public sector organisations within the Indonesian archipelago and its numerous provinces, each of which has unique social, cultural and economic settings. Policy implementation in Indonesia is still challenging, especially across local government where there is less consistency due to remoteness and communication problems, as well as economic, social and cultural barriers. Furthermore, the utilisation of NIS in this research limited the examination to institutional pressures in Indonesian central government budgeting reform rather than factors contingent on the reform process. It is possible to further explore the factors that influenced the process of PBB adoption and implementation within Indonesian local government, using a contingency model for financial management reform such as Lüder's financial management reform process model.

### 3.10 References

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## 4. Paper 3: The Implementation of Performance-Based Budgeting within Indonesian Local Government

### 4.1 Abstract

**Purpose:** This paper describes an investigation of the motives that underpinned the development of Performance Based-Budgeting (PBB) within Indonesian Local Government and the factors (including historical factors) influencing its implementation.

**Design/methodology/approach:** Primary data was obtained through interviews, whilst supporting data was gathered from an examination of Indonesian government documents, organisational and donor agency reports, independent newspapers, and academic literature. The Lüder financial management reform process (FMR) model (2013) was applied to examine how the budgeting system within Indonesian local government was reformed during 1999–2010.

**Findings:** This study produced four main findings. First the primary motive for PBB implementation within Indonesian local government was the need – expressed by Indonesian technocrats (government officers and scholars) and supported by the World Bank – to modernise its financial and reporting system. Second, the harmonisation of planning, budgeting and accounting helped embed reform. Third, the Lüder FMR model (2013) is a useful framework to identify key factors behind the implementation of PBB within Indonesian local government. Finally, weak performance identified after PBB implementation indicated that budgeting reform had been partly cosmetic.

**Research limitations/implications:** The small number of interviewees – people with a central role in the local government budgeting reform – reduces the ability to generalise the study's conclusions.

**Originality/value:** The study utilised the Lüder FMR model (2013) to investigate budgeting reform (specifically PBB implementation) within a developing country context. The paper therefore contributes to the PBB geographic subfield within the broader management accounting and public sector literature.

**Keywords:** performance-based budgeting, historical research, Lüder FMR model.

## 4.2 Introduction

The adoption of Performance-Based Budgeting (PBB) emerged within public sector organisations during the 1940s. As part of public sector budgeting reform, PBB was intended to replace the traditional budgeting system, and achieve greater efficiency and effectiveness within organisational activities (Dongsung, 2005). Several researchers (see Curristine, 2005; Joyce, 2011; Robinson, 2007; Ho, 2011) have asserted that PBB enhances the utilisation of performance information and measurement with respect to budget authorisation and resource allocation, thereby allowing better scrutiny of government operations and performance. PBB was implemented in many countries from the 1950s to the 1980s, including the United States of America (USA), India, Malaysia, Sri Lanka and the Philippines. PBB adoption increased rapidly from the latter half of the 1980s, in countries including Australia, New Zealand, Sweden, Denmark, the Netherlands, Mexico, Greece, Thailand, Singapore, South Korea and Japan (Curristine, 2005; Dean, 1986; Blöndal & Ruffner, 2004; Van Nispen & Posseth, 2006).

Despite widespread adoption, debate continues as to the real value and effectiveness of PBB. Scholars (Moynihan, 2006; Jordan and Hackbart, 2005; Melkers and Willoughby, 1998; 2001; Lu, 1998) have claimed that performance information linked to the budget assessment is often inaccurate, and offer different views as to how governments determine reliable performance measures and then how these are effectively applied to allocate organisational resources. Moreover, the experience of PBB implementation in developing countries (e.g. Malaysia, Bolivia, Thailand, Chile, Tanzania, Greece and South Africa) indicates a weak linkage between performance information and resource allocation (Shah, 2007; Curristine, 2005; Karkatsoulis, 2010; Siddiquee, 2006). Previous research has highlighted the tenuous link between performance information and resource allocation in the public budgeting process, as well as the problems experienced in the implementation of PBB in developing countries. However, in 2000 the Indonesian central government decided to officially

implement PBB across local governments (The Government of Indonesia, 2000). This was the responsibility of the Ministry of Home Affairs (MoHA) (*Kementerian Dalam Negeri*), the supervisor and coordinator of Indonesian local governments.

Based on Law No 32/2004 on Local Government (*Undang-Undang No. 32/2004 Tentang Pemerintahan Daerah*), the Indonesian government operates at both a central and local government level. Local government within Indonesia exists at two levels – provincial and city/district – and decentralisation has been ongoing since 1999 with central government's supervision over local government. The central government now commands sole authority over only six functions: foreign affairs, defence, security, the judiciary, monetary and fiscal policy, and religion. The other 31 authorities, including education, health, public works, spatial planning and transportation, are co-managed between central and local government (The Government of Indonesia, 2004a). Law No 33/2004 relating to the Financial Arrangement of Central and Local Government (*Undang-Undang No. 33/2004 Tentang Perimbangan Keuangan Pusat dan Daerah*) was established in order to manage the newly decentralised system of government. Under this law, the Indonesian central government allocates funds to local governments (province and city/district) to manage their affairs. Most regulations (Laws, GRs, Presidential and Ministry Decree) involving financial management and funds transfers as well as financial management system (budgeting, accounting, performance reporting, and auditing) within local government are made by the central government through the Indonesian MoHA to conform uniformity within local government (The Government of Indonesia, 2004a; 2004b).

As noted above, in the year 2000 Indonesian local governments were mandated to implement PBB. This paper addresses questions as to how and why this budgetary reform occurred. Thus, the paper has three objectives: to (1) examine the contingency factors that influenced budgetary reform within the developing country of Indonesia, (2) examine the historical context leading up to PBB implementation

within Indonesian local government, and (3) reveal the process by which PBB implementation occurred within Indonesian local government.

In addition to the three research objectives outlined above, Lüder (2009) suggested accounting and budgeting in developing and/or Asian countries should be studied using the Lüder FMR model. Thus, this study was motivated by Lüder's (2013) call to use the Lüder financial management reform process (FMR) model to examine budgeting reform within a regional and local government context, focusing on process and outcome orientation. Lüder (2013) utilised the FMR model to compare governmental accounting and budgeting reform processes that occurred within the state of New South Wales (NSW) in Australia (in the 1990s) and the Hessian state in Germany (in the 2000s). Lüder (2013) found that various factors (such as stimuli, reform driver and promoters, and structural features) influenced the governmental accounting and budgeting reform process across the two states mentioned above. Noting a major gap in the literature on governmental accounting and budgeting, this study applied the latest Lüder FMR model (2013) as a conceptual framework for understanding the occurrence of budgeting reform, with emphasis on PBB implementation, within Indonesian local government toward the end of the 1990s. This study contributes to the management accounting and public sector accounting literature regarding local government budgeting models and implementation issues within developing countries. Moreover, this study is of benefit to the Indonesian government in facilitating assessment of the effectiveness of PBB implementation within local government, including its key success factors, problems and challenges.

The remainder of the paper is structured as follows. The next section explores PBB literature as the background for this study. The third section explains how the Lüder FMR model (2013) has been applied within a reform context. The fourth and fifth sections examine the research method, and analysis of Indonesian local government budgeting reform using the Lüder FMR model (2013) respectively. Next, the findings in relation to the influence of contingency factors within Indonesian local government, and the extent of PBB implementation, are summarised. The final

section presents the implications and the limitations of the study, and makes recommendations for future research.

#### **4.3 Performance-Based Budgeting in Public Sector Organisations**

Evidence shows that the initial form of PBB emerged at about the same time as the notion of performance management (Dongsung, 2005; Jones and McCaffery, 2010). Performance was part of budgeting reform within public sector organisations from the 1940s, with the introduction of a performance measurement system in the US federal budgetary system following demands from the public sector for more efficient and effective public expenditure. This initial PBB system was later termed the 'first wave' of PBB, and implemented across every level of US government. This first wave of PBB focused on the performance of organisational processes and outputs, including finance, services and programs and/or activities (Dongsung, 2005; Jones and McCaffery, 2010; Shah and Shen, 2007). However difficulties associated with outcomes and performance measurement hindered the first wave of PBB implementation, particularly in measuring the performance of human service programs (Jones and McCaffery, 2010). Furthermore, a major challenge of this first wave of PBB implementation in the US government was the fact that federal and state legislators were unwilling to relinquish the line-item form in the budget document (Dongsung, 2005). This line-item form (part of traditional budgeting) reduces budget efficiency and effectiveness (Robinson, 2007).

Notwithstanding these problems, PBB remains prevalent within the US government, although several modifications have been made since the initial implementation in order to meet the changing requirements of state and local governments (Jones and McCaffery, 2010, p.488). Moreover, despite the challenges experienced during implementation in the US, PBB has spread internationally through US and United Nations (UN) donor programs into developing countries such as the Philippines, India, Malaysia and Sri Lanka, where it faced similar implementation challenges (Dean, 1986a; 1986b; 1986c; Jones and McCaffery, 2010; Pedro, 1963).

During the 1960 to the 1980s, the first implementation of PBB (in the US government) was modified and transformed into several budgeting forms (such as zero-based budgeting (ZBB) and the planning, programming and budgeting system (PPBS))<sup>19</sup>. These budgetary forms still focused on using performance information to evaluate government budget documents. These budgeting forms also faced difficulties in their implementation such as: a) increased paperwork in the budgeting process (in both ZBB and PPBS), b) a lack of performance information needed for ZBB analysis, and c) difficulties in measuring the costs and benefits of programs and complexities in linking programs with budgetary structures in PPBS (United States General Accounting Office, 1997).

Due to these problems in the implementation of PPBS and ZBB, at the end of the 1980s the PBB was reborn within the US federal government as 'new PBB'. This second wave of PBB focused on the performance of organisational processes and outputs and was depicted as objectives focused, and output and outcome oriented, which reinforced an accountability culture and customer-oriented performance measurement (Wang, 1999; McGill, 2001; Dunleavy, 1994). Thus, with the emergence of the New Public Management (NPM) concept that aimed to improve the public administration system of governments, in which citizens are explicitly considered as customers (Denhart & Denhardt, 2000; Dunleavy, 1994), this new PBB model (the second wave of PBB) was seen as a key element of NPM that could deliver a performance measurement system focused on customer satisfaction (Hood, 1995; Hood, 1991; Robinson, 2002). Alongside NPM, the new PBB model spread and influenced a variety of budgetary systems across countries, including the Financial

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<sup>19</sup>ZBB is a method of budgeting which requires each cost element to be specifically justified, as though the activities to which the budget relates were being undertaken for the first time. Without approval, the budget allowance is zero (Scarlett, 2005).

PPBS assumes that efficiencies and improvements in government operations can be achieved through a common approach for (a) establishing long-range planning objectives, (b) analysing the costs and benefits of alternative programs which would meet these objectives, and (c) translating programs into budget and legislative proposals and long-term projections (United States General Accounting Office, 1997).

Management Initiative in the United Kingdom (UK), Program Management and Budgeting in Australia, and Performance Budgeting in New Zealand (Mascarenhas, 1996). Even though this new PBB form had advantages over old PBB, its implementation raised three issues that led to unintended outcomes and outright rejection of this form of budgeting (Karkatsoulis, 2010; Aristovnik and Seljak, 2009; Lu, 1998).

The first issue regarding new PBB related to the diverse nature of government services, which made it difficult to apply PBB techniques in government. Adapting performance measurement techniques that originated in the private sector to the needs of government, as per the PBB format, proved problematic such as difficulties in measuring governmental performance, particularly in human service programs (Pollitt and Bouckaert, 2011; Olson et al., 1998; Brignall and Modell, 2000; Arnaboldi and Azzone, 2010, Jones and McCaffery, 2010).

The second issue regarding PBB implementation was the lack of competency of government officers. Government officers are experienced in financial measurement within traditional budgeting, but they often lack skill with non-financial performance measures that are part of outputs and outcomes. This problem can hamper PBB implementation, particularly during its initial phase, which can lead to manipulation of performance measurement by government or even its abandonment if measures are not understood (Arnaboldi and Azzone, 2010; Lu, 1998).

Thirdly, the implementation of PBB frequently highlights the weak linkage between performance information and the allocation of resources. This has been observed in many developing countries (e.g. Malaysia, Bolivia, Thailand, Chile, Greece, Tanzania and South Africa), all of which experienced problems in determining reliable performance measures and in applying performance information directly in the allocation of resources (Shah and Shen, 2007; Curristine, 2005; Karkatsoulis, 2010 Siddiquee, 2006).



Indonesia implemented PBB as its budgeting system from the year 2000, alongside dramatic reforms in political (democratisation), structural (decentralisation) and financial (accounting, budgeting and accountability reform) administration (McLeod, 2006; Kristiansen, 2009). Despite 15 years since PBB implementation within Indonesian local government, little academic research on budgeting reform and PBB implementation in this context exists. Previous academic research (see Djamhuri and Mahmudi, 2006; Djamhuri, 2009; Harun and Robinson, 2010; Harun et al., 2012; Harun, 2007; Kristiansen et al., 2009; Mimba et al., 2013) has focused on accounting reform and annual performance measurement reporting rather than PBB. Research is needed to provide an understanding of how Indonesian local government budgeting reform (PBB implementation) occurs and the factors that influence reform.

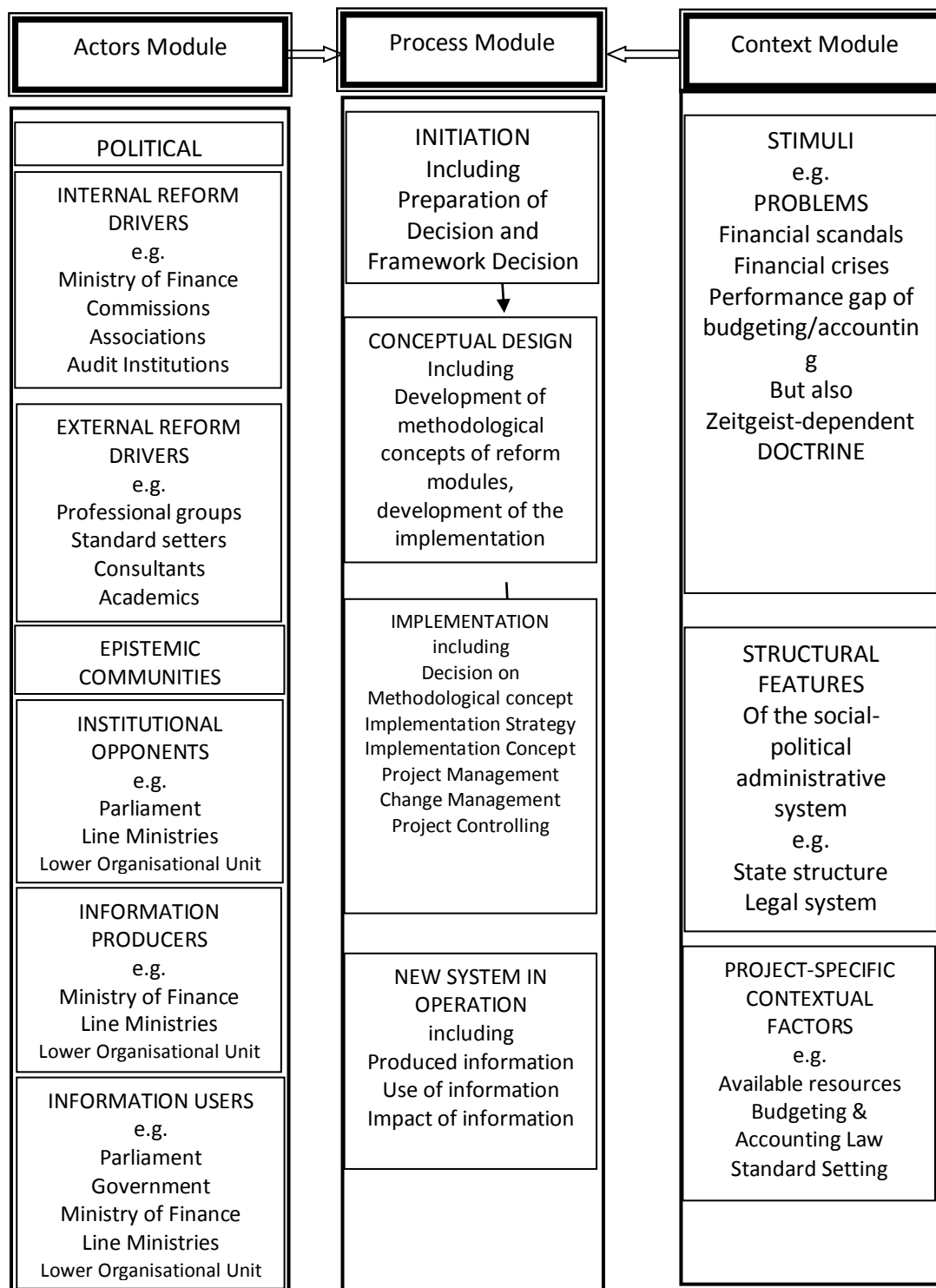
In order to understand the impact of Indonesian budgeting reform on public sector management practice, and to examine the effects that PBB adoption had within Indonesian local government, a theoretical framework is required (Sterck, 2007; Van Reeth, 2002). Previous research (see Lüder, 1992; Lüder, 1994; Chan, 1994; Lüder, 2002; Lüder, 2013; Bruno, 2014; Abushamsieh et al., 2013a; 2013b) demonstrated the utility of the Lüder contingency model (LCM) and its contemporary version, the Lüder FMR model, as a conceptual framework with which to analyse the relationship between government accounting and budgeting reform and the socio-political context that facilitates or inhibits such reform. Previous scholars (Devlin et al., 2002; Christensen, 2002; Lüder, 2002) found that the application of Lüder's FMR model has rarely been utilised to examine budgeting, financial reporting and auditing reform, despite its obvious utility. Following the research of Lüder (2013), this study analysed budgeting reform within Indonesian local government between approximately 1999 and 2010 with particular emphasis on changes in key actor behaviour. It also marries harmonisation information regarding PBB implementation with other financial reforms that occurred in Indonesia using the Lüder FMR model (2013) as a conceptual framework.

The following section discusses the Lüder FMR model (Lüder, 2013) as a conceptual framework, its application in the literature, and events relating to the introduction of PBB within Indonesia between 1999 and 2010.

#### **4.4 Conceptual Framework**

This paper applies the most recent version of the Lüder FMR model (Lüder, 2013) as a conceptual framework for analysing the process of budgeting reform (PBB implementation) within Indonesian local government and examining the factors that shaped this reform process. This conceptual framework provides a contingency model with which to identify and analyse the relevant contextual factors and key players in budgeting reform within Indonesian local government. This framework, like any model, will always be 'skeletal', requiring empirical detail to make it meaningful (Laughlin, 1995). It is important to analyse and detail the Indonesian local government budgeting reform process, using the Lüder FMR model (2013) in order to contribute to knowledge of the budgeting reform process within Indonesia as an economy in transition, and for the benefit of the broader accounting field.

The Lüder FMR model (2013) (see Figure 6) incorporates modules for actors, processes, and context. Actors comprise political promoters, internal and external reform drivers, the epistemic community, institutional opponents, information producers and information users. Three contextual modules address stimuli (or problems), structural features (institutional arrangements) and project-specific factors. There are also four reform process modules: initiation, conceptual design, implementation, and the new system in operation. Figure 6 displays the relationships or associations between the modules that help to identify the factors influencing reform.



**Figure 6. The Financial Management Reform Process Model (Actors - Process - Context modules) from Lüder (2013)**

Lüder (2013) utilised this FMR model (Actor – Process – Context) in a comparative analysis of budgeting and accounting reform within the NSW state government in Australia and across the Hessian State in Germany. The following section outlines the facets of the FMR model and its utilisation in previous research.

#### ***4.4.1 Stimuli***

The stimuli are the contextual variables found at the initial stage of accounting reform that establish the need for system improvement (Lüder, 2002). Lüder's (2013) comparative study across NSW and Hessian state found that accounting reform in both states was driven by an overall need to modernise government. NSW reform was driven by public and community expectations that government needed to constrain debt, resulting in the adoption of a private business model (accrual-based financial reporting) as a form of NPM (Christensen, 2002; Lüder, 2013). Hessian reform was motivated by the successful implementation internationally of widely accepted financial management concepts including NPM, accrual accounting and PBB as a basis for solving problems in government financial management (Lüder, 2013). Similar to the Hessian state, budgeting and accounting reform within the Campania region in Italy was prompted by the international doctrine of NPM, which focused on the harmonisation between budgeting and accounting that arose as a result of federal fiscal reforms (Bruno, 2014).

#### ***4.4.2 Structural Features***

Structural features represent the social-political-administrative culture within organisations that support or inhibit reform implementation. This module was previously referred to as 'institutional arrangements' in the Lüder FMR (2002) (see subsection 2.7.4 in chapter 2). Similar to institutional arrangements, structural features consist of several variables such as the legal system, state structure,

administration structure, and civil service qualification. The legal system refers to the basis of law between civil (codified law based on Roman law) and common (case law and precedent). State structure relates to the structure of the government, whether unitary or federal, cooperative or competitive federalism, unicameral or bicameral legislatures, or a combination of any of these. Administrative structure relates to the authority of central/federal government regarding decision-making. Decision-making could be centralised or decentralised administratively. The qualification of the civil service refers to the capability of governmental staff in implementing reform; lack of staff capability can derail the reform process (Lüder, 2002).

In the case of NSW, the Australian constitution provides for the decentralisation of decision-making, which is supported through common law. This flexibility in common law, coupled with stable and progressive civil services, provides the necessary culture for successful reform and allows new systems to be implemented easily (Lüder, 2013; Christensen, 2002). Similarly to the NSW government, a strong federal system and a stable and progressive civil service favoured Hessian reform. However, Hessian civil law code provides a cultural barrier to reform as laws and regulations are stipulated and detailed in codified law. Laws based on civil code provide less flexibility for judgement when implementing new systems (Lüder, 2013). Likewise, the Campania region in southern Italy has a civil law culture that provides less flexibility, as it is also codified within rigid systems (Bruno, 2014).

#### ***4.4.3 Project-Specific Contextual Factors***

Known as 'implementation' barriers in the LCM, project-specific contextual factors can suspend or obstruct reforms, divert reform direction, and in excessive cases, prevent reforms from being implemented (Lüder, 2002). In NSW, incomplete asset records and the inadequate accounting expertise of government employees were seen as barriers to implementation (Christensen, 2002; Lüder, 2013). In contrast, a lack of available resources and rigid budgeting and accounting laws were barriers to

reform in Hesse. Nevertheless, these problems were largely overcome during implementation (Lüder, 2013). In the Campania region of Italy, the lack of resources to modernise the information and communications technology system and of clarity in reform guidelines were barriers to the implementation of budgeting and accounting harmonisation (Bruno, 2014).

#### ***4.4.4 Political Promoters***

Political reform promoters are government leaders or legislative members who are influenced by stimuli and promote reform. These actors for the reform process might include the President and/or Prime Minister, Minister of Finance or a responsible minister, or members of parliament and/or congress who act as a promoter for the initiation of the reform, and are indispensable supporters in the transition from implementation to regular operation (Lüder, 2002; Lüder, 2013). Political promoters are also referred to as internal reform drivers (Lüder, 2013). The role of political promoters and how they influence reform are discussed in the following section.

#### ***4.4.5 Reform Drivers***

Reform drivers are the recognised institutions and/or professionals who act as organisational stakeholders in the promotion of reform. Internal reform drivers include parliament, the ministry of finance, government commissions, associations, and/or audit institutions. External reform drivers include professionals, standard setters, consultants and/or scholarly networks who influence budgeting and accounting reform (Lüder, 2013). An analysis of the NSW reform process revealed strong support from the premier's department, public accounts committee and the auditor-general as internal reform drivers in budgeting and accounting reform. External reform drivers were global accounting firms, the accounting profession and public commentators, who had significant influence due to the dependency on expert consultants in the reform process. NSW accounting reform was promoted by the Premier (then Nick Greiner) and Treasurer, who had established a treasurer's

accounting advisory panel comprising senior partners from the major accounting firms (KPMG, Price Waterhouse, Coopers & Lybrand, Arthur Andersen, Deloitte and Ernst & Young). In its report to the Treasurer, this panel identified current accounting issues affecting the public sector, which influenced the decision to apply accrual accounting within government (Christensen, 2002; Lüder, 2013). In contrast, Hessian reforms experienced weak support from internal (auditors-general, government branches) and external (consultants and accountants) reform drivers. Part of the reasoning was that government sought to apply private sector GAAP (Generally Accepted Accounting Principle) within government, but evidence suggested that the Hessian government only recruited public sector accountancy consultants. Private and public sector accountants had differing levels and capacity of education, problems arose as the Hessian government failed to harness private sector accounting expertise (Lüder, 2013). With respect to reforms in Campania, the parliament, ministry of economy and finance, and the Italian standards board committee (*Comitato per I Principi Contabili*), employed KPMG as consultants, reinforcing internal and external reform drivers to harmonise the budgeting and accounting reform process.

#### ***4.4.6 Epistemic Communities***

Epistemic communities are groups of experts and professionals who influence the initiation and implementation of reform (Lüder, 2013). Research has asserted that an epistemic community influenced reform in Campania (Bruno, 2014), and private sector consultants and professional governmental accountants played a significant role in initiating and implementing reform in NSW (Lüder, 2013; Christensen, 2002). Epistemic communities have a similar role to reform drivers in influencing reform (Lüder, 2002).

#### ***4.4.7 Institutional Opponents***

Institutional opponents are members of parliament or government institutions, or external powerful organisations, who influence reform as 'inhibitors' (opponents). These opponents actively or passively resist reform, eager to lessen the effects of reform or at least postpone its implementation (Lüder, 2013). Evidence of institutional opposition can be found from the existence of an interregional coordinating group who asked the Ministry of Economy and Finance to postpone reforms in Campania for one year (Bruno, 2014). As Lüder (2002) mentioned, institutional opponents could be also categorised as reform drivers and stakeholders given their influential role in reform.

#### ***4.4.8 Information Producers and Users***

Information producers are government institutions who have a positive attitude towards a more informative budgeting and accounting system, and are willing to change existing systems (Lüder, 1992). In practice, these producers of information are also internal reform drivers (e.g. Ministry of Finance, line ministry, lower organisational unit) who support the reform due to their recognition of the need for a new accounting and budgeting system (Lüder, 2013). Information users also constitute internal and external reform drivers (e.g. parliament, Ministry of Finance, line ministries, lower organisation units), who are users of government information and willing to change systems (Lüder, 2013).

#### ***4.4.9 Initiation***

Initiation is the first step in the reform process, also termed 'intention to reform' that is influenced by the reform drivers (as key actors). This first step is the preparation of a decision or framework design that is impacted from the stimuli and determined by the reform drivers and promoters (Lüder, 2013). With respect to NSW and Hessian reform, initiators wanted to modernise government through the



implementation of new budgeting and accounting systems using an accrual-based financial reform project and new administrative management projects respectively (Lüder, 2013). The intention of reform in Campania was to harmonise budgeting and accounting systems as a basis for achieving successful accrual accounting implementation through the use of trial budgeting and specific accounting projects (Bruno, 2014).

#### ***4.4.10 Conceptual Design***

Conceptual design is the methodological approach to developing a full or modified system (such as full or modified accrual accounting) and subsequent implementation processes (Lüder, 2013; Lüder, 2002). This step requires systematic analysis of the implementation system as a fundamental concept of budgeting and accounting reform, given that this may affect the success or failure of the entire reform process (Lüder, 2013; Jorge, 2003). In NSW, limited consideration and preparation went into designing the full accrual accounting concept (Christensen, 2002). In contrast, the conceptual design for the new administrative management (including accrual, and output-based budgeting and accounting) project in Hessian state, was preceded by several years of discussion and numerous trial processes (Lüder, 2013). Whilst harmonisation of budgeting and accounting emanated at the federal level in Italy, reform design in Campania included a three-year trial process involving approximately 150 entities (Bruno, 2014).

#### ***4.4.11 Implementation***

Implementation is the process of deciding the methodological concepts, implementation strategy, implementation concepts, project management and project control in implementing reform (Lüder, 2013). This strategy includes the decision to use authoritarian or participative strategy; involves centralised or decentralised guidance; proceeds with or without a pilot model; comprises one or multiple steps in implementation; includes considerable or minimal user discretion; has an

implementation period of varying length; and proceeds with or without systematic staff training (Pollitt and Bouckaert, 2011, Lüder, 2002). Christensen (2002) found the implementation of accrual accounting, in selected NSW state departments, occurred through a rigid top-down approach, by removing significant barriers (such as flawed accounting records [assets] and inadequate public sector accounting expertise) obstructing reform. Similarly, the implementation of Hessian reform was also authoritarian in nature, involving a top-down strategy, but was seen as more rational in that each step relied on reasoned planning and training (Lüder, 2013, p. 10). In contrast, in Campania, there was a three-year trial period process using a bottom-up approach based on the shared experiences of group members (Bruno, 2014).

#### ***4.4.12 New System***

The new system is the outcome of the innovative reform process, which includes producing the information, utilising it, and assessing its impact (Lüder, 2013). The outcome of this reform process is that accrual-based financial reporting emerged as a new system in NSW; however, Lüder (2013) argued that reform in NSW was largely cosmetic, with accrual accounting reform being based on rhetoric not realism, as the reality was the unsuitable adoption of the private sector 'performance' model within the NSW government (Guthrie, 1998). On the other hand, the outcome of reforms in the state of Hesse and the Campania region are difficult to assess as they have only recently been completed (Lüder, 2013; Bruno, 2014).

Discussion based on the Lüder FMR model (2013) allows an examination of the actor, process, and context factors influencing the budgeting and accounting reform process. However the Lüder FMR model (2013) has not been used to date to analyse specific budgeting reforms relating to PBB implementation, which this study seeks to do with reference to Indonesian local government. The following section examines the research method applied in this study.

## 4.5 Research Method

This research employed a case study approach to examine the implementation of PBB within Indonesian local government. Case studies allow the exploration of an individual or institution within specific settings, utilising data collected through documents, archival records, interviews, direct or participant observations, and physical artefacts (Ormrod and Leedy, 2005; Salkind, 2012). Case studies are the preferred method within social science research (psychology, sociology, political science, history and economic) for examining questions surrounding the 'how' and 'why' (Yin, 2008; Ormrod & Leedy, 2005). Christensen (2002) and Harun and Robinson (2010) suggested the case study approach as a means by which to examine accounting reform in government. This approach was also used by Lüder (2013), and Bruno (2014), who applied the Lüder FMR model to examine the harmonisation of budgeting and accounting reform in local government.

Data for this study was collected from semi-structured interviews<sup>20</sup> (see Bryman, 2001), Indonesian government archival documents (laws, government regulations, decrees and reports), publications by international organisations including the World Bank and the International Monetary Fund (IMF), reports from foreign donor projects in Indonesia, and newspaper articles. The Lüder FMR model (2013) was used to support the design of the interviews, which involved questions based on a review of the relevant literature. The original interview guide was constructed in English but translated into *Bahasa* Indonesia to suit participants who used *Bahasa* as a first language.

Primary data collection occurred between November 2013 and January 2014. Interviews were undertaken with 15 people involved in the early stages of PBB implementation within Indonesian local government, including the Indonesian MoHA (n=4), local government associations (n=3), university academics (n=3), and

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<sup>20</sup> Semi-structured interviews involve a series of questions that are in the general form of an interview schedule, but the interviewer is able to vary the sequence of questions (Bryman, 2001).

the *Ikatan Akuntan Indonesia* (Indonesian Institute of Accountants – IAI) (n=2). Also included were several Indonesians involved as consultants in donor projects (n=3,) including the United States Agency for International Development (USAID), Canadian International Development Agency (CIDA) and the *Deutsche Gesellschaft für Internationale Zusammenarbeit* (German Organisation for Technical Cooperation – GTZ). Participants were selected because of their historical understanding of the Indonesian government budgetary system and their involvement in the formulation of regulations related to PBB implementation within Indonesian local government or more broadly. Participants were recruited using a snowball sampling method, allowing the researcher to identify the next respondent based on the previous respondent's suggestion or introduction (Lewis-Beck et al, 2004). In this study, the first participant was a member of the team who formulated Indonesian regulations relating to PBB and its implementation within local government. An initial informal discussion about the research with this participant yielded knowledge of other key actors with significant knowledge of the history of the Indonesian local governmental budgetary system, and the formulation of regulations related to PBB implementation within it.

The interviews took 60-90 minutes and were conducted in the participants' offices or homes in cities across Indonesia. Interviews were conducted in *Bahasa* Indonesian and audio-recorded with the permission of participants, then transcribed by the researcher. Participants were not identified by name, in accordance with the requirements of Macquarie University's Human Ethics Committee. The interview transcriptions were later translated into English by an Indonesian professional English translation service based in an Indonesian local university to confirm the quality of translation. A re-translation of five transcripts from English to *Bahasa* Indonesia by a staff member of Macquarie University's linguistic department, who is also a staff member at an Indonesian State University, confirmed the validity of the translations.

Interview responses were analysed and interpreted using the Lüder FMR model (2013). As indicated earlier, interviews were supported and supplemented by a review of archival documentary evidence (Yin, 2008), which was linked to the Lüder FMR model (2013) through thematic patterns evident from interview responses. The following sections provide an historical overview of Indonesian local government budgeting, and these findings are discussed to generate an understanding of the history and motivations behind the adoption and implementation of PBB.

#### **4.6 A Historical Overview of Indonesian Local Government Budgeting**

This section responds to the second and third research objective of this project (see the introduction section in this chapter), which relate to the historical events leading up to PBB implementation within Indonesian local government and the process by which PBB implementation occurred. This section contextualises the findings of this research and enhances our understanding of the PBB reform process within Indonesian local government. Based on interview data analysis and archival document review, this historical overview includes financial, political and structural reform, all of which provide insights into the budgetary reform process.

##### **4.6.1 *Indonesian Government System - Prior Budgeting Reform***

Prior to Indonesian government structural, financial and political reform commencing in 1999, the system remained largely centralised. Local governments had limited authority over their territory. Traditional budgeting – including annual, incremental, balanced and line item budgeting – was implemented within the local government system based on Law No. 5/1974 on ‘The Principles of Regional Government Administration’ (*UU RI No. 5 Tahun 1974 tentang Penyelenggaraan Permerintahan di Daerah*), and the *Indische Comptabiliteitswet* Stbl. 1925 No. 448, a financial regulation legacy of the Dutch colonial era.

Annual budgeting requires expenditure and revenue to be formulated and forecast for a single year (short-term budgeting). This approach is often not in line with medium to longer-term organisational programs that become fragmented in the budget appropriation and decision process (Wildavsky, 1978). Incremental budgets formulate the current year's budget by increasing/decreasing revenue and expenditure based on the previous year's budget (Wildavsky, 1978). This budgeting form is inefficient and ineffective in relation to public expenditure accountability as it lacks comprehensive review. Budget allocation is not based on an established public need, and merely preserves the previous budget and/or activities (Khan and Hildreth, 2002). Balanced budgeting requires revenue and expenditure to be equal, which is deficient when producing financial reports as it utilises the cash basis instead of accrual accounting. Thus, cash inflows from debts or taxes are recorded as revenue, and cash outflows for capital expenditures (building, road and bridge) or routine expenses (wages, maintenance, supplies) are recorded as expenditure (Chowdhury and Sugema, 2005). In line-item budgeting, revenues and expenses are separated into specific centres for wages, supplies, travel, etc. This approach is also problematic as it does not indicate whether each item is necessary, and/or whether the proposed expenditure or revenue in each item has been allocated efficiently (Schick, 1966). One interviewee provided an Indonesian model of the traditional budgeting system:

*Indonesian government financial management was traditionally [approach and incremental]... so, if this year [it is] five, [then] next year should be six, [then the following] year should be seven and continuously. The important thing is that all money must be spent. The system [resulted in] accountability not being [fully] assessed. In fact, a [financial] report ... was [only based on] ... receipt/payment, and it [this financial report] did not use a modern accounting system (Interviewee No. 1 - senior officer, MoHA).*

Indonesian technocrats (e.g. officers of MoF and MoHA, and Indonesian academics) have made several efforts to reform Indonesian budgeting since the Suharto era (1969–1998) in conjunction with other financial management systems (e.g. accounting and auditing). However progress has been slow due to the lack of qualified personnel and low political commitment from government (Harun and

Robinson, 2010). Nevertheless, several budgeting milestones have been achieved, including the decision to implement PBB as a budgeting system in the mid-1990s, developing the *Sistem Akuntabilitas Kinerja Instansi Pemerintahan* (SAKIP – Government Agencies Performance Accountability System) in 1996, and implementing the *Laporan Akuntabilitas Kinerja Instansi Pemerintahan* (LAKIP – Government Agencies Performance Accountability Report) in 1999 (Ruswandi, 2005, The Indonesian Government, 1999a, 1999b).

*The SAKIP and LAKIP model as the legacy [of performance measurement initiated], were the embryo for PBB [as part of budgeting] reform. Although it was also postponed, as a financial crisis occurred in Indonesia (Interviewee No. 8 – the IAI member).*

*We [several government officers and academics] sought to reform Indonesian financial management after [we came] back from [the] financial management workshop in the UK [in] 1992. Therefore this decision to implement PBB was, in fact, initiated in the 1990s, although this process stopped in 1997 because of the financial crisis that occurred in Indonesia. (Interviewee No. 1 - senior officer, MoHA)*

Another interviewee provided similar reasoning:

*We started to think about budgeting reform long before the financial crisis occurred in Indonesia. [...] As I remember, this notion of PBB was in fact discussed in the early 1990s after several friends returned from attending a course in the UK. Inspiration for PBB arose...from the implementation of [the] Government Performance Results Act in the USA in 1993. (Interviewee No. 10 - university professor)*

#### **4.6.2 Budgeting Reform in the Indonesian Local Government**

After the financial crisis in 1997 that forced political reform in 1998, the IMF encouraged the Indonesian government to adopt NPM to improve management of public expenditure. This was stipulated in one of the clauses of the IMF funding agreement (IMF, 1998), which also specified that the Indonesian government must decentralise its management structure. This structural reform resulted in the distribution of additional funding and the delegation of authority to local governments (provinces and cities/districts). Consequently, several new financial

management techniques relating to accounting, budgeting and auditing were needed to manage the impact of this structural reform within local government (Djamhuri and Mahmudi, 2006; Djamhuri, 2009). The requirement for these new financial management techniques led to the Indonesian government enacting Government Regulation (GR) No. 105/2000 on Local Government Financial Management and Accountability (*Peraturan Pemerintah No. 105 Tahun 2000 tentang Pengelolaan dan Pertanggungjawaban Keuangan Daerah*). This regulation introduced double-entry accounting and PBB across all levels of local government (The Government of Indonesia, 2000).

All interviewees indicated that although the decision to implement PBB occurred in the mid-1990s, and legal reform (GR 105/2000) was subsequently enacted to support adoption, there was no agreement regarding the concept or form with which PBB would take in Indonesia. Thus, by 2002, PBB had still not been implemented at the local government level (Djamhuri; 2009). As an interviewee noted:

*After enactment of GR 105/2000, we had [still to agree on] the concept of PBB that would [be] implemented [with]in Indonesian local government, both in [terms of] budget structures and performance measurement. The development of [the] PBB concept and manual were still being discussed [at] the formulation team meeting [at the] MoHA. (Interviewee No. 2 - senior officer, MoHA)*

However, several foreign donors such as Building Institutions for Good Governance (BIGG), the National Democratic Institute (NDI), *Vereniging van Nederlandse Gemeenten* (VNG - Netherlands Association of Municipalities) and the United Nations Development Project (UNDP) sought to introduce a concept and form of PBB that had been adapted from the best practice of foreign countries. For example, since 2001, USAID - through BIGG projects - introduced to its Indonesian local government partners a model of PBB based on best practice experience from US cities and counties (ICMA, 2001; ICMA, 2002).

*Our project started working with Indonesian local government in 2000, but we started to introduce PBB [with]in our local government partners since 2001. That also involved joint collaboration with other*



*donor projects. (Interviewee No. 5 - former senior consultant, donor project)*

Despite evidence of several PBB models being introduced from various donor projects, this study found that PBB was adopted on a larger scale after MoHA<sup>21</sup> developed the PBB manual and associated implementation guidance (The Government of Indonesia, 2002b). As local governments in Indonesia are dependent upon central government in the implementation of new financial management systems, their ability to implement new systems is dependent upon the necessary training and dissemination of information from MoHA in order to ensure uniformity and consistency in applying PBB concepts and techniques (The Government of Indonesia, 2002b).

*Based on [current] regulations, our (local government) leader is MoHA. [Therefore], regarding the implementation of [a] new system, we should wait for training and dissemination from MoHA as we did not want to [waste time on] activities such as implementing a PBB model [which] has not been prepared by MoHA. (Interviewee No. 13 - former member of a local government association)*

With respect to disseminating PBB concepts across local government in Indonesia, MoHA developed a training team consisting of MoHA officers, academics, representatives of several local government entities, and donor project experts. Some members of the training team were also involved in the formulation of regulations such as GR No. 105/2000 on Local Government Financial Management and Accountability and MoHA decree No. 29/2002 on Manual of Financial Formulation, Accountability and Supervision: Procedures of Budget Preparation for Local Government.

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<sup>21</sup> The MoHA manual was developed by an enactment of the MoHA decree No. 29/2002 on Manual of Financial Formulation, Accountability and Supervision: Procedures of Budget Preparation for Local Government (*Keputusan Menteri Dalam Negeri No. 29 Tahun 2002 tentang Pedoman Pengurusan, Pertanggungjawaban dan Pengawasan Keuangan dan Belanja Daerah, Pelaksanaan Tata Usaha Keuangan Daerah dan Penyusunan Perhitungan Anggaran Pendapatan dan Belanja Daerah*). This PBB Manual explains PBB and how to implement it as a new budgeting system in Indonesian local government (The Government of Indonesia, 2002b).

*We were involved in the formulation of several financial regulations [which] was why MoHA recruited us to formulate MoHA decree No. 29/2002. Thus, it was also our responsibility to disseminate PBB and train local government officers [to enable an] understanding of this budgeting system. We hoped, they could train their staff to apply PBB [effectively] [with]in their local government [authority]. (Interviewee No. 3 – ex-senior officer in MoHA)*

Not only were MoHA's trainers involved in disseminating PBB to local government, but several donors who were influential in the initial phase of PBB in 2001 were involved in providing training and technical assistance to their local government partners. Several Indonesian private consultants were influential in the process of PBB adoption and implementation, although some appeared to be primarily focused on financial gain:

*These consultant organisations helped introduce this new PBB system for local government staff and officers. They arranged an event for organisers to deliver some seminar and training for our government staff. Although these [seminar and training provided by these consultants] were [appeared to be solely about] to take an opportunity to get some money from ... participant[s]. (Interviewee No. 4 - senior officer in MoHA)*

The first version of PBB in local government was based on MoHA decree No. 29/2002; it was a modified form of PBB that combined elements from international organisations (the UN and the World Bank), developed countries (the UK and the USA), and local influence from the *Lembaga Administrasi Negara* (LAN – State Administration Office) and *Badan Pengawas Keuangan dan Pembangunan* (BPKP – Financial Development and Supervisory Agency) (The Government of Indonesia, 2002b; 1999a; Ruswandi, 2005).

According to MoHA decree No. 29/2002 on the *Manual of Financial Formulation, Accountability and Supervision: Procedures of Budget Preparation for Local Government*, the first version of PBB implemented within Indonesian local government incorporated five dimensions of performance measures (inputs, outputs, outcomes, benefits, and impacts) (The Government of Indonesia, 2002b; 1999a). Originally from

the term of the LAN (The Government of Indonesia, 1999a), input measures refer to the number or value of resources used in delivering government activities (services), for example, money, skilled staff, operating equipment and facilities, and electricity. Output measures refer to the goods or services (products) delivered from one or more jobs from one activity in a ministry or agency. An activity could have one or more outputs with different units or product type. Outcome measures relate to everything that reflects the functioning of an activity's output in the medium term. An outcome is a measurement of how much of each product/service meets the public's needs and expectations. Benefit measures denote the usefulness of an output that is beneficial to the people, such as the availability of public facilities. Impacts measure the multiplier influence of government activity on social, economic, environmental or other public wellbeing. Impact is also evident in the medium and longer terms, as it describes the macro aspects of program objectives, the purpose of sectoral programs, and wider coverage areas both regionally and nationally. To understanding how performance information was used in budgetary plans during the first PBB implementation, see Appendix 5.

In many cases, local government staff members were unable to record complete performance measurements. There was claim from most of interviewees that performance measurement was a new term, with no agreement on measurement methods among PBB trainers and consultants. Budget teams rarely used performance information in budget development sessions and legislative budget committees rarely used them in budgetary decisions<sup>22</sup>, as two interviewees commented:

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<sup>22</sup> In early PBB implementation in Indonesia, there were two budgetary process steps. The first was budget formulation, requiring departments and agencies to submit their budget for review and analysis by a local government executive budget team. Departments and agencies compete to have their activities funded by government based on the budget allocation of each department and/or agencies. This step results in a budget draft document. Second, in a process termed budget enactment, the executive budget team presents the budget draft to the legislative budget committee for review and approval, based on the budget allocation for each department and/or agencies (The Government of Indonesia, 2002b).

*As far as I know, the budgetary team [executive] hardly considered any performance information in [the] RASK (Rencana Anggaran Satuan Kerja; budget proposal each activity) document to decide on which activity is approved or rejected. They only focused on the money spent on this activity, as each activity needed to fit within the total budget allocation. (Interviewee No. 14 - former member of a Local Government Association)*

*In legislative budget committee meetings, they [were] only concerned about how much allocation [there was] for each department or activity when approving [the] budget. They never looked back on the inputs, outputs or outcomes of each activity. It [was a waste of] time [using] their consideration. Only a few committee members considered performance information when deciding the budget. (Interviewee No. 15 - former member of a Local Government Association)*

The early version of PBB distinguished expenditure for offices of governmental officials (Local Government Secretary Office, Department of Finance, Planning Agency, Inspectorate, and Human Resources Agency) from those of the department of public expenditure (such as Department of Education, Department of Health, Department of Agriculture, and Department of Public Works). Further classification of these expenditures included general administration, operation and maintenance, and capital outlays (The Government of Indonesia, 2002b). However this budget classification was subject to debate among trainers and consultants who were impacted by the implementation. This debate related to the segregation of governmental official expenditure (*Belanja Aparatur*) and public expenditure (*Belanja Publik*) in the early version of PBB<sup>23</sup>. As mentioned above, several consultants argue that this segregation means that supporting departments' (such as the local Secretariat [*Sekretariat Daerah*], Planning Department [*Bappeda*], and Finance Department [*Badan Pengelola Keuangan Daerah*]) expenditures were categorised as 'official governmental expenditure' while functional departmental (including education, health, and public works) expenditure was classified as 'public

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<sup>23</sup> Based on the public expenditure theory, all public expenditure by government should be categorised as public whether it was spent on government officers or directly on public goods or services (Premchand, 1993). Thus, this Indonesian segregation of public expenditure seems unnecessary and unhelpful.

expenditure’. However, another consultant argued that this segregation was related to each department. Thus, using an example from the health department, the expenditure for the head of department and supporting staff are classified as governmental official expenditure, whilst expenditure for doctors, medical staff, and medicines are classified as public expenditure. See comment below:

*The first budget classification is very confusing; we found some local governments classify the governmental official expenditure [as being for] for all supporting departments’ [Setda, Bappeda, BPKD] expenditure, while unit departments’ [health, education, public work] expenditure were classified as public expenditures. However, in [other] local government [authorities], they used governmental official expenditure and public expenditure in each department. Based on their thoughts, all expenditure for staff is classified [as] governmental official expenditure, although it is found in the unit departments [health, education, public works]. Public expenditure is all expenditure [that relates to] public and society, although it is found in the supporting departments [Setda, Bappeda, BPKD]. However, both of these classifications were not based on the theory of public expenditure that categorised all expenditure in public organisation as public expenditure. (Interviewee No. 11 - university lecturer)*

Despite the first version of PBB being widely implemented across local governments, several problems were evident. First, there was potential budget duplication as a result of line-item utilisation within this version. Consequently, the budget continued to focus on line-item classification rather than program and/or activity categorisation. Budget items such as ‘general administration funds’, and ‘operation and maintenance’ were highlighted as objects of duplication, as similar sub-items existed in both items. Secondly, distinguishing between public expenditure and government official expenditure was problematic, as there was no single concept of how to segregate government expenditure. Finally, performance measurement became challenging and problematic for government officers and staff, as they lacked the necessary skills. The following quotes from interviewees illustrate these points.

*Based on my experience as a member of the MoHA team, budget duplication is one of the problems in the first version [of PBB]...[which] is [the result of] budget classification between the*

*general administration fund, and operation and maintenance.  
(Interviewee No. 11 - university lecturer)*

*In my opinion, the budget classification of 'pure budget spending' and 'governmental official spending' was confusing for us. It was still debatable and even, among team members, [there was no real understanding of the] concepts underlying this categorisation.  
(Interviewee No. 14 - former member of a Local Government Association)*

*The major problem in implementation is the difficulty in [understanding what is] performance measurement, as it is a new term in local government budgeting. Moreover, there are no similar examples of performance measurement that were introduced by MoHA team members or other central government agencies such as LAN and BPKP. (Interviewee No. 15 - former member of a Local Government Association)*

In 2003, the Government of Indonesia established Law No. 17/2003 on State Finances (*UU No. 17 Tahun 2003 tentang Keuangan Negara*) that fundamentally changed the financial regulation of central and local governments. This law required all levels of government to implement accrual accounting, a medium-term expenditure framework (MTEF), and PBB as their financial management approach. Consequently, budget formulation would incorporate a performance-based MTEF, with reporting based on the accrual accounting system (The Government of Indonesia, 2003). Law No. 17/2003 was followed by an enactment of GR No. 58/2005 on Local Government Financial Management [*Peraturan Pemerintah No. 58 Tahun 2005 tentang Pengelolaan Keuangan Daerah*], which oversaw local government implementation of the new financial management system (The Government of Indonesia, 2005).

Following the enactment of these new financial management regulations, and the problems experienced in the first phase of PBB implementation, the MoHA introduced a revised version of PBB by enacting MoHA decree No. 13/2006 on Local Financial Management (*Peraturan Menteri Dalam Negeri No. 13 Tahun 2006 tentang Pedoman Pengelolaan Keuangan Daerah*) in 2006. No. 13/2006 sought to eliminate line-item utilisation by focusing on program and/or activity classification, improving

performance measurement, and simplifying budget categorisation. The new version of the budget proposal form for each activity has only three performance measures (inputs, outputs, and outcomes), reduced from the five in the previous form (see Appendix 7). The measurement of benefit and impact were considered difficult within a one-year budget cycle, but the period principle remains in the new PBB version. Furthermore, to overcome the debate over the segregation of governmental official expenditure and public expenditure, this current version eliminates the segregation and replace it with a new form of expenditure segregation, namely direct (*Belanja Langsung*) and indirect (*Belanja Tidak Langsung*) expenditure (The Government of Indonesia, 2006). This new segregation was created to conform to the accounting classification of expenses, although it was still questioned by several consultants due to incompatibility to accounting practices (Abdirojo, 2010; Sugiyono, 2008). For instance, the departmental supplies and electricity expenses were categorised as direct instead of indirect expenses, while subsidy expenses were categorised as indirect instead of direct expenses (The Government of Indonesia, 2006).

Difficulties in the new version of PBB were also evident in the first version. Some local government entities rarely considered performance information within budgetary assessment when it reflected weak and low-quality aspects of performance measurement. Hence, this form has already focused on the classification of program and activity as one of PBB requirement despite the line-items (as part of traditional budgeting form) still existing. In addition to considering the MTEF adoption, the new form required each activity budget proposal to include the previous year's budget (year n-1), current budget (year n) and predicted year budget (year n+1) estimates.

With regard to Law No. 17/2003 on State Finances and GR No. 58/2005 on Local Financial Management, the implementation of the new MoHA decree sought to eliminate problems encountered in the first version of PBB. More importantly, its application was in parallel with the implementation of accrual accounting and

auditing as part of NPM concept, to expand the information publicly available (The Government of Indonesia, 2005; Harun et al, 2015). Accordingly, several elements were harmonised in the new PBB system, including the formulation of the *Bagan Akun Standar* (BAS – Account Standard Chart), which included accounting and budgeting accounts (Assets, Liabilities, Equity, Revenue, Expenditure and Financing). Thus the BAS accommodated the combining of the budget implementation report within the overall accounting report, and introduced the terms ‘budget report entity’ and ‘accounting report entity’ (The Government of Indonesia, 2006; RTI-International, 2009).

Further improvements that accompanied the implementation of the new version of PBB included enhanced integration and the linkage of local government planning and budgeting documents. This included linkages from programs and activities formulated in the planning document, which are then proposed and implemented in the budgeting document, and finally reported using accrual-based accounting reports (Dixon and Hakim, 2009). Until 2010, numerous efforts were made to integrate the planning, budgeting and accounting system through the revision of regulations. This included the enactment of MoHA decree No. 26/2006 and 59/2007 to revise MoHA decree No. 13/2006, and GR No. 71/2010 on the accrual accounting standard (RTI-International, 2009).

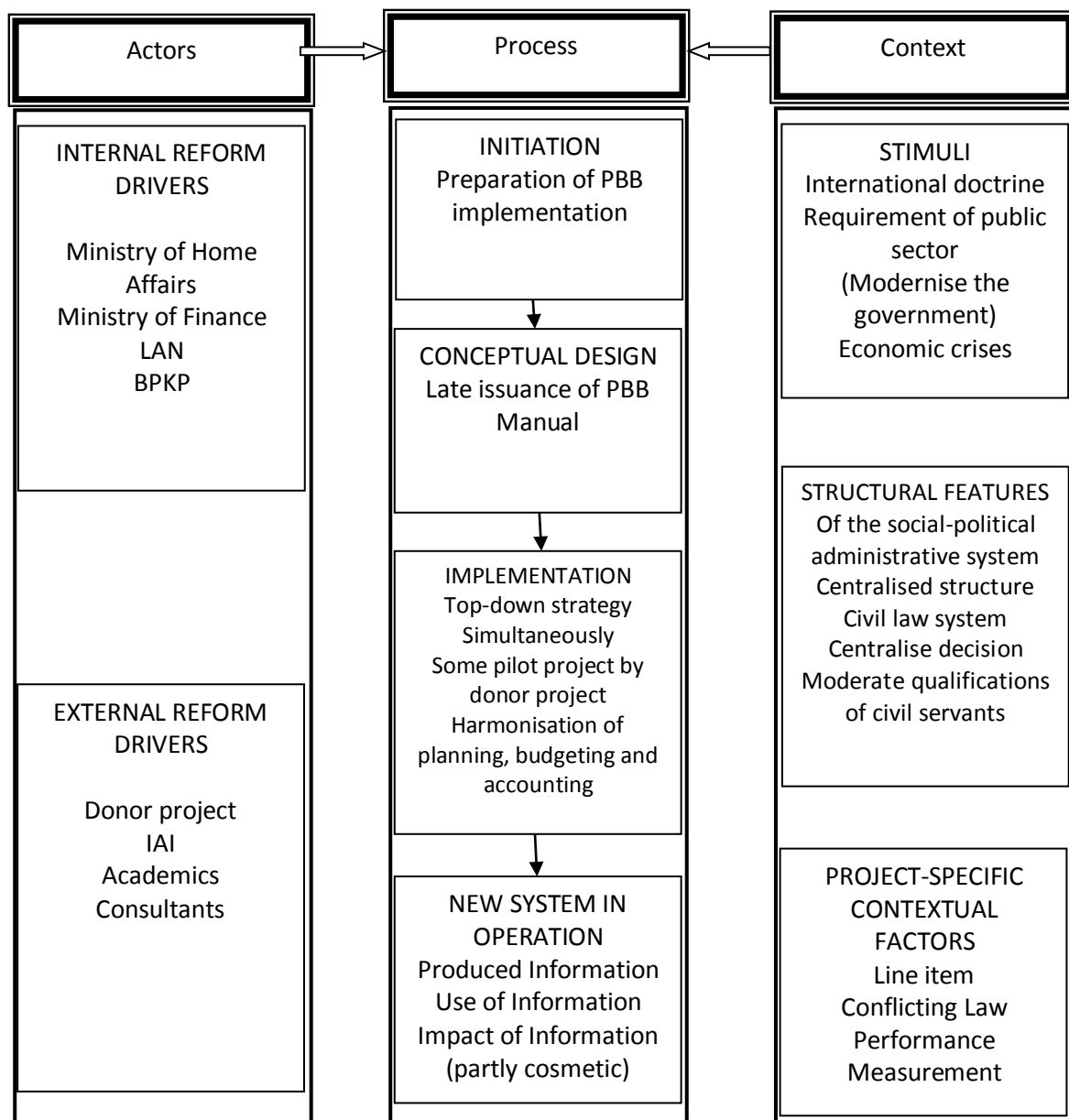
The following section applies the 2013 Lüder FMR model as a conceptual framework to examine the factors influencing the implementation of PBB within Indonesian local government during the period 1999–2010.

#### **4.7 The Factors Influencing Indonesian Local Government Budgeting Reform**

This section responds to the first research objective (see the introduction section of this chapter), related to the contingency factors that influenced budgetary reform within Indonesia. Section 4.4 outlines the FMR model (Lüder, 2013), and includes suggestions as to how to reclassify the political promoters, epistemic community,



institutional opponent and information users and producers into reform drivers. This study proposed a version of the Lüder FMR model (2013) designed to facilitate this research into Indonesian local government budgeting reform. The findings of this research are presented with respect to each module from the adapted Lüder FMR model (2013), as shown in Figure 7.



**Figure 7. Author's elaboration of a new financial management reform process model (Actors - Process - Context modules) from Lüder (2013) in the Indonesian local governments budgeting reform (an adoption of PBB)**

#### 4.7.1 Stimuli

It was claimed by most of participants that the first stimulus for Indonesian budgeting reform came from internal government officers and academics who sought to change and modernise the government's financial management system in the 1980s (see the interviewees' statement in section 4.6.1). However, this stimulus was not strong enough at that time to reform the budgeting system, as there was low political support from executive government. Nevertheless, this failure to reform served as a factor in the decision to implement PBB during the 1990s, which was triggered by the international uptake of NPM reform that included the PBB system (Ruswandi, 2005). Two interviewees confirmed this view:

*Without doubt, PBB implementation in Indonesia was triggered by the emergence of NPM reform. As a part of [the] NPM concept, the central idea of PBB is to create value for money. [W]e can measure the budget performance for program[s] and activit[ies]. (Interviewee No. 3 – ex-senior officer, MoHA)*

*We teach that ... our reform originated from NPM, because Indonesia [was] influenced by this model after the spark of NPM in the UK.... it was agreed that NPM was the source of the spirit for budgeting reform in Indonesia (Interviewee No. 6 – former senior consultant, donor project)*

The financial crisis of 1997 significantly accelerated progress towards decentralisation and democratisation in Indonesia (Hadiz, 2004), and strong stimulus for PBB adoption within local government was a reflection of this. Decentralisation was followed by a significant amount of funds being transferred from central to local government, which resulted in the need for new budgeting systems (Dixon and Hakim, 2009). This is consistent with Harun and Robinson's (2010) finding that the financial crisis and decentralisation triggered accrual accounting adoption within Indonesian local government. According to the Lüder (2013) classification, this study argued that the stimulus of Indonesian local government budgeting is one of "doctrine driven project initiation" (p.11), where the

primary intention of budgeting reform is to implement PBB as the generally accepted financial management technique.

#### **4.7.2 Reform Drivers**

Participants consistently agreed that within Indonesian local government budgeting reform, strong internal reform drivers included the Indonesian MoHA and the Indonesian MoF. MoHA exercises authority over reform through:

- their influence (with the MoF) on the formulation of Law 17/2003 on State Finances;
- GR No. 105/2000 on local government financial management and accountability and 58/2005 on local government financial management (also with the MoF); and
- several MoHA decrees (No. 29/2002, No. 13/2006, No. 26/2006 and No. 59/2007) regarding the local government financial management manual. These MoHA decrees are fundamental to PBB implementation.

*A strong supporter for PBB implementation [within] local government is MoHA. They [are] involved in every regulation concerning local government financial management [including] Laws [Law 17/2003], GRs [GR 105/2000 and GR 58/2005] and of course their [MoHA] decrees [No. 29/2002, No. 13/2006, No. 26/2006 and No. 59/2007] (Interviewee No. 8 – the IAI member).*

The LAN and BPKP also act as internal reform drivers. Both were influential in improving performance measurement through PBB implementation within local government. Support from legislative members in the central government was evident from their agreement on the enactment of Law No. 17/2003, although it is limited (Ruswandi, 2005; Harun, 2010). Apart from Law No. 17/2003, legislative support at the local level was varied. Some legislative members support PBB as a technique that encourages transparency in public spending, whilst some reject PBB adoption due to greater difficulty and complexity than traditional budgeting (The World Bank, 2007b). This was articulated in greater detail by an interviewee:

*As far as I know, support from central legislative [authorities] is only evident in the support for Law 17/2003... [From a local perspective] not much evidence was found [to support PBB]. It was dependent on the local government authority. Some of their legislative members provide good support [to the reform], but other local government [officers] experienced weak support [from their legislature]. (Interviewee 4 - Senior Officer in MoHA)*

Both scholarly networks and epistemic communities are external reform drivers that can provide strong support for implementation. The decision to implement PBB for local government was made by central government officers in consultation with academic scholars. Some academics were also members of the regulatory team that supported implementation through the formulation of:

- Law No. 17/2003 on State Finances, GRs (such as GR No 105/2000 on Local Government Financial Management and Accountability;
- GR No. 58 on Local Government Financial Management and Minister's decrees (MoHA decrees No. 29/2002, No. 13/2006, No. 26/2006); and
- MoHA decrees No. 59/2007 regarding the local government financial management manual (The World Bank, 2007b; 1998).

Another external reform driver is foreign country donors through their Non-Government Organisation (NGO) projects, such as BIGG, the NDI, PERFORM (Performance Oriented Regional Management), VNG and the UNDP. All helped influence the introduction of PBB concepts to their local government partners (RTI International, 2009). They also participated in joint collaborations with the MoHA and the MoF on PBB dissemination (RTI International, 2009; Harun and Robinson, 2010). As one interviewee noted:

*We worked together with several local governments as partners in pioneering PBB implementation in Indonesia. We also influenced the formulation of regulations as consultants, and helped finance PBB implementation [through the use of] our funds. (Interviewee No. 7 - former donor project senior consultant)*

All interviewees mentioned that the IAI members influenced the introduction of the PBB model within local government in several ways. The IAI members were involved in delivering PBB training in seminars for government officers, and several IAI members, as individuals, influenced the formulation of MoHA decrees on PBB (Harun, 2010). Interviewees said:

*We [IAI] sometimes raised the topic of double-entry bookkeeping and PBB implementation in the seminars and workshops and invited government officers to discuss. However, some IAI members also [acted on their own accord to assist] organisational consultants [with] technical assistance in some [of the] ministries. (Interviewee No. 8 – IAI member)*

*Some of us... for instance [Mr A] and [Mr M], influenced how PBB [was taught and understood] as a member of the regulatory team. Albeit they acted as individuals, they are [nevertheless] also IAI members. (Interviewee No. 9 – the IAI member)*

In addition, several private consultants from various technical backgrounds influenced PBB implementation; some of them were non-governmental organisation (NGO) members with expertise in budgeting, whilst others were academics with expertise in public sector management:

*We knew several friends from NGOs and universities who also engaged with consulting firms to deliver the necessary training and technical assistance on PBB. (Interviewee No. 7 - former donor project senior consultant)*

#### **4.7.3 Structural Features**

Using the Lüder FMR model (2013) classification of structural features, this study identified several unique cultural attributes of the Indonesian social-political-administrative system – state structure, legal system, administrative structure, and the qualifications of civil service personnel – that might have enabled or hindered PBB implementation. Firstly, Indonesia is a unitary of states government with a bicameral parliament, the People’s Consultative Assembly (*Majelis Permusyawaratan Rakyat*) and the People’s Representative Council (*Dewan Perwakilan Rakyat*), which is also referred to as the House of Representatives. Both of these chambers are symbols

of legislative power, with the President as head of the Executive. In the previous New Order (*Orde Baru*) era<sup>24</sup>), the division of power between the legislative and executive branches did not exist in reality, as the *Golongan Karya* (GOLKAR) party of President Suharto controlled more than 60% of the seats in parliament. The authoritarian regime had absolute power to control all sectors, including parliament, opposition parties, the media, economic development, trade and the exploitation of natural resources (Liddle, 1999).

The New Order regime, with its strong political structure and control of the Indonesian economy, hindered the implementation of any new system (including budgeting and accounting) that would have made government finances more informative and transparent, as it would have threatened their absolute power (Hadiz, 2004; Hadiz and Robison, 2005; 2013). Thus, the state structure was a barrier to attempts to adopt PBB. However, the fall of Suharto's regime as a result of the Indonesian economic crisis gave rise to the new democratisation era in 1999, and a greater separation of power between the legislative and executive branch was created after the 1999 election (Hadiz and Robison, 2005; 2013). This new era, known as the 'Reform Order' (*Orde Reformasi*), mandated the implementation of new systems (including budgeting and accounting) for more informative and transparent government finances. The MoF and the MoHA led this transformation, with support from the IMF and the World Bank (Harun, 2007). My study found that this combined structure, along with strong executive power from MoHA and MoF, is beneficial in supporting governmental reform and PBB implementation.

Secondly, the Indonesian legal system, being a legacy of Dutch colonialism (Emerson, 1983), is based on the Roman-Germanic tradition, where there is a comprehensive and detailed system of statute, civil and code law (Lüder, 1992; 1994). Countries with the Roman-Germanic tradition have procedures and principles

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<sup>24</sup> The New Order (*Orde Baru*) is the regime established in 1966 after the fall of former President Sukarno following the Indonesian army's anti-communist purge. The new order regime was led by General Suharto until his resignation in 1998 (Hadiz, 2004)

specified and detailed in codified law within rigid systems. There is less flexibility for reform than in some other systems (Lüder, 1992), which is an impediment to PBB implementation as local government has no discretion to modify PBB concepts. Consequently, the identical PBB concept and form is found across the 34 provinces, 98 cities and 416 districts of Indonesia, despite differences in social, economic and cultural factors. As one interviewee noted:

*We [have inherited a] legacy [including] a political culture, legal system and administrative framework from Dutch colonialism. In my opinion, this sometimes hinders the implementation of new financial management systems. (Interviewee No. 11 – university lecturer)*

Furthermore, this focus on uniformity, being identical PBB form, resulted in a lack of substance. Thus, as PBB is a part of the accounting management system, it contradicted the accounting concept of “substance over form”. As stated by one interviewee:

*...when we talk [about] accounting standards, there is a substantial principle [regarding] form, [namely] substance over form. In [the Indonesian] government, [this] principle is not [applied], why? [Because] in Indonesia [PBB form] must be based on the regulations [and uniformity in each local government],... therefore, the principle is ...not appropriate [as there is no discretion to develop their own format in achieving substance]. (Interviewee No. 11 – university professor)*

Thirdly, the control of the administrative structure, including PBB implementation within the Indonesian government, relates to the central government. Although decentralisation of PBB has been implemented across Indonesia, several aspects, including regulation and new system implementation, remain under the direction of central government authorities (Harun and Robinson, 2012). Lüder (2013) argued that weaknesses in centralised decision-making are a barrier to new system implementation. In support of this, this study has found that remnant colonial administrative structures that originated from Dutch-Roman administration (Harun et al., 2015), also pose barriers to Indonesian PBB implementation.

Fourthly, the qualifications of Indonesian civil servants and their ability to implement reform vary. Most cities in Java, and parts of Sumatra, Sulawesi, Kalimantan, Bali, and West Nusa Tenggara, have highly educated and professionally qualified civil servants, which increases the chances for successful PBB implementation in these areas. However, in the remaining areas of Indonesia, poorly qualified and experienced staff often means PBB implementation failure although significant effort has been made to minimize this problem.

*Well-qualified civil servants are concentrated mostly in Java, and partly in Sumatra, Bali and West Nusa Tenggara, and some other big islands [Kalimantan, Sulawesi]... They have the capability to absorb [and understand] training materials ... and implement PBB within their local government. However, some of them [civil servants] do not want to learn. They depend on the consultant to help them formulate their budgets. (Interviewee No. 12 – university lecturer)*

*[The] qualification of [our] government staff also sometimes hinders implementation ... [Some] have qualified staff, however, in other local governments, it was rare [to have qualified staff] (Interviewee No. 4 – senior officer in MoHA)*

#### **4.7.4 Project-Specific Contextual Factors**

In the case of Indonesian local government budgeting reform, line item utilisation in the first version of PBB was claimed by participants to be one barrier to PBB implementation in its full format (see Appendix 6), as evidenced by two interviewees:

*We know that our first PBB still had line items. It needed to be eliminated [as it was a problem for implementation] (Interviewee No. 2 – senior officer, MoHA).*

*Based on this [PBB] model, [we] still used [the] line-item model. It is a problem. So, I guarantee that [by using this model] in the local government, their [executive and legislative] focus is on the structure, not on the performance. The reason is it [relates to] their money. They do not care for performance as long as they get their money. (Interviewee No. 9 – the IAI member).*



The introduction of the new PBB version reduced, but did not eliminate this barrier (see Appendix 8) (The Government of Indonesia, 2006). The second impediment to PBB implementation were the conflicting laws evident during the first implementation phase, namely Law No. 17/2003 on State Finances and GR 105/2000 on Local Government Financial Management and Accountability, which mandated PBB implementation within local government. Furthermore Law No. 22 /1999 on local government offered local governments 'discretion' when undertaking financial management (Harun and Robinson, 2010), although it was repealed and there was a return to more centralisation by the new Law No. 32/2004 on local government (The Government of Indonesia, 2004a). Despite PBB implementation being widespread across local government, another implementation barrier was the low quality of performance measurement and utilisation of performance information during budget formulation. This problem arose due to qualitative performance information, which is available in the budget proposal, rarely being used as a basis for budget evaluation. Two interviewees noted.

*As a lecturer and consultant, I realise that their [local government] quality of performance measurement is still weak. More often than not, they leave the performance measurement elements in the budget proposal still blank or uncompleted. The reason is [that the] executive budget team and legislative budget committee rarely use this performance information to assess the budget proposal. .. Assessment of the budget proposal often only considers quantitative [levels of expenditure] not the qualitative performance of the expenditure categories. (Interviewee No. 12 – university lecturer)*

*Most of us had a lack capability of staff knowledge, and we also had a problem with our performance measurement. As you know, it was new for us, and we do not have data regarding our first performance information. We worked very hard to improve our competencies (Interviewee No. 15 – - former member of a Local Government Association)*

#### 4.7.5 *Initiation*

The reform of Indonesian budgeting commenced during a meeting between academics and government officers who had previously attended financial management training in the UK during the 1990s. This discussion resulted in the initial decision to adopt PBB as a basis for Indonesia's central budgeting system. Subsequent preparations included the formulation of performance measurement plans and designs for project implementation (Harun and Robinson, 2010; Ruswandi, 2005). However, the initial phase was postponed due to the lack of qualified personnel and low political commitment from government (Harun, 2007).

#### 4.7.6 *Conceptual Design*

The conceptual design of the PBB, as the second process underlying its implementation, was formulated and promulgated by the MoF at the central government level and MoHA at the local government level. After the economic crisis subsided, the concept of PBB once again gained traction with the design, development and formatting of PBB modules (Ruswandi, 2005). However, before the development of PBB modules was completed, a formal decision to implement PBB was made by the issuance of GR No. 105/2000 on Local Government Financial Management and Accountability. GR No. 105/2000 led to confusion, as whilst the regulation ordered the implementation of PBB, the concepts, modules and manuals underlying PBB had not yet been decided or completed by the MoHA team (ICMA, 2002). Hence, from the first PBB manual from MoHA (see the MoHA decree No. 29/2002 explanation in the section 4.6.1), the conceptual design for PBB in Indonesia was a modified PBB system that still included the line-item and incremental forms (as part of traditional budgeting). One interviewee explained that the reason for modification was:

*..to make a clear understanding [for us] that a new system cannot be directly implemented without modification, so we need to modify each*

*system. It relates to the culture [or the organisation] (Interviewee No. 13 – former member of a Local Government Association)*

#### **4.7.7 Implementation**

In 2002, two years after the issuance of GR No. 105/2000, the first PBB manual (see the MoHA decree No. 29/2002 explanation in section 4.6.1) was finally published and ready for implementation. This meant that the implementation of PBB included the authoritarian and centralised guidance from the MoHA. Further, the MoHA teams adopted a top-down approach and direct conversion for PBB system implemented throughout Indonesian local government simultaneously. Regular training sessions and workshops were held in Jakarta and in several local governments across Indonesia to accelerate the dissemination and implementation of PBB (The World Bank, 2007b). One interviewee noted:

*Once they [MoHA finished] formulating [the] new MoHA [decree], they...disseminated [this] and [then] directly implemented this system. So it was direct implementation (Interviewee No. 14 – former member of a Local Government Association)*

Many local governments indicated their readiness to implement this new system as they had experience with a pilot project as a focus area during a donor program (RTI International, 2009; ICMA, 2004).

#### **4.7.8 New System**

The final part of the reform process is the implementation of the new system. In the case of Indonesian local government budgeting reform (PBB implementation), this step allows governments to produce reports, using performance information and detailed unit data in the budgetary process, and obtain the impact of the new system. In fact, after an implementation process over several years, PBB was finally implemented as a budgeting system within Indonesian local government, with varied results. Whilst PBB has been relatively successful at face value to date in terms of having a system implemented, numerous problems have been encountered

and many have yet to be resolved. Considering the poor quality of performance measurement attributes evident during the PBB implementation process and subsequent budgetary reports, and given that performance measurement is the most significant principle of PBB, borrowing Guthrie (1998) terminology, the impact of budgeting reform within Indonesian local government has largely been cosmetic and one of rhetoric. PBB implementation has resulted in little actual performance measurement. However, throughout the second phase of this reform, efforts were made to harmonise planning, budgeting and accounting to enhance budgeting reform and allow better integration with other reforms (The Government of Indonesia, 2010).

Overall, by using the Lüder FMR Model (2013) as a conceptual framework, this study was able to examine in detail, the motives that underpinned the development of PBB within Indonesian Local Government, the process and outcome of this budgeting reform, and the factors influencing its implementation.

#### **4.8 Conclusion**

The purpose of this research was to investigate the motives for the development of PBB within Indonesian local government and the factors influencing its implementation. This study involved an application of the latest FMR model (2013) as an interpretive framework for understanding budgeting reform within Indonesian local government. This research also drew on Lüder's (2013) appeal to study budgeting reform within a regional and local government context, using the Lüder FMR model, which focuses on process and outcome orientation in local government. Based on the findings with regard to budgeting reform within Indonesian local government, several conclusions can be drawn that relate to the three research objectives outlined earlier in the chapter/paper.

The first research objective related to the contingency factors that influenced budgetary reform within a developing country. The first stimulus for budgetary

reform in Indonesian local government (implementation of PBB) was public sector interest in modernising government, inspired by the international doctrine from superior countries' (the US and the UK) budgeting practices. This government modernisation process was supported by the World Bank. The PBB system was generally accepted as one solution for modernising government, and a decision to implement PBB was initially conceived among government officers and academics who had experienced NPM training overseas.

This first stimulus was followed by the Indonesian financial crisis of 1997, generally regarded as the main stimulus for accrual accounting reform within Indonesian central and local government (Harun and Robinson, 2010; Harun et al, 2015). Economic crisis as a stimulus for change was also evident during the first wave of PBB adoption in the US federal government that emerged after the Great Depression and an unstable economic situation before and after World War II (see Jones and McCaffery, 2010). Similar events drove PPB adoption after Denmark's economic crisis in the 1980s (Ginnerup et al, 2007) and crises in other OECD member states, such as Portugal (Jorge, 2003) and Greece (Karkatsoulis, 2010). However, different stimuli such as budget deficits and performance measurement problems were found in the Malaysian second wave of PBB (the Modified Budgeting System) (Siddiquee, 2006). In the UK, strong political power that required a more informative budgeting system was the stimulus for the adoption of PBB (termed the Financial Management Initiative) (Gray and Jenkins, 1986).

Indonesian local budgeting reform was initiated by the Indonesian central government in 2000 (the Government of Indonesia, 2000) with the decision to fully implement PBB with the support of various ministries and agencies (MoHA, MoF, BPKP and LAN) as internal reform drivers, and external reform drivers including donors, academics, the IAI and consultants. Thus, compared to the NSW, Hessian (Lüder, 2013), and Campania situations (Bruno, 2014) previously discussed, Indonesian local government had strong contingency factors supporting budgeting reform.

The decision to adopt, and preparatory efforts to implement, PBB within Indonesian local government, was made in the 1990s by Indonesian technocrats (government officers from MoF and MoHA, and Indonesian academics). This was driven by their awareness of more efficient and effective budgeting systems, an early motive for PBB implementation within Indonesian local government, and this concept was supported by the World Bank. However the initial implementation of the budgeting reform process (prior to the Indonesian economic crisis in 1997), experienced delays due to the lack of qualified personnel and low political commitment from government, despite several achievements (see section 4.6.1). The implementation continued after the economic crisis of 1997 as part of NPM reform to address one of the clauses in the funding agreement between the IMF and the Indonesian government. In discovering the historical context leading up to budgetary reform, and the contingency factors that influenced budgetary reform (PBB implementation) within Indonesian local government, this study achieved its first and second research objectives.

The third objective of this study was to determine how PBB implementation occurred within Indonesian local government. This study found that the implementation of PBB was initiated from MoHA, which was the oversight body within the Indonesian central government that supervised and controlled local government. Therefore, the PBB concept was formulated under the authority of MoHA and later disseminated across Indonesian local government (provinces and cities/districts) through regulations, training and technical assistance. Although the formal initiation of PBB implementation within local government commenced in 2000 (as an enactment of GR No. 105/2000), in reality this was effective from 2002 after the MoHA enacted decree No. 29/2002, which was supported by the MoHA and MoF. The other donor projects (such as USAID, CIDA, NDI, and UNDP), the IAI and consultants also supported the process of PBB implementation within Indonesian local government.

Similar to the reforms in Campania (Bruno, 2014), there was a degree of harmonisation between PBB implementation and accounting reform in Indonesia. Better integration of budgeting and planning allowed for greater harmonisation between planning, budgeting and accounting reform in 1999–2010 within Indonesian local government. This supports Ho's (2011) and Melkers & Willoughby's (2001) suggestion that to fully comprehend the significance of PBB, complementary reforms are necessary.

The most significant barriers for PBB implementation were: (1) utilisation of a line-item and incremental approach during the first implementation phase, as these approaches were the legacy of the traditional budgeting process that resulted in budget inefficiency and ineffectiveness; (2) conflicting regulations relating to local financial management; and (3) weak performance measurement within the budgeting reform process that resulted in PBB implementation being partly cosmetic. This problem also occurred in the first implementation of PBB in countries such as Malaysia, India, Philippines, Sweden, Slovenia and Denmark (Aristovnik & Seljak, 2009; Dean, 1986a; Curristine, 2005). Therefore, despite achievements being made in the implementation of PBB within Indonesian local government, success was tempered by the low quality, and consequent under-usage of, performance information and measurement. However, this barrier was also a possible motivator for the next reform, as suggested by Lüder (2013).

Overall, the data from this study answered the research question of how and why, throughout the period 1999–2010, the Indonesian central government (through MoHA) mandated Indonesian local governments to reform their budgeting systems using PBB. This study was able to examine the contingency factors that influenced budgetary reform within Indonesian local government, using the Lüder FMR Model (2013) as a conceptual framework. Furthermore, this study revealed the historical context leading up the implementation of PBB within Indonesian local government, and determined the process by which it occurred. Additionally, to allow PBB to be fully integrated into Indonesian local government, several improvements should be

made such as to fully remove the line-item and incremental forms in the current Indonesian PBB format, thereby providing a clear segregation between direct and indirect expenditure using an accounting approach. This would provide a good example of performance measurement across local government departments, and provide valid data for accurate performance measurement.

This study adds to the management accounting literature on PBB and budgetary reform by utilising the Lüder FMR Model (Lüder, 2013) as a conceptual framework to examine budgeting forms, particularly the development of PBB and its application in Indonesia as a developing country. In using this framework, this study analysed the contingency factors influencing the adoption of PBB within Indonesian local government, and examined the main motives for Indonesian local government budgeting reform.

This study provides practical guidance for global organisations (e.g. OECD, IMF and the World Bank) and foreign donor projects (e.g. USAID, CIDA, NDI, and JICA), in that the results can help in the formulation and assessment of the influence of current and future policymaking on Indonesian central government and other transitioning countries. Furthermore, given the uniqueness of the Indonesian central government's budgeting reform process, this study provides guidance to the Indonesian central government on ways to further align policies that will strengthen and develop PBB over time, given the problems and challenges found during implementation. The Indonesian experience of PBB implementation has lessons for other developing countries that are adopting or intend to adopt and implement PBB.

This study has limitations with respect to research method, as the primary data were collected from only 15 respondents. Therefore, caution should be exercised when applying these results to PBB implementation across a broader range of public sector organisations within the Indonesian government.



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## **5. Conclusion**

This chapter presents a summary of the research, including overall findings and their implications, recommendations for successful implementation of PBB, and the limitations of this study. The chapter ends with an overall conclusion.

### **5.1 Overview**

This thesis incorporates three papers that collectively provide a new understanding of how countries adopt performance-based budgeting (PBB) as their budgeting system (Table 3). In particular, they reveal how and why Indonesian public sector organisations adopted and implemented PBB. This research was designed to fill a gap in knowledge concerning the history of PBB through an examination of its implementation as part of fiscal reform in the public sector, specifically in the Indonesian context.

Following the work of Lüder (2002; 2013) on the factors influencing public sector accounting reform, and Timoshenko and Adhikari's (2009) research on the institutionalisation process in accounting and budgetary reform, this study used Indonesian budgetary development (PBB adoption and implementation) from the 1990s to 2010 as a case study. In this period Indonesia, a developing and transitioning country, moved from an authoritarian and centralised system to a Western-style system of transparent government. Before this reform of the political system Indonesia had no transparent accountability process, including in its budgeting system. Despite an ongoing debate over the relevance and value of PBB in the public sector, the Indonesian government adopted and implemented PBB in an attempt to construct a more informative and efficient budgeting system. This study's objectives were to; 1) systematically examine the motives that underpinned the development of PBB and factors influencing its implementation across countries, 2) investigate how and why the Indonesian central governmental budgetary processes

changed in 2003, from traditional to PBB, and the extent to which isomorphism was evident during PBB implementation, and 3) investigate the motives that drove the implementation of PBB within Indonesian local government and the factors that influenced the process.

**Table 3: Summary of Thesis**

<b>THE ROLE OF PERFORMANCE-BASED BUDGETING IN THE INDONESIAN PUBLIC SECTOR</b>		
<b><u>Paper 1:</u></b> A Conceptual Framework for Budgetary Reform within Public Sector Organisations	<b><u>Paper 2:</u></b> The Transformation of Indonesia's Central Governmental Budgetary System	<b><u>Paper 3:</u></b> The Implementation of Performance-Based Budgeting within Indonesian Local Government
<b><u>Purpose:</u></b>  Reveal the motives that underpin the development of PBB and the factors influencing its implementation	<b><u>Purpose:</u></b>  Examine how and why the central governmental budgetary processes in Indonesia, a developing and transitioning country, changed in 2003 from traditional budgeting to PBB.	<b><u>Purpose:</u></b>  Investigate the motives for the development of PBB within Indonesian local government and the factors influencing its implementation
<b><u>Research Question:</u></b>  1. When and why did public sector organisations within nation states implement PBB in their budgetary reform? 2. Which reform drivers and institutional arrangements helped shape various governments' decisions to implement PBB? 3. What and why did public sector organisations, specifically governments, encounter barriers to PBB implementation during the budgetary reform process?	<b><u>Research Question:</u></b>  How and why did the Indonesian Central Government focus on implementing PBB as the new budgeting system from 2003 to 2010?	<b><u>Research Question:</u></b>  How and why did Indonesian local governments reform their budgeting system using PBB during 1999-2010?
<b><u>Design/methodology/ approach:</u></b>  <ul style="list-style-type: none"> <li>Lüder financial management reform process (FMR) model (Lüder, 2002).</li> <li>Secondary data obtained from public sector journals and literature, OECD publications and reports, international organisation publications and reports, and archival material including government legislation and promulgations.</li> </ul>	<b><u>Design/methodology/ approach:</u></b>  <ul style="list-style-type: none"> <li>New Institutional Sociology (NIS) Theory on isomorphism and institutional pressure for budgetary reform (DiMaggio and Powell, 1983; Meyer and Rowan, 1977).</li> <li>Primary data obtained through interviews and archival material including government reports and regulations, international organisational publications, foreign donor project reports, and academic literature.</li> </ul>	<b><u>Design/methodology/ approach:</u></b>  <ul style="list-style-type: none"> <li>Lüder FMR model (Lüder, 2013).</li> <li>Primary data obtained through interviews and archival material including government reports and regulations, international organisational publications, foreign donor project reports, and academic literature.</li> </ul>



<p><b><u>Findings:</u></b></p> <ul style="list-style-type: none"> <li>• PBB was first implemented in the US in 1949 and expanded to developing countries through US- and UN-funded projects.</li> <li>• The primary motive underpinning implementation in the US, the UK, Australia and Denmark was the rise in demand from the public sector for more informative and measured budgets.</li> <li>• Influence from the US and UK budgeting systems has been the primary stimulus for PBB implementation across the globe.</li> </ul>	<p><b><u>Findings:</u></b></p> <ul style="list-style-type: none"> <li>• In the initial period (1990s), most of the impetus for change originated from Indonesian technocrats (government officers and academics) who proposed PBB after their participation in an international public sector workshop.</li> <li>• During the second period (2003), moderate coercive pressure to implement PBB emanated from the IMF and the World Bank, and the Indonesian central government responded with an avoidance strategy.</li> <li>• This avoidance response, coupled with the occurrence of weak mimetic and strong normative (from Indonesian technocrats) pressure in the institutionalisation of PBB, is evident through the modified form of PBB used across the Indonesian central government.</li> </ul>	<p><b><u>Findings:</u></b></p> <ul style="list-style-type: none"> <li>• The primary motive of PBB implementation within Indonesian local government was the Indonesian technocrats (government officers and scholars) demand to modernise its financial and reporting system, with support from the foreign donor projects.</li> <li>• The harmonisation of planning, budgeting and accounting occurred as a means by which to embed reform.</li> <li>• The Lüder FMR model (2013) is a useful framework to identify key factors behind the implementation of PBB within Indonesian local government.</li> <li>• Weak performance development identified after PBB implementation indicated that budgeting reform was partly cosmetic.</li> </ul>
<p><b><u>Research Limitations:</u></b></p> <p>The Lüder FMR model (2002) has limited utility for examining historical budgetary reform in multiple countries; it requires more chronologically detailed data for deeper analysis relating to international events.</p>	<p><b><u>Research Limitations:</u></b></p> <p>Respondents had major roles in Indonesian central government budgeting reform, but their small number limits the ability to generalise from the results.</p>	<p><b><u>Research Limitations:</u></b></p> <p>Respondents had major roles in Indonesian local government budgeting reform, but their small number limits the ability to generalise from the results.</p>
<p><b><u>Originality/Value:</u></b></p> <p>The study included a novel utilisation of the Lüder FMR model (2002) to study the evolution and early global development of public sector PBB.</p>	<p><b><u>Originality/Value:</u></b></p> <p>The utilisation of NIS as a lens to examine the implementation of budgetary reform using PBB within a developing country is unprecedented in the field.</p>	<p><b><u>Originality/Value:</u></b></p> <p>The utilisation of the Lüder FMR model (2013) to investigate budgeting reform within a developing country context, specifically PBB implementation within Indonesian local government, is innovative.</p>

## 5.2 Summary of Findings

This research delivered an understanding of how countries around the globe adopted PBB. In particular, it revealed how and why Indonesian public sector organisations – as part of a transformation from an autocratic to a more accountable, transparent and democratic society, implemented PBB as their budgeting system.

This was achieved through a historical examination of political and economic events in Indonesia leading up to the major period of budgetary reform.

Indonesia in the New Order (*Orde Baru*) era was ruled by an authoritarian regime that controlled parliament, opposition parties, the media, economic development, trade and the exploitation of natural resources. This autocratic structure allowed (and encouraged) the Indonesian government system to become opaque and unaccountable.

Following the economic crisis in 1997 and the consequential inflationary pressures on the economy, riots among the Indonesian public forced the resignation of President Suharto and ended the New Order era. To end the economic crisis, the Indonesian central government asked for IMF aid. In supporting the Indonesian economic recovery, the IMF stipulated that the Indonesian government must implement sweeping changes, beginning with structural reform (decentralisation and democratisation) (Tarmidi, 1999; Hadiz, 2004; Hadiz and Robison, 2013). This structural reform was followed by government financial management reform, particularly in budgeting, accounting, auditing, and performance measurement. The Indonesian government decided to utilise PBB as their budgeting system both in central and local government, despite ongoing debate over the value and effectiveness of PBB. To understand the rise of PBB in Indonesia and elsewhere, this study examined the motives that underpinned the development of PBB and the factors influencing its implementation.

### ***5.2.1 Budgetary Reform within Public Sector Organisations***

Budgetary reform is major change in a budgeting system within a public sector organisation. Public sector organisations worldwide have reformed their budgetary systems utilising PBB, focusing on measuring performance, integrating performance reviews with budget submissions, and seeking to embed accurate performance measurement (see Moynihan, 2006; Franklin, 2006, Aristovnik and Seljak, 2009, Schick, 2007). Historically, PBB was developed at approximately the same time as

the idea of performance management. The first wave of PBB was implemented in the US federal government in 1949 in response to fiscal stress and financial scandals (Dongsung, 2005; Jones & McCaffery, 2010). PBB was integrated with program budgeting and focused on organisational structure, including mission statements, organisational goal/objectives, and core/sub-service activities, and was implemented across US states and local government (city and county) (Schick, 2007, Shah and Shen, 2007). Thus, prior studies in the US show that demand from the public sector for more informative and measured budgets was the initial motive underpinning PBB implementation. This stimulus is also evidenced in subsequent research in the UK, Australia and Denmark. However, the influence of former colonial powers and donor programs (largely US- and UN-funded projects) is the main stimulus behind PBB implementation across developing countries.

The first phase of PBB implementation (1949–1989) did not substantially improve the efficiency and effectiveness of public sector budgeting. Although the implementation of PBB resulted in better use of performance information in budgeting systems, this performance information was not used properly in linking performance information to resource allocation. This problem occurred due to weak performance measurement and the reluctance of management and legislators to use performance information in budget decisions. Hence, this first phase of PBB implementation was unable to eliminate the inefficiency and ineffectiveness caused by traditional budgeting. Another reason why the aims of the first wave of PBB were not fully achieved is the fact that implementation, particularly in developing countries, was strongly stimulated by the US and the UN through their donor programs, rather than being based on the requirements of the recipient country. In response to these difficulties, PBB was modified into several budgeting forms (such as zero-based budgeting [ZBB], and the planning, programming and budgeting system [PPBS]); however, these had their own problems, such as increased paperwork in the budgeting process, a lack of performance information needed for ZBB analysis, and difficulties in measuring the costs and benefits of programs and

complexities in linking programs with budgetary structures in PPBS (United States General Accounting Office, 1997).

In the 1980s, PBB was revived as part of the new public management (NPM) concept that aimed to make government more 'business-like', to ensure that government delivered the necessary services and was accountable to its citizens (Pollitt and Bouckaert, 2011). This rebirth of PBB, later termed 'new PBB', focused more on customer orientation as part of NPM. This new PBB came to dominate budgetary reform within governments, including the Indonesian government.

### ***5.2.2 The Transformation of Indonesian Governmental Budgetary System***

Two phases of PBB implementation occurred within the Indonesian central government. In the initial period (1990s), most of the impetus for change originated from Indonesian technocrats (internal governmental officers and academics) who proposed PBB after their participation in an international public sector workshop supported by the World Bank. The initial purpose of implementing PBB was to gain efficiency and effectiveness in public budgeting. Although this effort was hindered by the Indonesian economic crisis in 1997, it resulted in several notable achievements, including the decision to implement PBB as a budgeting system in the mid-1990s, developing the *Sistem Akuntabilitas Kinerja Instansi Pemerintahan* (Government Agencies Performance Accountability System) in 1996, and implementing the *Laporan Akuntabilitas Kinerja Instansi Pemerintahan* (Government Agencies Performance Accountability Report) in 1999 (Ruswandi, 2005).

As previously noted, in return for supporting the Indonesian central government during the economic crisis, the World Bank and the IMF wanted financial management reform (including accounting, budgeting and auditing reform). This financial management reform officially occurred through the enactment of Law No. 17/2003 on State Finances (*UU No. 17 Tahun 2003 tentang Keuangan Negara*), which ordered PBB implementation within Indonesian government. However, this study found that PBB was implemented during the second period (2003) only to gain

legitimacy in the eyes of the international community; the Indonesian PBB retained the incremental and line-item approach (part of traditional budgeting) to improve usefulness and assist localised implementation. Thus, the Indonesian central government implemented PBB to fulfil their obligation to the IMF and the World Bank rather than as a sincere attempt to improve budgetary efficiency and transparency. Furthermore, although PBB was implemented in all ministries and agencies, the implementation of PBB within Indonesian central government is still in its early stages. Thus, it is not yet possible to categorically judge whether the implementation of PBB in Indonesia has been successful or unsuccessful.

Despite uncertainty about the overall result, this study found PBB implementation in the Indonesian central government had improved in the form of PBB undergoing implementation, the integration of budgeting and accounting processes via a chart of account standard formulation, strengthening of performance measurement through greater data availability and reliability, the integration of planning, budgeting and accounting, and the harmonisation of PBB implementation with other financial management reforms (e.g. accrual accounting and MTEF implementation).

### ***5.2.3 The Implementation of Performance-Based Budgeting within Indonesian Local Government***

At the local government level, budgeting reform commenced with the enactment of Government Regulation (GR) no. 105/2000 on Local Government Financial Management and Accountability (*Peraturan Pemerintah (PP) No. 105 Tahun 2000 tentang Pengelolaan dan Pertanggungjawaban Keuangan Daerah*), which instructed all local governments (provincial and city/district) to implement PBB. This official mandate was issued by the Indonesian central government through the Ministry of Home Affairs (MoHA) (*Kementerian Dalam Negeri*) as the supervisor and coordinator of Indonesian local government.

The motive that initially underpinned PBB implementation within Indonesian local government was the desire to conform to the international doctrine that it is in the

public sector's interest to modernise government. The PBB system was generally accepted as a means of modernising government, which was clearly the motivation behind the decision to implement PBB by government officers and academics whom had experienced NPM training overseas. The economic crisis of 1997 was a second stimulus for the implementation of PBB within Indonesian local government. Implementation was initiated by the Indonesian central government through MoHA, which, together with the Ministry of Finance (MoF) and other government agencies (*Badan Pengawas Keuangan dan Pembangunan* (Financial Development and Supervisory Agency) and *Lembaga Administrasi Negara* (State Administration Office), was an 'internal reform driver'. There was further support from 'external reform drivers' including donor projects, academics, the *Ikatan Akuntan Indonesia* (Indonesian Institute of Accountants) and consultants.

During the implementation of PBB within Indonesian local government, efforts were made to harmonise planning, budgeting and accounting. However, problems hindering PBB implementation included (1) utilisation of a line-item and incremental approach during the first implementation phase [a legacy of traditional budgeting that results in budget inefficiency and ineffectiveness], (2) conflicting regulations relating to local financial management, and (3) weak performance measurement within the budgeting reform process, which resulted in PBB implementation being partly cosmetic.

### **5.3 Reflections on Lüder's Financial Management Reform Process Model**

The author views the Lüder FMR model (2002; 2013) as a valuable conceptual framework for understanding how countries adopted PBB as their budgeting system. The Lüder FMR model is a basic contingency model that enables identification and analysis of the relevant contextual factors and key players in the evolution of PBB from an historical perspective, as part of public financial management reform, across multiple countries. The Lüder FMR model has been used within public sector research, specifically the Comparative International

Governmental Accounting Research (CIGAR) network, to understand the transition from traditional governmental accounting to a more informative accounting system (Lüder, 2002). A refinement of the Lüder contingency model, the Lüder FMR model is designed to aid in the assessment of the conduciveness of environmental factors to the implementation of governmental accounting reform.

Although previous research has used the Lüder FMR model primarily within the context of accounting reform, paper 1 (chapter 2) utilised the model (2002 version) as a conceptual framework for understanding budgetary reform, the history of PBB implementation, and whether similar factors influenced early PBB development in various countries. The literature review in paper 1 revealed that legislative support, executive action, and public sector community support are important for successful PBB implementation. Thus, the environmental factors within the Lüder FMR model (2002) previously demonstrated within an accounting reform context, are applicable within a budgeting reform context. However, using the Lüder FMR model in examining accounting reform across countries within an historical research method, lacked an in-depth analysis, as it required more chronologically detailed data to examine deeper levels of analysis relating to events across countries within an historical context. Alternatively, the Lüder FMR model (2002) can be applied across countries using comparative research without an historical overview, or only applied in single country analysis with an historical overview.

The Lüder FMR model is a conceptual as well as a contextual framework, and like any model will always be 'skeletal'; the model required empirical detail to make it meaningful (Laughlin, 1995). Hence, paper 3 (chapter 4) used the Lüder FMR model (2013) as a conceptual framework for generating an empirical understanding of Indonesian local government budgetary reform (PBB implementation) as a single country study. The Lüder FMR model (2013) acts as a conceptual framework by which to contribute to the knowledge of budgeting reform modelling within Indonesia as an economy in transition, and the broader accounting field.

The Lüder FMR model, both 2002 and 2013 versions, could be used in investigating similar or other types of public sector management reform in other developing countries, or in exploring performance measurement systems and public sector auditing processes.

#### **5.4 Reflections on New Institutional Sociology Theory**

This study used the NIS perspectives developed by Meyer and Rowan (1977) and DiMaggio and Powell (1983) relating to the institutional pressure and isomorphism, and the organisation's strategic response to institutional pressure developed by Oliver (1991), to examine budgetary reform in Indonesia. Specifically, this study sought to address the occurrence of institutional pressure and organisational responses to this pressure with respect to the implementation of PBB within the Indonesian central government.

From NIS perspectives, it appears that a moderate degree of coercive pressure from international organisations (the IMF and the World Bank) occurred within Indonesian central government budgetary reform, particularly with respect to the institutionalisation of PBB. This study also confirmed that the Indonesian central government response was one of avoidance and concealment in order for the Indonesian central government to conform to international pressure to change its budgeting system. This avoidance and concealment response, coupled with the occurrence of weak mimetic and strong normative (from Indonesian technocrats) pressure in the institutionalisation of PBB, is evident in the modified form of PBB now used across the Indonesian central government. This modified form of PBB reveals the strong influence from technocrats that were forced to adapt PBB based on their necessity, whilst covering-up essential PBB concepts using an artificial appearance in order to gain the necessary legitimacy that was fundamental to satisfy providers.



The Indonesian PBB form retained the incremental and line-item approach to improve usefulness and assist localised implementation. Thus, the Indonesian central government had only a weak rational motive to achieve efficient and effective budgeting through PBB implementation, as the line-item and incremental approach contributes to inefficiency and ineffectiveness. It appears that the Indonesian central government implemented PBB only to comply with the Letter of Intent it had agreed with the IMF and the World Bank.

In this study, NIS facilitated a clear examination of how and why the Indonesian central government initiated the implementation of PBB as their budgetary system, and how the Indonesian central government responded to institutional pressure. NIS was also able to reveal the historical context and therefore the motives and the factors behind the implementation of PBB in the Indonesian central government, and underpinned an evaluation of the institutional processes of the Indonesian central government's budgetary reform.

Future studies could utilise NIS to examine other types of public sector management reform, such as performance measurement system implementation or public sector auditing, or as part of case studies of other developing countries.

## **5.5 Implications of the Study**

Budgetary reform is typically a long process, involving several stages; key actors and stakeholders have varying and often clashing requirements. Thus, depending on the gap between the outcome of the reform and the reform concept, a response to bring back to the initial process may be needed to encourage a subsequent reform loop by considering the reform concept (Lüder, 2002). Successive reform processes might be needed to implement PBB to fully fit the requirements of the Indonesian public sector community.

Robinson (2007) argued that the model of PBB employed in industrial/developed countries cannot be transposed blindly into developing countries, due to the characteristics and constraints of the receptor countries (e.g. public servant demographics, low wages, nepotism) and the low level of sanctions. This implies that the PBB model should be adapted prior to implementation and that conditions supporting a favourable PBB implementation should already be in place.

Problems from the first phase of PBB implementation in Indonesia included (1) insufficient information and poor stakeholder awareness about PBB, (2) lack of sufficiently trained staff who understood the PBB model and how it is to be implemented, and (3) limitations within various information systems. To implement PBB successfully, performance information systems, performance indicator formulation, management accounting systems, and analytical and evaluation tools should be in place (Robinson, 2002). Moreover, to avoid the problems that arose in Indonesian PBB implementation and take full advantage of PBB, complementary reforms (such as accounting, auditing and political reform) are necessary (Ho, 2011; Melkers and Willoughby, 2001).

PBB implementation in Indonesia is still in its early stages; implementation to date has been partly cosmetic, as several traditional budgeting approaches (such as the line-item and incremental approach) are still used within PBB. Given the finding of strong coercive pressure from regulation in Indonesia, the Indonesian government needs to provide improved regulations and guidelines to support PBB implementation, such as totally removing the line-item and incremental approach; strengthening performance measurement through data availability and reliability; integration of planning, budgeting and accounting to improve the validity and reliability of performance measurement; and the harmonisation of PBB implementation with other financial management reforms (e.g. accrual accounting and MTEF implementation). Furthermore, systems that regulate the corresponding reforms (political, planning, accounting, budgeting and accountability) should be coordinated to prevent confusion among government staff. Particularly in local

government PBB implementation, the Indonesian MoHA must provide clear definitions of segregation of direct and indirect expenditure using an accounting approach, providing both examples of performance measurement across local government departments, and guidelines for recording or producing valid performance measurement data in each local government authority.

## **5.6 Recommendations**

In addition to the implications of the study described above, several specific recommendations are presented. These recommendations are for the consideration and benefit of international organisations, donors, the Indonesian government and other key stakeholders in public sector reform processes.

- The institutionalisation of new budgeting systems should consider the interests of both donor (external) and recipient (internal) organisations, to ensure the institutionalisation process is accepted from both sides.
- International organisations and developed countries' donor programs should recognise the possibility that recipient countries will perform 'window dressing' rather than ensuring that budgeting reform is delivered as promised.
- The institutionalisation of new budgeting systems should be driven by recipient countries rather than donors to ensure effective localised embedding of accountability, rather than it being resisted due to it being seen as imposed externally.
- PBB implementation cannot 'stand-alone'; it should be integrated with other public sector reforms, such as in planning, accounting, auditing, and performance measurement systems.
- The Indonesian central and local governments' officers need more technical training to be able to implement PBB effectively.

## **5.7 Limitations**

This thesis outlines a detailed analysis of the evolution and implementation of PBB globally, and in particular within the Indonesian government (both central and local). It presents several milestones in PBB implementation in addressing the traditional budgeting limitation previously mentioned in chapter one (introduction) and each paper.

This study has several limitations. First of all, given that this paper did not gather primary data, this chapter may have limitations regarding the inappropriateness of the data. This may have occurred as this chapter has relied on other literature in interpreting the results (Denscombe, 2007). Furthermore, the voices of respondents are critical to this research, as they play a central role in the adoption of PBB and its implementation within Indonesian government. However, only 15 respondents were interviewed, so caution must be exercised in generalising the results to the wider public sector within Indonesia and other countries.

## **5.8 Directions for Future Research**

Some of the implications and limitations identified earlier, indicate that this study has not embraced all facets and affiliations that exist in practice. Thus, there are several interesting implications for future research that remain for further study.

First of all, there is a requirement for the use of the Lüder FMR model within a single country examination for a detailed study on how reform takes place, with the ability to draw upon more context-specific data and the rationale behind actions, through interviews with key stakeholders in the reform process. It would be worthwhile to better elaborate and capture all aspects of the demand for and supply of PBB implementation in specific countries, along with other issues that facilitate or inhibit implementation, such as good governance and corruption.

Second, future research could elaborate and conduct additional data collection through participatory observations along with more in-depth interviews to capture more nuances on the Indonesian budgetary reform process, which should provide more information and insights regarding the motivations and interests underpinning PBB implementation in Indonesia.

Finally, future studies may elaborate and examine the demand and supply factors that stimulate budgeting reform using PBB as a new system. The requirement for PBB emerged from a demand for performance information on budgeting. However, there is a lack of supply of valid and qualified data for PBB. Therefore future studies could explore the extent to which the demand for performance information is matched by the organisations ability to supply it, and the role of key actors and stakeholders in this demand and supply.

## **5.9 Overall Conclusion**

This thesis describes and examines the motives behind the adoption and implementation of PBB within government. It focuses particularly on PBB implementation in the Indonesian central and local government, as a developing country case study.

Achieving successful implementation of PBB, particularly within the Indonesian government (both of central and local), depends on more than strong stimuli. Changes in key-actor behaviour to reform the Indonesian budgeting system is a more important factor, as there is strong normative isomorphism in the influence of PBB adoption and implementation based on evidence regarding the behaviour of Indonesian technocrats' (as the internal and external reform drivers). Sound institutional arrangements, such as a transparent political and administrative culture, create an important pillar for reform, as well as the harmonisation of PBB adoption with corresponding reforms in planning, accounting, auditing, and performance measurement systems. Thus, in practical terms, the Indonesian

experience of PBB implementation has lessons for other developing countries who are adopting, or intend to adopt and implement PBB.

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### Appendix 1: Table of Application of the Lüder model (FMR and LCM)

Authors	Country	Level of government	Model applied
Lüder, 1992	Canada, Denmark, Sweden, USA, Germany, France, European Community & UK,	Central, federal, state & local	LCM
Lüder, 1994	Italy, Japan & Spain	Central	LCM
Chan, 1994	United States	Federal	LCM
Mader & Schedler, 1994	Switzerland	Federal	LCM
Pallot, 1995	New Zealand	Central	LCM
Godfrey et al, 1995	Kenya, Tanzania and Uganda	Central and local	LCM variant
Montesinos & Vela, 1996	Germany, UK, France & Spain	Local	LCM
Budaus & Buchholtz, 1996	UK, Netherlands, Finland, Germany, USA & New Zealand	Local	LCM
Khumawala, 1997	India	Federal	LCM
Yamamoto, 1999	Japan	Local	LCM
Julve, 2000	Spain	Auditing in local Authorities	LCM variant
Christensen, 2002	Australia	New South Wales state	LCM variant
Jorge, 2003	Portugal	Local	FMR
Abushamsieh et al, 2013	Palestine	Central	FMR
Abushamsieh et al, 2013	Qatar	Central	FMR
Jones et al, 2013	France, Germany, UK and USA	Central	FMR variant
Bruno, 2014	Italy	Local	FMR variant



## Appendix 2: Coding for the Transformation of Budgetary Reform in the Indonesian Central Government

### The institutional pressure in the Indonesian central government budgeting reform

ISOMORPHISM IN PBB IMPLEMENTATION IN THE CENTRAL GOVERNMENT			
THEME	1 <sup>st</sup> Level Coding	2 <sup>nd</sup> Level Coding	3 <sup>rd</sup> Level Coding
Coercive	World Organisation (IMF, World Bank)	- Direct Influence	- Decision to implement PBB - Process of implementation
		- Indirect Influence	- Decision to implement PBB - Process of implementation
	Developed countries' donor organisations (USAID, CIDA, GTZ, etc.)	- No Influence	- Decision to implement PBB - Process of implementation
	Indonesian Regulations (Laws, Government Regulations, Minister decrees)	- Direct Influence	- Decision to implement PBB - Process of implementation
Mimetic	Developed Countries	- Part of model	
		- Modification	
Normative	Governmental accounting standard committee	- No Influence	- Process of implementation
		- Weak Influence	- Process of implementation
	Consultant organisation	- Weak Influence	- Process of implementation
	Indonesian Accounting Institute	- Weak Influence	- Process of implementation
	Indonesian technocrats	- Strong Influence	- Decision to implement PBB - Process of implementation

**The history and nature of PBB, and its implementation in the Indonesian central government.**

THE INDONESIAN CENTRAL GOVERNMENT FINANCIAL REFORM	
THEME	1 <sup>st</sup> Level Coding
History of Budgetary reform in Indonesia	The influence of the New Public Management (NPM) Concept
	Budgetary reform in 2003
	Types of prior budgeting system types
	Relationship of PBB implementation and other financial reforms
	PBB model changes, 2003–2010
Value of PBB	Problem of implementation
	Challenges and solutions of implementation
Characteristic of PBB	Technical examples of PBB superiority over other budgeting models
	Presentational performance budgeting
PBB Implementation	Reason for the PBB implementation
	Problems, challenges and solutions of PBB implementation
	Benefit of the implementation

## Appendix 3: Example of Central Government Budget Plan Using PBB

### BUDGET AND WORK PLAN OF DEPARTMENT FOR YEAR 2006 DETAIL ACTIVITY AND OUTPUT

MINISTRY/AGENCY : HEALTH  
 ORGANISATION UNIT : DIRECTORATE GENERAL OF MOTHER AND CHILD  
 DEPARTMENT : MATERNALITY  
 LOCATION : JAKARTA  
 SUB FUNCTION : HEALTH  
 PROGRAM : Handling of High-Risk Pregnancy  
 OUTCOME : Decreasing maternal mortality rate to 2/1000

Form 1.1

CODE	ACTIVITY AND OUTPUT	OUTPUT UNIT	OUTPUT TARGET			LOCATION	PIC
			2007	2008	2009		
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1	Monitoring of High-Risk Pregnancy					East Indonesia	XXXXXXX
	Indicator:						
	1. High-Risk Pregnancy monitored	1,5 million mother w/pregnancy	1,6 million mother w/pregnancy	1,7 million mother w/pregnancy	1,8 million mother w/pregnancy		
	2. Medical tools sufficient	500 public health centre	550 public health centre	600 public health centre	650 public health centre		
2	Socialisation of High-Risk Pregnancy						
	Indicator:						
	1. High-Risk Pregnancy socialised	1,5 million mother w/pregnancy	1,6 million mother w/pregnancy	1,7 million mother w/pregnancy	1,8 million mother w/pregnancy		
	2. Medical staff for socialisation	500 staffs	550 staffs	600 staffs	650 staffs		

An example of Ministry of Health's activity budget proposal  
based on GR No. 21/2004

#### Appendix 4: Central Government Expenditure Classification (Line-item)

CODE	EXPENDITURE CLASSIFICATION
	EXPENDITURE FOR CENTRAL GOVERNMENT
<b>51</b>	<b>Personnel Expenditure</b>
<b>51 1</b>	<b>Salaries and Allowance</b>
<b>51 2</b>	<b>Honorarium and overtime</b>
<b>51 3</b>	<b>Social contribution</b>
<b>51 3 1</b>	Pension
<b>51 3 2</b>	Health Insurance
<b>52</b>	<b>Goods Expenditure</b>
<b>52 1</b>	Goods and Services
<b>52 2</b>	Maintenance
<b>52 3</b>	Travel
<b>53</b>	<b>Capital Expenditure</b>
<b>53 1</b>	Land
<b>53 2</b>	Machine and Equipment
<b>53 3</b>	Building
<b>53 4</b>	Network
<b>53 9</b>	Other Physical Asset
<b>54</b>	<b>Interest Expenses</b>
<b>54 1</b>	<b>Domestic Debt</b>
<b>54 1 1</b>	Government
<b>54 1 2</b>	Bank Indonesia
<b>54 1 3</b>	Other
<b>54 2</b>	<b>Foreign Debt</b>
<b>54 2 1</b>	Government
<b>54 2 2</b>	Other
<b>55</b>	<b>Subsidiary</b>
<b>55 1</b>	<b>Government Company</b>
<b>55 1 1</b>	Financial Agency

CODE	EXPENDITURE CLASSIFICATION
	<b>EXPENDITURE FOR CENTRAL GOVERNMENT</b>
<b>55 1 2</b>	Non Financial Agency
<b>55 2</b>	<b>Private Company</b>
<b>55 2 1</b>	Financial Agency
<b>55 2 2</b>	Non Financial Agency
<b>56</b>	<b>Social Grant</b>
<b>56 1</b>	Social Compensation Fund
<b>56 2</b>	Religious and Education Agency
<b>57</b>	<b>Grant</b>
<b>57 1</b>	Foreign Country
<b>57 2</b>	International Organisation
<b>58</b>	<b>Other Expenses</b>
	<b>TRANSFER</b>
<b>61 1</b>	<b>Revenue Sharing</b>
<b>61 1 1</b>	Taxation
<b>61 1 2</b>	Natural Resources
<b>61 2</b>	<b>General Fund</b>
<b>61 2 1</b>	Province
<b>61 2 2</b>	City/District
<b>61 3</b>	<b>Special Fund</b>
<b>61 3 1</b>	Reforestation fund
<b>61 3 2</b>	Non Reforestation fund
<b>62</b>	<b>Specific Autonomy Fund dan Adjusment</b>
<b>62 1</b>	<b>Specific Autonomy Fund</b>
<b>62 1 1</b>	Papua
<b>62 2</b>	<b>Adjusment</b>
<b>62 2 1</b>	Pure Adjusment
<b>62 2 2</b>	Ad-hoc

An example of Expenses Classification (line-item based)

Based on GR No. 21/2004

## Appendix 5: Example of Local Government Budget Plan Using PBB

<b>BUDGET PLAN DEPT OF EDUCATION</b>		Form <b>RASK 3.1.1</b>	
District XXXX Budget Year 2004			
Gov. authorities : Education			
Activity : Information Technology Training for Teacher			
Location : Sub district xxxx			
<b>Performance Measurement</b>			
<b>Indicator</b>	<b>Performance</b>	<b>Target</b>	
Input	Money, the number of participants	Rp. Xxxx, 40 ppl	
Output	the number of teachers trained	35 ppl	
Outcome	Percentage of teachers trained	87 %	
Benefit	Increasing skills of teachers	40%	
Impact	Increasing teaching class process	30 %	
<b>Detail Budget on Activity</b>			
<b>Acc. Number</b>	<b>Name of Account</b>	<b>Amount (Rp)</b>	
<b>1</b>	<b>2</b>	<b>3</b>	
2 2 1 01 01	Honorarium of activity	<b>Rp. xxxxx</b>	
2 2 2 03 02	Supplies	<b>Rp. xxxxx</b>	
2 2 2 04 01	Food and beverages	<b>Rp. xxxxx</b>	
2 2 2 04 01	Maintenance	<b>Rp. Xxxxx</b>	
<b>Jumlah</b>		<b>Rp. xxxxx</b>	
xxxxxxxx,31 December 2003  Department of Education Leader  (Signature)  (Full Name) Employee Number.			

An example of department of education's activity budget proposal based on  
MoHA decree No. 29/2002

## Appendix 6: Example of Budget Classification Using PBB

<b>PROVINCE/CITY/DISTRICT XXXXX</b> <b>BUDGET PROPOSAL</b> <b>2004</b>		
<b>1. REVENUE</b>		
1.1. Local Revenue		Rp.xxxxxxxxxx
1.2. Transfer Funds		<b>Rp.xxxxxxxxxx</b>
1.3. Other Revenue		Rp.xxxxxxxxxx
<b>Total Revenue.....</b>		<u><b>Rp.xxxxxxxxxx</b></u>
<b>2. EXPENDITURE</b>		
2.1. Local government Official .....	Rp.	xxxxxxxxxxxxxx
2.1.1. General administration Funds	Rp.	xxxxxxxxxxxxxx
2.1.2. Maintenance and operation	Rp.	xxxxxxxxxxxxxx
2.1.3. Capital expenditure	Rp.	xxxxxxxxxxxxxx
<b>2.2. Public Expenditure.....</b>	<u><b>Rp.</b></u>	<u>xxxxxxxxxxxxxx</u>
2.2.1. General administration Funds	Rp.	xxxxxxxxxxxxxx
2.2.2. Maintenance and operation	Rp.	xxxxxxxxxxxxxx
2.2.3. Capital expenditure	Rp.	xxxxxxxxxxxxxx
<b>Total Expenditure.....</b>		<u><b>(Rp.xxxxxxxxxx)</b></u>
<b>Surplus/(Defisit).....</b>		<b>Rp.xxxxxxxxxx</b>
<b>3. FINANCING :</b>		
3.1. Receipt of Financing .....	Rp.	xxxxxxxxxxxxxx
3.2. Disbursement of Financing .....	<u>Rp.</u>	<u>xxxxxxxxxxxxxx</u>
<b>Amount of Financing.....</b>		<b>Rp.xxxxxxxxxx</b>

Local Government Budget Classification  
(Translated from MoHA decree No. 29/2002)

## Appendix 7: Example of Local Government Budget Plan Using PBB

<b>BUDGET PLAN DEPT EDUCATION</b>					Form <b>RKA-SKPD 2.2.1</b>	
District XXXX Budget Year 2007						
Gov. authorities : 1. 01. Education						
Organisation : 1. 01. 01. Education Department						
Program : 1. 01. 01. 16. Basic education						
Activity : 1. 01. 01. 16. 57. Training for teachers						
Location : Sub District xxxx						
Budget year n-1 : Rp xxxxxx						
Budget year n : Rp xxxxxx						
Budget year n+1 : Rp xxxxxx						
<b>Performance Measurement</b>						
<b>Indicator</b>		<b>Performance</b>			<b>Target</b>	
Program Goal		Increasing the quality of education			30 %	
Input		Money, the number of participants			Rp. Xxxx, 40 ppl	
Output		the number of teachers trained			35 ppl	
Outcome		Percentage of teachers trained			87 %	
Activity group target : Teacher						
<b>Detail budget on Direct Expenditure</b> <b>Based on Program dan activity on Local Government Department</b>						
<b>Acc. Number</b>		<b>Name of Account</b>	<b>Detail calculation</b>			<b>Amount (Rp)</b>
			<b>volume</b>	<b>unit</b>	<b>Price/unit</b>	
<b>1</b>		<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6=(3 x 5)</b>
5	2	1 01 01	Honorarium of activity	2	4	Xxxx <b>xxxxxx</b>
5	2	2 03 02	Supplies	4	3	Xxxx <b>xxxxxx</b>
5	2	2 04 01	Food and beverages	2	4	Xxxx <b>xxxxxx</b>
5	2	2 04 01	Maintenance	1	2	Xxxx <b>xxxxxx</b>
<b>Jumlah</b>						<b>Rp. xxxxxxxx</b>
xxxxxx,31 December 2006  Department of Education Leader  (Signature)  (Full Name) Employee Number.						

An example of department of education's activity budget proposal based on  
MoHA decree No. 13/2006



## Appendix 8: Example of Budget Classification Using PBB

<b>PROVINCE/CITY/DISTRICT XXXXX</b> <b>BUDGET PROPOSAL</b> <b>2007</b>		
<b>1. REVENUE</b>		
1.1. Local Revenue		Rp. xxxxxxxxxxxx
1.2. Transfer Funds		Rp. xxxxxxxxxxxx
1.3. Other Revenue		Rp. xxxxxxxxxxxx
<b>Total Revenue</b> .....		<u>Rp. xxxxxxxxxxxx</u>
<b>2. EXPENDITURE</b>		
2.1. Indirect Expenditure	.....	Rp. xxxxxxxxxxxx
2.1.1. Personnel Expenditure		Rp. xxxxxxxxxxxx
2.1.2. Interest Expenditure		Rp. xxxxxxxxxxxx
2.1.3. Subsidies Expenditure		Rp. xxxxxxxxxxxx
2.1.4. Grant Expenditure		Rp. xxxxxxxxxxxx
2.1.5. Social Expenditure		Rp. xxxxxxxxxxxx
2.1.6. Transfer Expenditure		
2.2. Direct Expenditure	.....	<u>Rp. xxxxxxxxxxxx</u>
2.2.1. Personnel Expenditure		Rp. xxxxxxxxxxxx
2.2.2. Good and Service Expenditure		Rp. xxxxxxxxxxxx
2.2.3. Capital expenditure		Rp. xxxxxxxxxxxx
<b>Total Expenditure</b> .....		<u>(Rp. xxxxxxxxxxxx)</u>
<b>Surplus/(Defisit)</b> .....		<b>Rp. xxxxxxxxxxxx</b>
<b>3. FINANCING :</b>		
3.1. Receipt of Financing	.....	Rp. xxxxxxxxxxxx
3.2. Disbursement of Financing	.....	<u>Rp. xxxxxxxxxxxx</u>
<b>Amount of Financing</b> .....		<b>Rp. xxxxxxxxxxxx</b>

Local Government Budget Proposal  
 (Translated from MoHA decree No. 13/2006)

## **Appendix 9: The Interview Guide for Paper Two: Performance-Based Budgeting Implementation in the Indonesian Central Government**

### **PART A: COERCIVE ISOMORPHISM**

1. To what extent do you think international organizations, such as the IMF, the World Bank, or donor from other countries (USAID, AUSAID, JICA, GTZ, etc) directly influenced on the decision concerning PBB implementation? Please, could you give me examples?
2. To what extent do you think international organizations, such as the IMF, the World Bank, or donor from other countries (USAID, AUSAID, JICA, GTZ, etc) indirectly impact on the decision to implement PBB? Please could you give me examples?
3. How do you think international organizations, such as the IMF, the World Bank, or donor from other countries (USAID, AUSAID, JICA, GTZ, etc) directly contribute to the process of PBB implementation? Please could you give me examples?
4. How do you think international organizations, such as the IMF, the World Bank, or donor from other countries (USAID, AUSAID, JICA, GTZ, etc) indirectly contribute to the process of PBB implementation? Please could you give me examples?
5. In terms of how Indonesian regulations affect the decision of PBB implementation, how do you think they can impact directly and indirectly? Please could you give me examples?
6. In terms of how Indonesian regulations affect the process of PBB implementation, how do you think they can occur directly and indirectly? Please give me examples?

### **PART B: MIMETIC ISOMORPHISM**

1. In your opinion, to what extent does the PBB model applied and implemented in Indonesia imitate PBB models used in other countries'? Could you give me an example of a country(s) which has a model that was used by Indonesia? Were there any modifications made to the model used in other countries to support its application in the Indonesian context?
2. How did the process of mimicking occur? Was it the whole model or possibly only part of it?

## **PART C: NORMATIVE ISOMORPHISM**

1. In regards to the influence of professional bodies (Indonesian Accounting Standard Board, or Indonesian Governmental Accounting Standard Board ) on the decision of PBB implementation, how did it take place directly?
2. In regards to the influence of professional bodies (Indonesian Accounting Standard Board, or Indonesian Governmental Accounting Standard Board ) on the decision of PBB implementation, how did it take place indirectly?
3. In terms of the influence of professional bodies (Indonesian Accounting Standard Board, or Indonesian Governmental Accounting Standard Board ) on the process of PBB implementation, how did it take place directly?
4. In terms of the influence of professional bodies (Indonesian Accounting Standard Board, or Indonesian Governmental Accounting Standard Board ) on the process of PBB implementation, how did it take place indirectly?
5. To what extent did professional bodies directly influence the types of personnel responsible for handling PBB implementation in government organization in Indonesia?
6. To what extent did professional bodies indirectly influence the types of personnel responsible for handling PBB implementation in government organization in Indonesia?

## **PART D: BUDGETARY REFORM AND PBB IMPLEMENTATION**

1. Do you think the New Public Management (NPM) concept contributed to the political reform in 1998 which in turn influenced financial reform? If yes, how?
2. Could you tell me why did central governmental budgetary reform occur in Indonesia in 2003?
3. What type of budgeting system was implemented in Indonesia prior to the introduction and implementation of PBB? What would you say about its adequacy?
4. What factors triggered the implementation of PBB in in Indonesia?
5. What sort of benefits has the Indonesian government obtained from adopting a PBB model?
6. Could you give technical examples which exhibit the superiority of PBB over other models of budgeting in public sectors?
7. How would you describe the relationships between the implementation of PBB and that of other financial reforms?
8. What kinds of problems (for example, human, technical, educating people to use it, using consultants) did the government encounter when introducing PBB for the first time? What has been done to resolve the problems?

9. Based on OECD's term<sup>25</sup>, which type of PBB has been implemented in Indonesia?
10. In what way do you think that the adoption of PBB contributes to the overall Indonesian public sector reforms?
11. How do you think that the adoption of PBB was intended to create value for money (efficiency, effectiveness, and economic) in public finance management?
12. What sort of challenges or problems do you think that the implementation of PBB in Indonesia may have resulted in? What solutions did the government propose to overcome or deal with these challenges and problems?
13. Are there any changes to the PBB model that was implemented in Indonesia? Could you tell me why the changes were made?

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<sup>25</sup> Based on Organization for Economic Co-operation and Development (OECD)'s term, there are three models of PBB namely:

**Presentational performance budgeting** is that performance measures are presented in budgeting documents or other government documents. In this category performance information is included, at best, as background information only. It does not play a role in decision making on allocations nor is it necessarily intended to do so.

**Performance-informed budgeting** is a form of budgeting that relates fund allocation to measurable results in the form of outputs and/or outcomes. Resources are related to results in an indirect manner. Indirect linkage implies that results –along with other information – are being actively and systematically used to inform budget decisions. Performance information is very important in the decision-making process but it does not necessarily determine the amount of resources allocated.

**Direct-performance budgeting** involves allocation of resources based on the results achieved implying that, PBB is directly applied and the performance result has clear link with outcomes.

## **Appendix 10: The Interview Guide for Paper Three: The Implementation of Performance-Based Budgeting within Indonesian Local Government**

### **Part A: Stimuli**

1. Could you tell me why local governmental (provinces and cities/districts) budgetary reform took place in Indonesia in 1999?
2. To what extent do you think the financial crisis, which occurred in Indonesia in 1997 stimulated the decision made by the members of government and parliament concerning PBB implementation within local governments? How would this have occurred?
3. To what extent do you think financial scandals in Indonesia stimulated the decision made by the members of government and parliament in implementing PBB within local governments? How would this have occurred?
4. In what way do you think the world organizations (IMF, World Bank, OECD, UN) stimulated the decision made by the members of government and parliament concerning PBB implementation within local governments? How would this have occurred?
5. In what way do you think developed countries (USA, UK, Australia, New Zealand, etc) stimulated the decision taken by the members of government and parliament concerning PBB implementation within local governments? How would this have occurred?

### **Part B: Reform Driver**

1. Which recognized institutions (government commission, standard setting bodies, audit associations and consulting firms) do you think influenced the decision of members of government and parliament concerning PBB implementation in local governments? How do you think they influenced this process, directly and indirectly? Could you please give me examples?
2. Which professionals (professional associations and scholar network) do you think influenced the decision of members of government and parliament concerning PBB implementation in local governments? How do you think they influenced this process, directly and indirectly? Could you please give me examples?

### **Part C: Political Reform Promoters**

1. In your opinion, to what extent did members of Indonesian government (president or ministers or governor, or mayor or head of district) or members of Indonesian parliament or local parliament play their role in the design of

budgetary reform in Indonesian local governments? Could you please give me examples how they play their role?

2. In your opinion, to what extent did members of Indonesian government (president or ministers or governor, or mayor or head of district) or members of Indonesian parliament or local parliament play their role in the implementation of PBB in Indonesian local governments? Could you please give me examples how they play their role?

**Part D: Institutional Arrangement**

1. In regards to the Indonesian legal system which is derived from Dutch tradition (Continental legal system tradition), how did it influence the design and strategy of PBB implementation in local governments?
2. To the extent that the Indonesian state structure is unitary state, how did it influence the design and strategy of PBB implementation in local governments?
3. In term of the Indonesian administrative structure, which is decentralized and fragmented in financial functions, how did it influence the design and strategy of PBB implementation in local governments?
4. Concerning to the qualification of Indonesian civil services in terms of PBB implementation in Indonesian local government; how did the qualification of Indonesian civil services influence the PBB implementation in local governments?
5. In your opinion, to what extent did the social cultures in the Indonesian government influence the design and strategy of PBB implementation in Indonesian local governments? Please, could you give me an example?
6. In your opinion, to what extent did the administrative cultures in the Indonesian government influence the design and strategy of PBB implementation in Indonesian local governments? Please, could you give me an example?
7. In your opinion, to what extent did the political cultures in the Indonesian government influence the design and strategy of PBB implementation in Indonesian local governments? Please, could you give me an example?

**Part E: Stakeholders**

1. Could you identify which Indonesian government/local government stakeholders (for instance, citizen/local citizen, parliament, Non-Government Organizations (NGOs), educational ministry, local government educational department) may have influence to the design and strategy of PBB implementation in Indonesian local governments?
2. To what extent did Indonesian government/local government stakeholders (for instance, citizen/local citizen, parliament, Non-Government Organizations (NGOs), educational ministry, local government educational department) influence the design and strategy of PBB implementation in Indonesian local governments? Please, could you give me an example?

**Part F: Reform Concept**

1. In your opinion, how and to what extent was Indonesian government involved in designing the concept of PBB implementation in Indonesian local governments? Could you please give me examples?

**Part G: Implementation Strategy**

1. In your opinion, how did the PBB implementation process and strategy in the Indonesian local government take place? Was it just mainly authorized by the central government or did it involve participation from the local governments? Did it make use of the central guidance from the central government or partly discrete from local governments? Did the implementation process occur within pilot or parallel or phased model or others? Did it use one or multiple steps?

How long did the implementation take place? Was it implemented with or without systematic staff training?

#### **Part H: Outcome of the Reform**

1. What sort of challenges or problems do you think that the implementation of PBB in Indonesian local government may have resulted in? What solutions did the government propose to overcome or deal with these challenges and problems?
2. Do you know of any changes to the PBB model that was implemented in Indonesian local governments, taking the case study of the department of education from 1999 to 2010? Could you tell me why the changes were made?
3. How do you think the adoption of PBB in educational department was intended to create value for money (efficiency, effectiveness, and economic)?
4. Based on OECD's term<sup>26</sup>, which type of PBB has been implemented in Indonesian local governments? Please, could you give me brief illustration of PBB model and system in Indonesian local government?

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<sup>26</sup> Based on Organization for Economic Co-operation and Development (OECD)'s term, there are three models of PBB namely:

**Presentational performance budgeting** is that performance measures are presented in budgeting documents or other government documents. In this category performance, information is included, at best, as background information only. It does not play a role in decision making on allocations nor is it necessarily intended to do so.

**Performance-informed budgeting** is a form of budgeting that relates fund allocation to measurable results in the form of outputs and/or outcomes. Resources are related to results in an indirect manner. Indirect linkage implies that results –along with other information – are being actively and systematically used to inform budget decisions. Performance information is very important in the decision-making process but it does not necessarily determine the amount of resources allocated.

**Direct-performance budgeting** involves allocation of resources based on the results achieved implying that, PBB is directly applied and the performance result has clear link with outcomes.



## Appendix 11: An Approval Statement of the University Human Ethics Committee for Paper Two



**MACQUARIE**  
University

ANDY DWI BAYU BAWONO <andy-dwi-bayu.bawono@students.mq.edu.au>

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Approved - 5201300575

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Mrs Yanru Ouyang <yanru.ouyang@mq.edu.au>

Fri, Sep 6, 2013 at 1:34 PM

To: Dr Vicki Baard <vicki.baard@mq.edu.au>

Cc: Dr Elaine Evans <elaine.evans@mq.edu.au>, Mr Andy Dwi Bayu Bawono  
<andy-dwibayu.bawono@students.mq.edu.au>

Dear Dr Baard,

Re: 'The Transformation of the Indonesian Governmental Budgetary System.'

Reference No.: 5201300575

Thank you for your recent correspondence. Your response has addressed the issues raised by the Faculty of Business & Economics Human Research Ethics Sub Committee. Approval of the above application is granted, effective "6/09/2013". This email constitutes ethical approval only.

This research meets the requirements of the National Statement on Ethical Conduct in Human Research (2007). The National Statement is available at the following web site:

[http://www.nhmrc.gov.au/\\_files\\_nhmrc/publications/attachments/e72.pdf](http://www.nhmrc.gov.au/_files_nhmrc/publications/attachments/e72.pdf).

The following personnel are authorised to conduct this research:

Dr Elaine Evans

Dr Vicki Baard

Mr Andy Dwi Bayu Bawono

Please retain a copy of this email as this is your official notification of ethics approval.

Yours sincerely,

Kay-Wah Chan

Acting Chair, Faculty of Business and Economics Ethics Sub-Committee

## Appendix 12: An Approval Statement of the University Human Ethics Committee for Paper Three



**MACQUARIE**  
University

ANDY DWI BAYU BAWONO <andy-dwi-bayu.bawono@students.mq.edu.au>

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### Approved - 5201300689

23 messages

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Mrs Yanru Ouyang <yanru.ouyang@mq.edu.au>

Fri, Nov 1, 2013 at 1:40 PM

To: Dr Vicki Baard <vicki.baard@mq.edu.au>

Cc: Dr Elaine Evans <elaine.evans@mq.edu.au>, Mr Andy Dwi Bayu Bawono <andy-dwi-bayu.bawono@students.mq.edu.au>

Dear Dr Baard,

Re: 'The implementation of performance-based budgeting in the Indonesian local governments.'

Reference No.: 5201300689

Thank you for your recent correspondence. Your response has addressed the issues raised by the Faculty of Business & Economics Human Research Ethics Sub Committee. Approval of the above application is granted, effective "1/11/2013". This email constitutes ethical approval only.

This research meets the requirements of the National Statement on Ethical Conduct in Human Research (2007). The National Statement is available at the following web site:

[http://www.nhmrc.gov.au/\\_files\\_nhmrc/publications/attachments/e72.pdf](http://www.nhmrc.gov.au/_files_nhmrc/publications/attachments/e72.pdf).

The following personnel are authorised to conduct this research:

Dr Elaine Evans

Dr Vicki Baard

Mr Andy Dwi Bayu Bawono

Please retain a copy of this email as this is your official notification of ethics approval.

Yours sincerely,

Parmod Chand

Chair, Faculty of Business and Economics Ethics Sub-Committee

## Appendix 13: Participant Information and Consent Form (Paper 2)



Department of Accounting and Corporate Governance

Faculty of Business and Economics

MACQUARIE UNIVERSITY NSW 2109

Phone : **61-2-9850 9192**

Fax: **61-2-9850 8497**

Email: vicki.baard@mq.edu.au

Chief Investigator's / Supervisor's Name : Vicki Caron Baard

Chief Investigator's / Supervisor's Title : Doctor

### **Participant Information and Consent Form**

Name of Project: The Transformation of the Indonesian Governmental Budgetary System.

You are invited to participate in a study examining the Indonesian governmental budgetary system reform particularly the implementation of performance-based budgeting (PBB) in Indonesian Public Sector Management. There are three objectives of this study: 1) To understand the institutional process of governmental budgetary reform in a developing country with the Indonesian government as a case study; 2) To examine the historical events leading to PBB implementation in Indonesia. 3. To determine how PBB implementation actually occurred; and 4) To understand the extent to which New Public Management principles are reflected in the financial reform relating to PBB.

The study is being conducted by Andy Dwi Bayu Bawono (email andy-dwi-bayu.bawono@students.mq.edu.au; telephone +61 451417499) Department of Accounting and Corporate Governance, Faculty of Business and Economics, Macquarie University; as part of the requirements of a PhD Degree under the supervision of Doctor Vicki Caron Baard (email: vicki.baard@mq.edu.au; telephone: 61-2-9850 9192), and A/Prof. Elaine Evans (email: elaine.evans@mq.edu.au; telephone: 61-2-9850 6477), Department of Accounting and Corporate Governance, Faculty of Business and Economics, Macquarie University, Sydney, Australia.

If you decide to participate, you will be asked to be involved in an interview, which will last for about 60 – 90 minutes, to share your knowledge, experience and perceptions in relation to the themes of the project. The interview will be recorded using an audio recorder with your consent. You will be provided with an opportunity to read any transcriptions of your personal accounts to verify the accuracy of the content by email. To express appreciation to participants for participating in this research, each participant will receive a power bank.

Only the researcher and supervisors will have access to the data. The results of this research will contribute to the completion of a doctoral thesis. Research findings may also be made published in academic journals and possibly in a book format. In all of these instances, data will be presented in an aggregated format. Transcriptions, comments and quotations will not contain anything that may identify research participants. Any information or personal details gathered in the course of the study are confidential. No individual will be identified in any publication of the results. Acknowledgements made in any publications will be general in nature. A summary of the results of the data can be made available to you on request.

Your participation in this study is entirely voluntary. You are not obliged to participate and if you decide to participate, you are free to withdraw at any time without having to give a reason and without consequence.

If you would like clarification of any aspects of this study and ethical concerns, please do not hesitate to contact Fatchan Achyani, as the local contact of this research in Indonesia, at email: fatchan\_achyani@yahoo.com or telephone: +62 8122989040.

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I, ....., have read and understood the information above and any questions I have asked and have been answered to my satisfaction. I agree to participate in this research, knowing that I can withdraw from further participation in the research at any time without consequence. I have been given a copy of this form to keep.

Participant's Name: \_\_\_\_\_

(Block letters)

Participant's Signature: \_\_\_\_\_ Date: \_\_\_\_\_

Investigator's Name: \_\_\_\_\_

(Block letters)

Investigator's Signature: \_\_\_\_\_ Date: \_\_\_\_\_

The ethical aspects of this study have been approved by the Macquarie University Human Research Ethics Committee. If you have any complaints or reservations about any ethical aspect of your participation in this research, you may contact the Committee through the Director, Research Ethics (telephone (02) 9850 7854; email [ethics@mq.edu.au](mailto:ethics@mq.edu.au)). Any complaint you make will be treated in confidence and investigated, and you will be informed of the outcome.

**(INVESTIGATOR'S [OR PARTICIPANT'S] COPY)**

## Appendix 14: Participant Information and Consent Form (Paper 3)



Department of Accounting and Corporate Governance

Faculty of Business and Economics

MACQUARIE UNIVERSITY NSW 2109

Phone : **61-2-9850 9192**

Fax: **61-2-9850 8497**

Email: vicki.baard@mq.edu.au

Chief Investigator's / Supervisor's Name : Vicki Caron Baard

Chief Investigator's / Supervisor's Title : Doctor

### **Participant Information and Consent Form**

Name of Project: The Implementation of Performance-Based Budgeting in the Indonesian Local Governments.

You are invited to participate in a study examining the implementation of performance-based budgeting (PBB) in the Indonesian local governments within education departments as case study. There are three objectives of this study: 1) To understand the contingency factors (stimuli, institutional arrangement, reform drivers, political reform promoters, stakeholders, reform concept and implementation strategy) influencing the budgetary reform in the Indonesian local government as developing country case, specifically the education department in local governments; 2) To identify the historical factor influencing and/or stimulating PBB implementation in the Indonesian local governments; 3) To determine how PBB implementation in the educational department in the Indonesian local government actually occurred.

The study is being conducted by Andy Dwi Bayu Bawono (email andy-dwi-bayu.bawono@students.mq.edu.au; telephone +61 451417499) Department of Accounting and Corporate Governance, Faculty of Business and Economics, Macquarie University; as part of the requirements of a PhD Degree under the supervision of Doctor Vicki Caron Baard (email: vicki.baard@mq.edu.au; telephone: 61-2-9850 9192), and A/Prof. Elaine Evans (email: elaine.evans@mq.edu.au; telephone: 61-2-9850 6477), Department of Accounting and Corporate Governance, Faculty of Business and Economics, Macquarie University, Sydney, Australia.

If you decide to participate, you will be asked to be involved in an interview, which will last for about 60 – 90 minutes, to share your knowledge, experience and perceptions in relation to the themes of the project. The interview will be recorded using an audio recorder with your consent. You will be provided with an opportunity to read any transcriptions of your personal accounts to verify the accuracy of the content by email. To express appreciation to participants for participating in this research, each participant will receive a power bank.

Only the researcher and supervisors will have access to the raw data (the interview and recording). The final transcript interview will be de-identified prior to it being sent to professional translator. The professional translator entities will just access to the final transcript of interview in Bahasa Indonesia which will translate to English. The results of this research will contribute to the completion of a doctoral thesis. Research findings may also be made published in academic journals and possibly in a book format. In all of these instances, data will be presented in an aggregated format. Transcriptions, comments and quotations will not contain anything that may identify research participants. Data including hard copy and soft copy will be kept in a locked cabinet in the co-investigator's home and office (building E4B room 402), and also on the co-investigator's password-protected laptop. The audio recordings and correspondence will be retained for at least 5 years after which they will be destroyed in a secure manner. Any information or personal details gathered in the course of the study are confidential, except required by law. No individual will be identified in any publication of the results. Acknowledgements made in any publications will be general in nature. A summary of the results of the data can be made available to you on request.

Your participation in this study is entirely voluntary. You are not obliged to participate and if you decide to participate, you are free to withdraw at any time without having to give a reason and without consequence.

If you would like clarification of any aspects of this study and ethical concerns, please do not hesitate to contact Fatchan Achyani, as the local contact of this research in Indonesia, at email: fatchan\_achyani@yahoo.com or telephone: +62 8122989040.

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I, ....., have read and understood the information above and any questions I have asked and have been answered to my satisfaction. I agree to participate in this research, knowing that I can withdraw from further participation in the research at any time without consequence. I have been given a copy of this form to keep.

Participant's Name: \_\_\_\_\_

(Block letters)

Participant's Signature: \_\_\_\_\_ Date: \_\_\_\_\_

Investigator's Name: \_\_\_\_\_

(Block letters)

Investigator's Signature: \_\_\_\_\_ Date: \_\_\_\_\_

The ethical aspects of this study have been approved by the Macquarie University Human Research Ethics Committee. If you have any complaints or reservations about any ethical aspect of your participation in this research, you may contact the Committee through the Director, Research Ethics (telephone (02) 9850 7854; email [ethics@mq.edu.au](mailto:ethics@mq.edu.au)). Any complaint you make will be treated in confidence and investigated, and you will be informed of the outcome.

**(INVESTIGATOR'S [OR PARTICIPANT'S] COPY)**