Indonesian Management &
Accounting Research
Vol 8. No.1
January 2009
pp. 19 - 48

THE NPFM IN EMERGING ECONOMIES: THE MODIFIED BUDGETING SYSTEM (MBS) IN MALAYSIAN GOVERNMENT

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Abstract: This study examines the impact of the MBS on overall financial management in the Malaysian central government organisations. This study adopted cross sectional survey with two main stages of data collection - questionnaire and interview surveys. Providing evidence on the applicability of NPFM in developing countries, generally the respondents agreed that the MBS had improved financial management processes of their organisations by virtue of Expenditure Target, greater autonomy to operational managers and result based performance measures. However, structural weaknesses related to annuality and resistance to change by managers might undermine the reforms. Problems including shortfall of allocations and delays in receiving funds at responsibility centres should be addressed by the government. More importantly, this study provides evidence about the effectiveness of the NPFM mechanisms, which has its western origin, to civil service organisations in emerging economies.

Keywords: New Public Financial Management (NPFM), Modified Budgeting System (MBS), Evaluation, Emerging Economies, Financial Management.

1. Introduction

Following the trends of market led public sector modernisation undertaken by government worldwide particularly in developed nations to improve performance of government organisations, Treasury Circular No. 11 (1988) authorised the Malaysian central government organisations to implement a devolved budgetary reforms namely the Modified Budgeting System (MBS) in the early 1990s. Besides overcoming weaknesses of the government budgeting system at the time, the MBS was introduced with features of the New Public Financial Management (NPFM) undertaken in the developed nations such as greater participation of line managers in budgeting process and results based accountability. These changes would achieve flexible situations to improve service delivery in government organisations (Hood, 1995; Ferlie et al., 1996; Bogt, 1999; Hyndman and Eden, 2001). However, despite of these reforms undertaken in developing countries, there were very limited studies undertaken to understand the effectiveness of these initiatives.

In light of the call for evaluation of the public sector reforms particularly in developing countries (see, for examples, Lane, 1997; Pollitt and Bouckaert, 2000; and Boyne et al., 2003), this paper provides empirical evidence on the impact of the Modified Budgeting System (MBS) on achieving its objectives to improve financial management of Malaysian central government organisations. Specifically, this study investigates the impact of the MBS on changes in budget preparation and monitoring, budgetary authority of line managers, cost savings, linkage between input and output, and overall management of financial resources. Therefore, this paper is organised as follows. The next section provides a review of literature on devolved budgeting in general and the Modified Budgeting System in greater details. Following that is a discussion on the research methodology. Finally, results and analysis of the findings will be presented with the main implication of the study is drawn in a conclusion section.

2. Devolved Budgeting as the New Public Financial Management (NPFM)'s Tool

With the efforts to bring efficiency of private sector to government bodies, the New Public Financial Management (NPFM) was introduced with different packages such as cost improvement programmes, financial management information system, accountable management, greater role of accounting, result based performance measurement, and devolved budgets (Petterson, 1999). Groot (1999) argued that these measures should provide better chance for government to enhance efficiency and improving effectiveness of public service operations. Amongst these changes, devolved budgeting was introduced to permit faster and more flexible responses to changing conditions than the system by which all resources were allocated to government organisations centrally (Bourn and Ezzamel, 1987; Mayston, 1998, Torres and Pina, 2002). With devolved budgeting, public sector reform architects recognize the importance of civil service managers to actively involve in both financial and operational management of their organisations (Bogt and Helden (2000). With appropriate level of financial autonomy, they will be able to respond quickly to external developments (Ibid., p. 265). When line managers are responsible and accountable for planning and controlling public resources in light of value for money consideration, this will encourage the more efficient and effective use of resources (Boyle, 1991). Prior to this, financial management tended to be held mainly by accountants and line managers' main concerns were with outputs and not the relationships between outputs and inputs (Ibid., p. 11).

A meaningful performance assessment is only possible when the outcomes and results of a given resources and activities achieve their intended purposes. Understanding on relationships between outputs and inputs as reflected in efficiency and effectiveness indicators is important to measure performance. However, Boston (1993) argued that it is difficult to measure performance in the public sector because its outputs are immeasurable. For that reason, the introduction of NPFM to shift the focus of accountability from mainly input control to mainly results based performance criteria was seen as part of these on going attempts to better understand how government organisation actually perform.

Boyle (1991) outlined a few main strategies that central government could adopt to ensure a greater flexibility for civil service managers to manage their resources. These include increased in year flexibility to transfer allocation across heads of expenditures (virement), increased between year flexibility to carry over unspent allocation to the following year, and revenue and savings retention, in which a portion of revenues and savings made can be retained by the government organisations to offset the operating expenditures instead of returning them to the Treasury (Ibid., p. 15). Bogt and Helden (2000) assert that capacity to organise accounting systems according to management needs, empowerment to purchase certain good or services from any supplier through formal contract, and, to develop management's own plan to strengthen the planning and control cycles in the organisation are all important ingredients to improve organizational performance. In addition, Pendlebury and Karbhari (1995) argued that an increase in the number of responsibility centres and budget holders, as a consequence of devolved budgetary participation, should lead to improvement of management accounting systems to support the needs of devolved management in government organisations. Supported by Lapsley (1994) study, responsibility accounting has assumed an important role in devolved budgeting environment (i.e UK's Agencies and hospitals). On the impact of devolved budgeting on financial management of government organisations, relatively few studies can be found in the literature (see, for examples, Bogt, 1999; Bogt and Helden, 2000; Pendlebury and Karbhari, 1997).

However, these studies did not provide consistent results that greater financial freedom would lead to improved financial management of government organisations. In one hand, the study by Pendlebury and Karbhari (1997) found that the managers in the UK's Executive Agencies were more satisfied with the quality of management accounting information provided in their agencies as compared to before agencification process. As agencies to be managed separately from mainstream departmental activities and be separately accountable, this led to agencies developing their own financial and management accounting systems specifically designed to meet the needs of their managers. Regarding the central issue of the management accounting process (mainly budgetary preparation and control), Pendlbury and Karbhari (1997) found agencies with greater flexibility to manage their allocations (net running cost control regime) had made more progress in developing management accounting practices than their more strictly controlled gross running cost control counterparts. Also, agencies subjected to stricter control mechanisms and facing no competition were less likely to benefit from the decentralisation process in terms of improved management accounting processes. In short, the greater financial flexibility these organisations experienced led to greater improvement in the financial management.

In contrast, Bogt and Helden (2000) reported that decentralisation did not lead to changes in financial management as desired to support greater efficiency. While traditional input control (i.e financial budget) was still dominant, the organisations paid little attention to outputs. Controls were still mainly input-oriented, aimed at not exceeding the available budgets (Ibid., p. 265). They argued that the failures were attributed to the absence of financial stress, moderate pressure from politicians towards outputs, lack of commitment from top management towards the new changes, and a lack of necessary knowledge and skills among financial staff to accommodate the new financial instruments. Similarly, Groot(1999) found that budgetary reforms with output based accountability failed to cut down expenditure, and to improve effectiveness and efficiency of operation. As a result, in meeting the health care service demands, output-based budgeting was replaced by mainly input-based budgeting. Interestingly, Groot discovered that short-term measures to restrict investments and incremental budgeting were effective in curbing cost increases. In incremental budgeting, budget holders are given the same percentage annual increase in their level of funding, historical spending pattern will be maintained without any guarantee that resources are allocated according to needs (Mayston, 1998). In addition, Aidemark (2001) found that poor accounting information system and attitudes of major stakeholders (patients and employees) to maintain status quo undermining the impact of the responsibility accounting and internal market in promoting cost-effective awareness among medical staff.

3. The Modified Budgeting System (MBS) New Public Financial Management (NPFM) in Malaysian Central Government

The Modified Budgeting System (MBS) was a landmark of knowledge sharing between Malaysian government and the Australian treasury. It was officially introduced for the 1990 annual operating budget preparation with the issuance of Treasury Circular No. 11, 1988. The MBS was first introduced in three pilot Ministries: the Ministry of Health, Ministry of Work, and Ministry of Social Welfare (Malaysian Treasury, 1988). The MBS was implemented in all ministries and departments in 1992, also it was applied to statutory bodies in 1997 (Malaysian Treasury, 1996). The statutory bodies involved were those receiving operating budget from the Treasury.

The MBS reflected the Treasury concerns to improve the budget management of government organisations. Besides to counteract weakness in the implementation of Programme and Performance Budgeting System (PPBS), which had been in place since 1969, the MBS was also meant to introduce several NPFM mechanisms such as contract management, emphasis on results based performance measures, and financial freedom to line managers. The PPBS's major weaknesses included the focus on line items instead of results, no emphasis on performance measures, lack of top management participation in the budget process, limited financial autonomy for effective decision-making, the practice of gaming by spending organisations, the failure to use the system as a management tool to achieve value for money, and a distinct dichotomy between financial management and operating matters (Gnaneswari, 1993; Commonwealth, 1995).

Specifically, main principles and objectives of the MBS as laid down in the Treasury Circular (1988) are to improve and modernise the process of resource allocation on the basis of performance, to delegate greater authority over the management of resources to as low a level of management as practicable, and to introduce a result oriented and cost effective management. While maintaining the programme structure from the previous budgeting system, the MBS places special emphasis on spending limit by Expenditure Target (ET), delegating budget authority to operating managers via 'Let managers manage' policy, and output based performance accountability through Programme Agreement (Malaysian Treasury, 1988). The structure of the programme and activities should be designed in a manner in which inputs and output can be meaningfully related. It should also be expected that the MBS would enable the government organisations to restructure their programme and activities in a manner that performance of these activities could easily be assessed.

The expenditure target (ET) is a budget ceiling for an on-going programme. The Treasury arrives at the ET of an on-going programme by adjusting the previous year's allocation for "one offs" (extraordinary and non-recurrent expenditures

provided in the previous year), salary increment and inflation with an efficiency dividend of one per cent is to be deducted from all administrative expenses (except emoluments, grants and transfer payments). In addition, the management of government organisaitons are given the freedom to suggest allocation of the Expenditure Targets to programmes and activities they consider will achieve the best possible performance, as long as the allocation made is consistent with the priority of government policies (Malaysian Treasury, 1988). On top of ET, government organisations can apply for additional allocations for new policies, an extension of on-going programmes and one offs (hereinafter called new policies) under the new policy proposal stage. Furthermore, government organisations are encouraged to put up savings proposals. In the event savings proposals are made by operating agencies, a certain amount of savings can be retained by these operating agencies. However, if saving proposals are made by the Treasury, the agencies will lose all of the savings. Thus, the final allocation of an agency will be as follows:
Total Allocation = Expenditure Targets for existing policies + Allocation for approved new policies and one off events - Savings from approved policy.

If there are no new policies, the expenditure target then becomes the programme's allocation for the budget year. The use of ET may lead to incremental budgeting. Mismatch of needs and allocation in incremental budgeting may undermines efforts to achieve organisational goals. Additionally, the ET is similar to the Cash Limit regime implemented in the UK in 1974/75. The cash limit regime was introduced to discipline civil servants from overspending from the original estimates (Henly, 1989). Schick (2003) suggested that providing an expenditure ceiling to government budget will only be effective to curb overspending and opportunistic politicians to break rules when there is a right fit between budget projections and budgetary control.

The emphasis of the MBS manifested itself in it's the 'Let managers manage' policy. The MBS sought to encourage greater delegation of authority from the Treasury to government organisations and then on to line managers (Malaysian Treasury, 1988). The flexibility that goes with this policy is related to resource allocation, procurements and 'generalised approach' to budgetary control. With the MBS, the Treasury's function should have become that of a monitoring body over government organisations. Under the previous programme and performance budgeting systems, resource allocation responsibility was held either at a higher government level or at the Treasury. With greater control over reallocation, it was hoped managers would be motivated to manage programmes within the budgets allocated and to achieve their output targets (Bujang, 1996; Xavier, 1996). Greater autonomy on procurements relates to that budget holders and their representatives in government organisations are given higher limit of spending ceiling. The three methods of procurements are public tender, price quotations and direct purchases.

While public tender involves amount up to RM$50 million, managers can undertake purchases via price quotations and direct purchases for amount lower than RM$50 thousands (Malaysian Treasury, 2001). As the Treasury encourages this autonomy should be delegated to lowest possible level of management, this freedom will enable line managers at responsibility centres to obtain services from suppliers faster. In addition, the 'generalised approach' to spending control would also provide the civil servants with greater autonomy over virement. Unlike before, virements of the expenditures across heads of expenditures provided they did not expect to incur accumulated deficits by their actions.

Interestingly, the Treasury imposed stricter controls on additional allocation request as to ensure the effectiveness of ET and the potential benefits of the generalised expenditure control to curb over spending of the government organisations, (Malaysian Treasury, 1988). Additional funds from the treasury can only be obtained for expenditures that are specially allocated by any new legislation during the budget period. Failure to comply with these aggregate controls over expenditure exposed the civil servants concerned to disciplinary action. In short, additional allocation on the approved activities would defeat the purpose of tightening expenditure control that the government is trying to implement.

With delegation of budgetary autonomy to government organisations, the Treasury introduced the contract management mechanism to enhance the accountability of the civil service managers. Consistent with the NPM's emphasis of result based accountability, the Programme Agreement is a performance contract between government organisations' top management and the Treasury. Among the main components of the Programme Agreement are output and outcome performance targets. Output targets need to be provided for each programme and activity of the organisations covering quantity, quality, timeliness and unit costs (Malaysian Treasury, 2001). With these changes, activities of government agencies should be organised in a manner that input and output relationships should be enhanced thereby the evaluation of efficiency and effectiveness can be properly undertaken. Moreover, implementation of the MBS requires reviews on programmes and activities to be undertaken at least once in five years. This would ensure that government services remain relevant in serving their target group of customers. In addition, the review findings could be used to improve future resource planning which can be used by the Treasury (Budgetary Division), the Economic Planning Unit of Prime Minister Office (EPU), and the Public Service Commission for policymaking (Xavier, 2000).

However, Xavier (1996) rightly argues that one of the main weaknesses of the MBS is that it does not cover the whole of the budget process and the related institutional arrangements, but focuses only on operating budget processes. The development budget is another part of the budget process, which is operated and monitored by the Economic Planning Unit of the Prime Minister's Department (Malaysian Government, 2000). The reason for separating these two types of budget is tightly linked to the government's agenda for economic development (Esman, 1972).

4. Methodology

This study essentially attempts to investigate the overall impact of the Modified Budgeting System (MBS) on financial management processes in Malaysian Central Government organisations, thus respondents should support the following proposition:

The overall perceived impact of the MBS is positive in improving each of the following areas:

1. Cost Savings
2. The budgetary authority of line managers
3. The linkage between inputs and outputs
4. Budget Preparation
5. Virement
6. Monitoring of actual against budget
7. Budgetary allocation carry-forward
8. Overall management of financial resources

Therefore, the respondents were invited to indicate, on a scale ranging from 1 (significantly decreased), through 2 (decreased), 3 (no change), 4 (moderately increased) to 5 (significantly increased), their perceptions of the level to which changes in the issues listed in the proposition were due to the MBS. These questions are considered relevant based on the objectives for which the MBS was implemented to overcome the weaknesses of the previous budgeting practice and to introduce the NPFM with its freedom to manage. Questions related to the impact of the MBS on autonomy over personnel matters and salary were also asked due to the fact that the substantial amount of operating budget relates to remunerations of civil servants, thus greater flexibility in recruitment, salary and training will have significant influence on the way the budget is managed. Consistent with the suggestion of Bogt (1999) in evaluating the effect of public reforms, an overall evaluation was considered appropriate because the MBS had been in place for more than 5 years by the time this study was conducted. Also, this study differs from the two previous studies on MBS in at least two ways. Bujang (1996) and Xavier (1996) studied the MBS in the pilot organisations, whereas this study covers all central government organisations. Secondly, while the two previous studies focused on the implementation process of the new budgeting system, this study examines the overall impact of the system on financial management. As the literature on the impact of the NPFM was mainly focusing on developed countries, thus, this study will extend further the literature on the relevance of the financial reform in the emerging economies.

Therefore, to achieve the objective of the study, perceptions of senior managers from the central government organisation were sought. Seeking senior managers' perceptions on organisational related performance was well established method in the literature (see, for example, Dess and Robinson, 1984; Pendlebury and Karbhari, 1997). This study adopted cross sectional survey with two main stages of data collection - questionnaire and interview surveys. The three central government organisations selected in this study are Ministries, Departments and Statutory Bodies. Since this study is assessing the effectiveness of the MBS to bring in desired changes, the organisations concerned must already exist before the reform was introduced early 1990s. Considering this, 131 organisations were selected for this study comprising of 24 Ministries, 72 Departments and 35 Statutory Bodies.

These three organisations differ in their characteristics in terms of governance and budget allocation. Whilst both Departments and Statutory Bodies are agencies under the Ministries, statutory bodies received greater managerial and financial autonomy by virtue of their status (Othman, 2001). While departments were exist under the British's administration of Malaya, statutory bodies were created by the second Prime Minister, Tun Abdul Razak to speed up implementation of his socio-economic development agenda (Esman, 1972). The statutory bodies are governed by a board of directors comprising of members from relevant ministries, the Treasury, and independent directors appointed from private sectors. For budget allocation, the Treasury distributes the budget to controlling officers of government organisations. As the ultimate budget holders, the controlling officer is the person directly accountable to Parliament (Malaysian Treasury, 2002). The Ministries and departments share controlling officers and receive budget allocation in the form of warrants, while statutory bodies have their members of boards as controlling officers and receive the allocations in the form of grant monies. Owing to their historical status, Departments are responsibility centres of the Ministries (Othman, 2001).

With traditionally limited financial and managerial autonomy faced by Ministries and Departments than the Statutory Bodies, it can be proposed that Ministries and Departments will experience more impact of the MBS on the above mentioned financial management related issues because its main principle of greater freedom to managers would be new to these organisations than the Treasury dependent Statutory Bodies. Nevertheless, during the course of the study, it came to our notice that some statutory bodies are financially independent. As their financial affairs are entirely governed by the board of directors, these organizations are not required to implement the MBS by the Treasury. These organizations were identified and thus excluded from the study.

A questionnaire was issued to the named Chief Secretary for each Ministry, Director General for each Department and Chief Executives or General Manager for each Statutory Body. Recognising the risk of low response rate in developing countries particularly in government organisations, the questionnaire was personally sent and collected by the researcher to and from the organisations. Malaysian central government organisations are mainly concentrated in Kuala Lumpur and a neighbouring city, Putrajaya, except for organisations in distant places such as in different states where questionnaires were mailed out. 94 responses were received resulting in a usable response rate of 72%. Of the 94 (72%) usable responses, 14 (58%) were from Ministries, 55(76%) were from Departments and 25 (71%) were from Statutory Bodies.

Pendlebury and Karbhari (1997) argued that the seniority of respondents would indicate the stronger level of confidence about civil servants' perceptions on the impact of public sector reforms. An analysis was undertaken of the status of employment of the individuals named as having completed the questionnaire and the results of this are reported in Table 1. The seniority of the respondents gives strong support of our belief that the responses provide an authoritative source of information on the issues raised. The respondents were also asked to state the period of employment as civil servants and the responses revealed that over 90% had more than 15 years civil service experience. The average length of the service was 23 years.

Table 1: Status of Respondents by category of employment

	Departments		Statutory Bodies		Ministries		Total	
	No.	%	No.	%	No.	%	No.	%
Director General/ Chief Executives/Secretary General	10	18	1	4	2	14	13	14
Deputy Director General	9	16	3	12	4	29	16	17
Admin & Finance Directors	22	40	8	32	7	50	37	39
Director Of Corporate/ Planning	6	11	4	16	1	7	10	11
Senior General Managers	8	15	9	-	-	-	18	.19
Total	55	100	25	100	14	100	94	100

Our responses are dominated by civil servants who had experience of the provision of government services before and after the reform programmes being implemented. This fulfilled the assumption that those that filled in the questionnaire were holding the adequate experience to assess the changes that took place as a result of the reforms. A series of interviews were also conducted after analysis of questionnaire survey responses. Two types of interviewees were selected: top management and line managers on account of their ability to provide information on the changes they had experienced as a result of the financial and managerial reforms. Of the 36 officers interviewed (17 were from Departments, 14 from Statutory Bodies and 5 from Ministries), almost all (97%) had 15 years experience or more as civil servants and their average length of service was about 24 years. Interviews were taped, manually coded and thematically analyzed across variables and within cases using data display matrices to compare and contrast patterns of responses (Boyatzis, 1998).

5. Result

5.1.The Impact of Modified Budgeting System (MBS) on Financial Management Processe

Table 2 shows the perceived impact of the MBS on all areas in the proposition. It reveals that the majority of respondents indicated moderate or significant increase to all related issues, except budgetary allocation carry-forward. The highest level of impact of the MBS achieved by organisations related to monitoring of actual spending against budget, with 92 % of respondents indicating a moderate or significant increase. The second highest score related to budget preparation, with 87 % of the respondents indicating a moderate or significant increase, whilst overall management of financial resources scored the third highest, with as many as 86 % of the respondents indicating a moderate or significant increase. This strongly suggests that the MBS has improved the integral elements of public sector financial management including budget preparation and budgetary control. Another interesting finding is the impact of the MBS on the linkage between input and output with 77% of the respondents indicated the improvement. Regarding issues related to devolved budgeting, the respondents indicated encouraging feedback. In particular, ninety-two per cent of the respondents indicated that the MBS had increased the budgetary authority of line managers, and 81% indicated that the MBS had increased the virement authority of their organisations. This tends to suggest the success of the 'Let managers manage' policy to delegate greater budgetary autonomy to government organisations, particularly line managers in the organisations. This is further supported with the responses relating to autonomy over salary and personnel matter with 50% of the respondents indicated greater autonomy over salaries, and 62% of them indicated a moderate or significant increase in autonomy over personnel matter. The Treasury has influence over personnel matters such as salary changes across the civil services and civil service expansions with new recruitment. However, Table 2 also displays that the reluctance of the Treasury to delegate authority over budgetary allocation carry-forward, with more than half (62%) of the respondents indicating that either there had been no change or there had been a decrease regarding this matter. Overall, the majority of respondents indicated that their organisations were able to take advantage of the MBS with regard to devolved budgeting and financial management. Still, a noticeable level of respondents indicated that their organisations had not benefited from the MBS. (see table 2 and 3) The analysis by organisational status is presented in Table 3. Although the analysis produced no significant differences, several noteworthy trends were revealed. The statistical analysis of responses by organisational status was conducted based on a full 5 point Likert scale ranging from 1 (significant decrease) to 5 (significant increase). For presentational purposes, the responses reported in Table 3 have been collapsed into the three categories of 'decrease' (which combines moderate and significant decreases), 'no change', and 'increase' (which combines moderate and significant increases).

As it does not reveal any significant differences between responses, these findings did not support our expectations. We hypothesised that the impact of the MBS would be felt more in Ministries and Departments particularly because Statutory Bodies were assumed to have greater financial and managerial autonomy even before the MBS. Non significant differences of responses from these three organisations seem to suggest that when statutory bodies receiving funding from the central government, they were also subjected to strict financial controls of the Treasury in managing their budgets similar to the Ministries and Departments. Interestingly, the comparison of responses between Ministries and Departments further highlights critical dimension on the status of 'Lets managers manage' policy. Table 3 displayed that all respondents from the Ministries indicated that the MBS had improved the budgetary authority of line managers, budget preparation, virement, monitoring of actual spending against budget, and overall financial management. These responses from the Ministries indicating increases for these issues were higher (but not significantly so) than their counterparts from Departments. Since the latter receiving its budget allocations through the former, it appears that the position of Departments as responsibility centres of the Ministries moderated the impact of the reform initiative in addressing financial management problems. Interestingly, the responses from Departments (78%) regarding greater virement due to the MBS were lower than responses from the Ministries (100%). This may suggest that the Parent Ministries were reluctant to delegate virement authority to the Departments, and this finding, to a certain extent, contradicts the 'Let managers manage' policy. Another interesting trend is on responses related to the impact of the MBS on the linkage between inputs and outputs, with proportions of responses from Departments (87%) and Statutory Bodies (84%) indicated increase were higher (but not significantly so) than the proportion of respondents from the Ministries (67%) indicating similar responses. This seems to suggest the difficulty of managers at Ministries to take the advantage of the MBS in redesigning their activities in a manner that inputs and outputs relationships of these activities are better defined. With the traditional input control in government organisations already maintained its dominance, difficulty to measure outputs posed greater

challenge in civil services to establish this relationship to provide more meaningful performance assessment. In light of this, the fact that this happened at Ministries, it may mean that it is easier to assess performance of service delivery at agency levels than at Ministry level. This finding also provide support about the function of the Ministries to be mainly a supervisory role monitoring the performance of Departments and Statutory Bodies.

A. Results and Analysis of Interview Survey

Confirming the questionnaire findings, 77% of the interviewees disclosed that MBS improved overall financial management of their organisations. From the interview survey analysis, the impact of MBS on financial management processes of the Malaysian government organisations is discussed with specific reference on changes in budget preparation, budgetary control, and on improving linkage between input and outputs. Before that, the impact of MBS on greater involvement of top management and line managers in managing the constrained public resources is discussed. Lastly, drawbacks and challenges of the MBS are also highlighted.

B. The MBS attracted top management and line managers into the budgeting process

It could be argued that the main factor that underpins success story of the MBS was that it attracted greater involvement of top management and line managers in proposing, managing and controlling budget allocations. This change bolsters all other improvement in financial management brought in by the MBS. The consensus of the interviewees from the Departments and majority of the interviewees (65%) from the Statutory Bodies disclosed that MBS attracted the top management and line managers into the budgeting process. This change was attributed to several MBS's features including customer oriented focus, the controlling effect of the Expenditure Target, and increased responsibility and autonomy of the line managers into the budgeting. The customer-oriented focus is reflected with the customer review requirement as part of the programme agreement that needs to be disclosed and reported to the Treasury during the budget review. The use of the expenditure targets attract the top management in budgeting process because it helped the budget proposal to be used as operational planning document as mentioned in the discussion of the impact of the MBS on budget preparation.
Another, the consensus of the interviews disclosed that the active participation of line managers in the budgeting process because with MBS, they are given the autonomy to flexibly allocate the budget according to their needs to different activities and projects. Also with MBS, they are given the responsibility to set the performance targets and monitor the budget for the activities under his/hers controls. The comment of a senior finance manager in a medium sized Department

encapsulates the changes of budgetary culture that have been brought about by the MBS particularly well:

> "In my opinion there are two main benefits of MBS. First, the MBS enabled the increased commitment of the management in the budget process. This gives the budget information more meaning to current needs. Second, the increased budget responsibility of operational management leads to increased commitment to those managers to spend wisely based on available funds. Before, the managers spent as they like and it became burdensome for the finance division to request additional funds or sorting out unused funds from other activities."

With the MBS, the increased participation of the line managers offers further strength to the budgeting process by allowing inputs of current needs of their operations particularly the customers. Before MBS, budget proposal normally prepared by the staff of finance and administrative division and approved by the Director General based on previous year spending with lack of direct participation of line managers.

C. The Impact of Expenditure Targets on Budget Preparation

With the significance of budgetary preparation and control in government organisations (Henley et al.,1993; Pendlebury and Karbhari, 1997) and the findings of the questionnaire highlighted that these two are the most improved by the MBS, the results of interview survey provides further evidence of the changes that have occurred in this area. Consistent with questionnaire findings, the majority of the senior managers interviewed (7 of 9 from Departments, 7 of 8 from the Statutory Bodies and all from the Ministries) disclosed that MBS had improved substantially budget preparation process.

It became apparent from discussion with participants that MBS improved budget preparation process due to the use of Expenditure Targets (ET). As the budget ceiling for the existing programmes and activities, the interviews revealed that it improved budget preparation as it reduced gaming between spending organisations and the Treasury, improved the budget review process by the Treasury officials and improved the status of the budget proposal for purposes of operational planning. These three benefits are closely integrated. For instance, a reduction in gaming lowered the inflated budget proposal, reduced negotiation process of the budget review between spending organisation officials and the Treasury review officer as one was trying to maximise budget while another is sceptical with the figure. Without a substantial reduction of allocation from the initial budget proposal, the budget proposal can be used as the planning document for the organisation as a whole. The interviews also revealed that before MBS, the budget proposals were always subject to heavy cuts as the Treasury tried to minimise the budgetary slacks. Confirming the benefits of Expenditure Targets (ETs), one of the deputy directors in a large sized Department remarked: "Before, if we wanted 10, we asked for 15 ...We knew the budget cut. If they (the Treasury) cut 2, we win, if cut by 5, that is still draw. That was before. Now, MBS makes budgeting match our needs. Anyway, we have to prove, and then BRO would give what we want. Anyhow, we have to provide details, not in general request."

These changes also affected the way the Budget Review Officer (BRO)s of the Treasury evaluating budget proposals of the spending organisations. Instead of focusing in finding ways to cut the budget proposed, ET enabled the BROs to focus only on the budget proposal on the new activities that include the extension of the on going activities, new activities and one offs (which were extraordinary and non-recurrent expenditures). This is considered as benefits among managers because it as it shortens the negotiation process during budget review. The comments made by a finance director in one of the large size Statutory Bodies disclosed the BRO's preference in budget proposal review and the improved efficiency in the review. He remarked: "The scrutiny of BRO is limited to New Policies and One Off (events) of Expenditure Targets. This saved a lot of time as the Treasury did not give emphasis on Existing Policies during the review" Another impact of MBS's expenditure targets (ET) on budget preparation is that it improved the budget proposal as planning document. The interviews disclosed that budget preparation process is a lengthy process and time consuming. Operational planning process involves managers at all levels from top management to individual responsibility centre managers. Many government organisations held seminars and several meetings of top management and line managers before finalising the budget proposal. Confirming the benefit of Expenditure Target as contributing to planning process, one of the line-managers in a large size Department commented: "The use of Expenditure Target is one of the most significant change in budgetary process. It makes our budget proposal more meaningful for planning purposes." Confirming the benefit of use of Expenditure Target regarding improved planning, one finance director in a medium sized Statutory Body pointed out: "When we are given an estimated allocation by the Treasury, we prepare our budget accordingly. This makes our planning exercise more meaningful as severe budget cut undermines what we have planned earlier and planning is not an easy process." Managers generally felt that significant changes had occurred as a result of MBS in improving planning and budgeting relationship. They felt that more precise spending could now take place in light of their plan. The practice of budget cut undermines the operational planning process which forms the significant part of the overall budget preparation process. With ET of MBS, this weakness is significantly minimised.

Nevertheless, the application of ET was not without weakness. It was discovered that ET would lead to traditional incremental budgeting. Budgeted expenditures for the existing policies are expenditures recurring from the same activities of previous years. This forms the main amount of total budget allocation. All interviewees disclosed that past year expenditure is the important basis of the budget proposal. It would seem that the allocation for existing policy is mainly incremental with incremental rate being revised every 5-years. Arguably, the use of existing policies in determining budget allocation may perhaps make MBS largely incremental budgeting for the period of at least 5 years before programme evaluation is conducted. During the 5 year period, BRO's main concern of budget review is only on allocation for new policies and one off events.

5.2. The Impact of MBS on Budgetary Control

Besides improving budget preparation, MBS also had an impact on the budgetary control particularly relating to its 'Let Managers Manage' policy, which led to greater delegation of budget authority to lower level managers and strict additional allocation policy. Getting operating managers directly involved in budget monitoring may improve the timing of corrective actions if the spending goes off budget, as they are directly involved in the daily operations of the organisations. This may mean a better method of budgetary controls. Thus, this confirms the questionnaire survey, which revealed that 92% of the respondents stated that MBS improved monitoring of actual against budget (budget monitoring).

The interviews disclosed that the delegation of responsibility of monitoring the budget to the line managers made them more committed in spending within limit. Prior to reforms, the responsibility of monitoring was entirely shouldered by finance division's staff. Line managers had made requests on allocation and monitoring of that spending was left to the finance divisions. Commenting on the impact of MBS on budgetary control, a planning director in one of the medium sized Statutory Bodies pointed out: "MBS is about 'sharing of responsibilities'. Overall, our budgetary controlled improved because when delegation of autonomy to state directors and division managers, we at the central office have to monitor the spending based on what is being planned. The allocation distributed to those managers should be spent based on planning and not based mainly on their ad-hoc needs as before." Nevertheless, despite the shift in responsibility of monitoring to the activity managers and to the responsibility centres increased their commitments to meet the spending limit, this would not lead them to under spend the allocation.

In relation to delegation of autonomy, interviews also disclosed the widespread practice of expenditure reports being prepared at the responsibility centres. Although this practice of submitting monthly expenditure reports was in place before the introduction of MBS, this practice became wide spread even more with the creation of many responsibility centres. Respondents generally commented that along with an increase in procurement autonomy of the line managers, the creation of new responsibility centres became necessary particularly for organisations, which previously used centralised payment systems. Commenting on the benefits of preparing expenditure report at responsibility centres, the finance and administrative director of a medium sized Department director pointed out: "Now, the information provided is more informative. The managers at the state levels know the actual progress of the activities and projects. Our role is more of monitoring and co-ordinating. Before, we decided for them their procurement request. We did not know either what we decided for them was the right thing. Now, they can make their own purchases and payments. Autonomy has certainly been given.

"With this change, information reported in the expenditure reports was more informative. But for control purposes, the responsibility centres also need to copies of source documents to finance divisions for verification purposes. For Statutory Bodies, a copy each of the expenditure report is submitted to Parent Ministries and to the Treasury. On the other hand, a significant majority (7 of 8) of the top management of Departments interviewed disclosed that they only dealt with the Parent Ministry for monthly budget monitoring. The Departments did not directly feel the role of the Treasury in monitoring their spending. The minimal role of the Treasury in the budgeting process at the Departmental level was nicely expressed by a finance director of a medium sized Department: "The Treasury does not involve itself in budgetary control at the Departmental level, except for certain activities that involve national priorities. For instance, our Prime Minister has given us many new projects. For this, the Treasury deals directly with us. Other than that, in all financial matters, we deal with the Ministry." Obviously, this practice is consistent with the fact that Departments are under direct supervision of the Ministries. On examining the expenditure reports in several Departments, their contents were predominantly figures for budgeted amounts and actual spending to date for each voted activity. The figures were only in aggregated form and no budget profiling was revealed. Obviously, the monitoring exercise apparently places more emphasis on total expenditure with the main concerns of managers spending within budget than monthly spending with a focus on efficiency and effectiveness.

Despite the improvement on budgetary control mentioned above, it could have been done better if the structural problems of annuality on shortfall of allocations and unreasonable delay in giving out warrants and grants to spending units were addressed. The vast majority of managers interviewed expressed their concerns about the shortfall of allocations, as this affects their execution of planned activities. It would seem that relatively little change has occurred since the study undertaken by Xavier (1996) relating a fall short of budget allocation at lower levels of management. The interviews revealed that the shortage of allocation during the budget period was difficult to avoid due to time gap between budget preparation and actual spending .The time gap led to budget was approved at outdated rates and prices, as prices of goods and services generally increase over time. Nonetheless, Departments could obtain additional funds from the parent ministries. With the Treasury approval, the practice of mid year review of budget enables controlling officers at Ministries to provide additional funds to requesting Departments through virements of funds across programmes.

The Treasury does not give additional funds for activities voted for in the year. Additional funding from the Treasury is only for new activities that arise because of the new policies legislated by the Cabinet during the year. The interviews also revealed that the delay in receiving warrants and grants at the spending organisation level undermining reform efforts. Instead of receiving warrants in early January, they normally received them between February and March. As funds then need to be sub-allocated to the responsibility centres, this led to delays in running activities. This takes more time before the monies can actually be spent. Commenting on the impact of the allocation delay, a senior director of planning from a small sized Department remarked: "Although we know that the allocation has been approved, we receive the warrants late. Many of our activities have to be put off because we cannot run them based merely on allocation approval. We have to receive the warrants first; ...if spending without warrants, the officer in charge will have to pay a fine and he will be personally liable. Moreover, approved allocation without a warrant can be withdrawn. It is risky." It is obvious that the Departments suffer longer delays than the Statutory Bodies because they received budget warrants through Parent Ministries. Despite the fact that with the MBS;s 'Let managers manage' policy encouraging delegation of greater financial autonomy to lower level managers and creations of new responsibility centres, this does not change the original structure of Departments to receive allocation via the Parent Ministries.

5.3. The impact of MBS on improving the linkage between input and output

The literature highlighted the importance of results based performance measures in improving resource management, the majority of interviewees (60%) revealed that the use of output-based targets brought more focus on ways they managed their activities towards achieving the broad organisational objectives, rather than mainly to keep expenditures within budget. This confirms the questionnaire finding on the impact of the MBS on the linkage between input and output with 77% of the respondents indicated the improvement. The comment of a senior planning director in a medium sized Statutory Body encapsulates this development caused by the MBS particularly well: "Although we had our performance targets for our main activities prior this.... For any approved activities, the MBS make the performance measurement more systematic as targets are more comprehensive encompassing quality, timeliness and costs. It appears that greater involvement of line managers in budgetary management and improved focus on results based indicators provide managers a better framework to ensure greater value for money of the given resources. Nonetheless, the improvement on performance measurement was not shared by several organisations interviewed. The interviews disclosed the resistance of managers to change caused this dissatisfaction and they provided two excuses: difficulty to measure outputs targets within an annual budget period and lack of information usefulness. While difficulty to measure outputs could be considered as common performance related problem in public sector, lack of information usefulness issues should have been addressed. Another interesting finding was attributed to existing separation between development and operating budget.

Lack of information usefulness of the performance indicators relates to two inter-related factors: indicators were not developed for managerial use and weakness in The Treasury's guidance and effective enforcement. This resistance of managers seems to suggest that their tendency to maintain the status quo led to indicators not developed for managerial purposes, but rather to comply with the Treasury's requirements. These discouraged them from preparing the information required meaningfully. This dissatisfaction was captured in the following comment from one top management officer: "We don't feel the necessity to make these measurements. For me, as long as there is no public outcry about our services, we are successful. As our managers do not rely on these measures for their work, our performance is good as long as we can spend within the allocation given." Confirming the lack of usefulness of the performance indicators reported, a senior planning director in a medium sized Statutory Body pointed out: "Even though we are required to show these indicators, since we give them aggregated figures, they are not really any use to our managers. After all... impact indicators... are heavily dependent on the perception of the managers concerned. Nevertheless, we have to provide them to the Treasury, since we are required to." Hyndman and Anderson (1997) argued that the absence of useful targets would undermine the ability of government organisations to plan and control effectively.

Although the managers were given the full discretion to select their performance measures, they blamed the Treasury over lack of guidance on developing useful measures. Several managers interviewed that they expected a greater role of the Treasury in terms of advising and monitoring the performance measures and targets. Explaining this, a planning director in one of the medium sized Statutory Bodies pointed out: "Every time we prepare the performance and exception reports... the monitoring is not enforced at the Treasury level. We are not properly advised about whether what we measured is right or wrong."Although the Treasury could control on the performance target reports submissions, interviewees claimed that the Treasury officials failed to assess the relevance of these indicators as they were not well versed in the details of operation in these service delivery organisations. Consistent with the finding by Hyndman and Anderson (1997), without formal guidance, relied heavily on examples that had been used in previous years that existed even before the MBS. These targets were not necessarily output based indicators as required in the Programme Agreement of the MBS (i.e number of talks per year, number of exhibitions per year).

6. Conclusions

Analysis of the impact of the Modified Budgeting System (MBS) on the financial management of the government organisations revealed that the MBS was generally perceived by respondents to have achieved its major objectives. The perceptions of 94 senior managers participating in the questionnaire survey perceived that the Modified Budgeting System (MBS) had brought improvements in the financial management of central government organisations particularly the impact on budget preparation and budgetary control, delegating greater budgetary authority to line managers, and overall management of government organisations' financial resources. Comparing the results across organisational status highlighted that the Statutory Bodies dependent on government funding were subject to treasury controls similar to Departments and Ministries, thus experiencing similar change brought in by the MBS.

Providing encouraging evidence on the applicability of the NPFM in emerging economies, interview survey highlighted MBS's 'Let managers manage' policy underpins the improvement it brought in the financial management of Malaysian central government organisations. While Expenditure Targets (ET) improving budgetary planning and execution, the active involvement of top management and line managers in the budgeting process was considered significant to reduce the gap between financial, strategic and operational matters. The policy was reflected in increases in the autonomy experienced by activity managers to allocate resources based on their operational priorities, increases in the creation of new responsibility centres, and increased autonomy to procure goods and services from authorised suppliers. These led to improved operational efficiency. However, the interviews revealed that managers' resistance to change, ET's embedded incremental budgeting, annuality, and delays in receiving funds undermining the reform efforts. There are limitations in this study that may lead to significant future research. Firstly, this study was confined to the impact of the MBS on financial management in central government organisations. Thus, no reference is made to the impact of the MBS on other public sector components such as state government, local government, hospitals, and public schools and universities. Secondly, there are obvious limitations in asking senior managers of government organisations about improved financial management in their organisations. Senior managers may be biased because they have vested interests in the success of the reforms. Also, any deficiencies admitted might be perceived as deficiencies in their management abilities. This may produce bias in their perceptions. In addition, the overall response rate to the questionnaire survey was only seventy-two per cent. Although the response rate was considered high, based on common practice in questionnaire surveys, the twenty-eight per cent non-response rate may indicate inherent systematic bias. However, the fact that triangulation of data was undertaken through interview surveys to minimise bias generated by research respondents.

There are three ways in which the research as a whole could be extended. First, the perceptions and experiences of managers at the state and local government levels regarding the impact of the MBS on financial management in their organisations could be incorporated. This could be undertaken by distributing the questionnaire used in this study to these managers. Second, further research should ascertain to incorporate the perceptions and experience of officers from the Treasury and the Accountant General's Department who were directly involved in advising and monitoring the implementation of the MBS. Also of benefit would be a case study approach that would attempt to study in depth the changes in financial management practice that have taken place since the introduction of the new system. In-depth comparative research could be undertaken by studying cases of organisations that had adverse experiences and those that had positive experience of the reforms.

Table II: The Overall Impact of the Modified Budgeting System on the Management Accounting Process

Impact of the Modified Budgeting System on:	IMPACT OF the MBS(n=91)											
	Significant Decrease		*Decrease*		*No Change*		*Moderate Increase*		*Significant Increase*		*OVERALL*	
	No	%	No	%	No	%	No	%	No	%	MEAN	RANK
Cost Savings	-	-	3	3	24	27	52	59	9	11	3.76	7
The budgetary authority of line managers	-	-	1	1	6	7	67	74	16	18	4.09	4
The linkage between inputs and outputs	-	-	-	-	21	23	54	60	15	17	3.93	6
Budget Preparation	-	-	1	1	11	12	52	57	27	30	4.15	2
Virement	-	-	1	1	17	19	47	52	26	29	4.08	5
Monitoring of actual against budget	-	-	-	-	7	8	61	67	23	25	4.18	1
Budgetary allocation carry-forward	2	2	4	5	50	56	26	29	7	8	3.36	10
Autonomy on Staff Salary	-	-	-	-	45	50	37	41	8	9	3.59	9
Autonomy on Personnel Matters (i.e. recruitment and training)	-	-	1	1	34	37	47	52	9	10	3.70	8
Overall management of financial resources	-	-	1	1	12	13	53	58	25	28	4.12	3

Table III: The Overall Impact of the Modified Budgeting System on the Management Accounting Process analysed by Organisational Status

Impact of the Modified Budgeting System on:	Organisational Status											
	Departments (n= 55)				Statutory Bodies (n= 25)				Ministries(n=14)			
	Decrease %	*No Change %*	*Increase %*	*Mean*	*Decrease %*	*No Change %*	*Increase %*	*Mean*	*Decrease %*	*No Change %*	*Increase %*	*Mean*
Cost Savings	2	28	70	3.75	5	23	72	3.82	8	31	61	3.69
The budgetary authority of line managers	-	6	94	4.20	4	13	83	3.98	-	-	100	4.29
The linkage between inputs and outputs	-	13	87	3.88	-	16	84	4.09	-	33	67	3.81
Budget Preparation	-	15	85	4.11	5	14	81	4.14	-	-	100	4.36
Virement	-	22	78	3.88	4	22	74	3.86	-	-	100	4.29
Monitoring of actual against budget	-	11	89	4.09	-	5	95	4.27	-	-	100	4.36
Budgetary allocation carry-forward	4	63	33	3.37	9	43	48	3.48	14	50	36	3.14
Autonomy on Staff Salary	-	56	44	3.51		43	57	3.71	-	36	64	3.71
Autonomy on Personnel Matters (i.e. recruitment and training)	-	40	60	3.69	5	23	72	3.86	-	50	50	3.50
Overall management of financial resources	-	16	84	4.09	5	14	81	4.09	-	-	100	4.29

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