NEW PUBLIC FINANCIAL MANAGEMENT IN INDONESIA (1999 – 2012): CONFUSION IN IMPLEMENTATION

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1. INTRODUCTION

New public financial management (NPFM) has been recognised as a global movement (Olson et al., 1998a; Olson et al., 1998b). Many countries have implemented NPFM reforms, such as Australia, New Zealand, Spain, Sweden, the United Kingdom, and United States, Canada, Ireland, Italy, the Netherlands, and Eastern European countries, such as Bulgaria, Lithuania, and Romania (Olson et al., 1998b; Humphrey et al., 2005).

NPFM, part of the wider movement of New Public Management (NPM), concentrates on accounting and financial aspects. Olson et al. (1998b) identified five different elements of NPFM: (1) the development of market-oriented management systems; (2) the development of the budgeting systems; (3) the development of performance management systems in government entities; (4) the reform in government financial reporting systems; (5) the reformation in public sector audits mechanisms.

However, NPM is not a comprehensible and well-defined concept implemented consistently from country to country. (Carlin and Guthrie, 2003; Olson et al., 2001; Pollitt, 2001a). Different types of reforms have been promoted at different levels of government, by different political parties and in different social and economic contexts. For example, in some countries, NPFM reforms have been implemented in the central government, meanwhile other governments conducted the reforms at the state or local levels (Olson et al., 1998b).

Although there are wide diversities, there is a fundamental similarity in the ideas underpinning NPM (Osborne and Plastrik, 1999). NPM supporters claim that such reforms will develop a government which is less interventionist, and more liberated, with reduced taxation, improved public sector efficiency and effectiveness, greater public service responsiveness and accountability to consumers, increased choices from public or private providers of public services, stimulated private sectors and better national economic performance (Steane and Carroll, 2001). In the broader sense, from an NPM point of view, reform in the public sector is intended to achieve 'value for money' (i.e., efficiency and effectiveness) in public service management (Broadbent and Guthrie, 1992; Parker and Gould, 1999; Hoque, 2005; Pina and Torres, 2003; Pollitt, 2001a; Parker and Bradley, 2000). NPM is designed to replace old bureaucratic characteristics, such as systems based on rules and procedures, structured hierarchies, political authorities and formalised decision-making processes, with values which emphasise adaptability, risk-taking, productivity, efficiency and effectiveness (Parker and Bradley, 2000; Hood and Peters, 2004). Also, the reforms are intended to simplify regulation and reduce its costs (Mathiasen, 1999). From the narrower perspective, specifically from reforms on financial reporting system, adoption of the accrual basis should assist users by providing information for decision making and accountability (Christiaens and Rommel, 2008; Hyndman and Connolly, 2011).

This research describes NPFM reforms in the Indonesian public sector. From analysing formal regulations, it is revealed that the Indonesian government has implemented five elements of NPFM. The implementation of the Indonesian reforms follow an NPFM normative pattern (in term of the five elements) proposed by (Olson et al., 1998a; Olson et al., 1998b) regarding how financial management public should be conducted.

2. FRAMEWORK OF THINKING AND RESEARCH METHOD

Olson et al. (1998a) find that the pursuit of a more accountable public sector may produce service provisions that are not as efficient and effective as originally hoped. Bowerman (1998), in discussing contradictions in NPFM concepts, identifies three terms (i.e., paradoxes, tensions and confusions), which are related to reform failure, that is, the promised conditions were not created.

First, the concept of 'paradox' implies a contradiction between the stated aim of the reforms and their outcome (Bowerman, 1998). Paradoxes refer to contradictions between what hopes or promises have been stated on the regulations and what have been achieved by reforms. For example, Hood and Peters (2004) note that the traditional bureaucracies are in many cases retained and augmented during the NPM implementation period. NPM may produce a bureaucracy that is more rule based and process driven than a traditional bureaucracy. A reform that does not achieve the stated objective can be categorised in the form of goal displacement. Hood and Peters (2004) indicated this phenomenon as the paradoxical effect of the NPM.

In line with Hood and Peters' notion, Olson, Humphrey and Guthrie (2001) noted that NPFM may produce the 'evaluatory trap'. They state that adopting accounting techniques from the business sector tends to generate fewer public services with ever-higher unit costs because these techniques are intended to achieve efficiency and effectiveness. Adoption of business accounting techniques in the public sector is aimed at enhancing legitimacy. To assure efficiency and effectiveness, public service organisations need more audit and evaluation, thus raising the indirect costs of the organisations. Instead of cutting legitimate indirect costs, such as evaluation (audit) activities, public sector organisations may instead focus on cutting direct costs (Olson et al., 1998a), with the effect of limiting service provision.

Second, 'tension' is based on a conception that reforms may affect varied stakeholders in different ways (Bowerman, 1998). A reform may be regarded as an improvement by some stakeholders, at the same time, the same reform may be considered as a problem by others. Stakeholders' position and perception influence their opinion of the reforms. Discrepancies in views of NPFM may cause tensions among stakeholders with the possible effect of reform refusal.

Third, the concept of 'confusion' implies a lack of clearness or anticipation before conducting a reform program (Bowerman, 1998). A type of confusion is inconsistencies in concepts and thoughts, which should be clear in order to develop a framework underpinning public sector reforms. In many cases, there are also contradictions between formal regulations (which construct practices) and techniques (how those regulations are put into practice). Confusion may exist in terminologies of concept, scope, and effect of the reforms. This confusion makes the reform produce unresolved and unintended consequences.

In addition to discussing Indonesian public sector reforms based on the NPFM perspective, this article also explores several confusions (contradictions) among concepts in Indonesian regulations and the NPFM precepts. The precepts are derived from the practices of NPFM, which commonly are implemented in several countries, and also from academic views on how NPFM should ideally be implemented. Several stipulations of the formal regulations controvert with those generally accepted NPFM precepts.

The results will be useful in term of providing early indications of the cause of paradoxes and this can inform discussion regarding improvement of Indonesian public sector reforms. Likewise, the Indonesia experience in implementing NPFM reform may be useful in implementing public sector reforms in other countries.

Essentially, this paper discusses accounting and management disciplines in the public sector domain, encompassing accounting and management systems, i.e., budgeting, accounting and financial reporting, auditing, and performance evaluation. This paper shows that the Indonesian public sector reforms have transformed these systems within the Indonesian government. Systems of accounting and financial reporting, and auditing were not recognised before such reforms. Since 1999, the Indonesian government has adopted systems like those implemented in the private sector.

This research is an archival and historical study, based on material from various existing academic literature and public documents. The literature review includes published material in academic books and articles, and also, regulations and reports published by the Indonesian Government.

This article consists of nine sections. The next section explains the objectives, the framework, the method and the contribution in relation to this research. Section 3 reviews briefly the Indonesian public sector reforms from the NPFM perspective. Comparisons between the generally accepted meanings of NPFM concepts and the interpretations of those concepts by the Indonesian government will be explored from section 4 to section 8. Section 9 concludes.

3. INDONESIAN PUBLIC SECTOR REFORM: A NEW PUBLIC FINANCIAL MANAGEMENT PERSPECTIVE

The Indonesian government initiated reform in politics and economics after the Asian currency crisis in 1998. From a government financial administration perspective, the reforms were aimed at improving the legal framework, which prior to the currency crisis, was not effective in regulating financial administration systems in public sector Indonesia. In fact, the systems were basically a furtherance of the Dutch colonial regulations. The legal regulations which were a heritage from Dutch Government were: (i) Indische Comptabiliteitswet (ICW) Stbl. 1925 No. 448, (ii) Indische Bedrijvenwet (IBW) Stbl. 1927 No. 419 jo. Stbl. 1936 No. 445, (iii) Reglement voor het Administratief Beheer (RAB) Stbl. 1933 No. 381. Although Indonesia became independent in 1945, some Dutch regulations adopted by the Indonesian Government at the turn of the century, remained.

Indonesian government administration is based on legal regulations, which take a hierarchical approach as follows (in descending order): (1) the Constitution, (2) laws, (3) government regulations, (4) presidential regulations, (5) local government regulations (The-Indonesia-Republic-Government, 2004a). Only with consent (approval) from the House of Representatives and the Regional Representatives Council (the upper chamber), can the Constitution be amended. Laws can be passed only after obtaining ratification from the House of Representatives. Government regulations and presidential regulations are prepared by the central government, and do not require consensus from the Parliament. Last, local government regulations are prepared by a local government, and need to be approved by a local government parliament.

The following section outlines laws that serve as a new legal framework for government financial administration (central, provincial and county).

i. The Local Governance Law No. 22/1999 (which has been amended by Law No. 32/2004)

   The Law regulates sharing authorities in public service provision between the central government and local governments. These relate toprimary education, public health, public infrastructure, agriculture, industry, trade, investment, the environment, land, labour, and transportation. Also, the Law define that local governments consist of provinces (provinsi) and counties (kabupaten and kota). Local governments have their own parliament and an executive government. Each local government is the authority for education, health, urban planning, housing, social-care services, forestry, farming, commerce, tourism, and, energy and mineral (The-Indonesia-Republic-Government, 2007). Central and local governments have a coordination relationship, that is not hierarchical. Local governments are independent of the central government. The president does not have authority to remove Governors as a head of a provincial government. Also, governors do not have an obligation to report to the President.

ii. The Fiscal Balance Law No. 25/1999 (which has been amended by Law No. 33/2004)

The Law gives authority to local governments to manage their own public finances, including the right to generate revenues and to prepare budgets. Also, the Law describes fund transfer (allocation) system from the central government to local governments.

iii. The State Finance Law 17/2003

The Law outlines the budget process and: (i) rules budgeting schedules from the preparation to disbursement; (iii) specifies budgeting general principles; (iv) assigns officials who have responsibilities of state finance management, (v) and builds financial relation between the central government and other state agencies.

iv. The State Treasury Law 1/2004

The Law introduces the responsibilities of the state treasurer and treasurers in government ministries, state institutions, and other government agencies. The Law also specifies general principles in managing state finance and accountability of public funds.

v. The State Planning Law 25/2004

The Law introduces the role of the National Development Planning Agency (Badan Perencanaan Pembangunan Nasional or BAPPENAS) and regulates processes of the national development planning, from the preparation to approval of plans, both short-term and long-term planning.

vi. The State Audit Law 15/2004

The Law specifies the role of the Supreme Audit Institution of the Republic of Indonesia (Badan Pemeriksa Keuangan or BPK). The Constitution mandates the state institution as a professional and independent state auditor. The Law also requires the institution to submit its reports to the Parliament.

The first element of NPFM is the building of a market-oriented management system. The Indonesian government has adopted this approach by introducing the President Regulation of

Financial Management for General Service Provider No. 23/2005. The Regulation details the stipulation in The State Treasury Law 1/2004 which states that General Service Providers (Badan Layanan Umum/BLU) are government agencies that provide goods or services based on productivity and efficiency, and do not seek profits (The-Indonesia-Republic-Government, 2004c). According to the regulation, General Service Providers (GSP) should be awarded flexibility in implementing business practices into government agencies (The-Indonesia-Republic-Government, 2005). The regulation is intended to give opportunities to compete between service providers, both private and public organisations.

In 1999, the Indonesian government enacted The Local Governance Law No. 22/1999 and The Fiscal Balance Law No. 25/1999. The Laws redefined the meaning of local autonomy, to change the legal framework of local authorities, to revise rules by which local leaders (i.e. governors of provinces and mayors of counties) are elected (instead of selected), to empower local parliaments. The Laws aim to provide independence for local government in managing financial matters, and to achieve a balance in control over local resources. From an NPFM standpoint, the Laws were an effort to implement NPFM (i.e. delegate the process of establishing a budget). Those Laws provide authority to local governments for setting their budget without central government intervention. Prior to the 1999 reforms the central government had authority to approve all local government budgets.

By launching the State Finances Law 17/2003 reforms in the new budgeting systems were introduced, so that the budget system is based on performance. The new system, which adopts the ‘performance budgeting’ concept, is supposed to eliminate drawbacks associated with the previous budgeting system. The new budgeting system requires that all government agencies prepare their own draft budget and propose it to the Ministry of Finance. Furthermore, government agencies must declare programs and expected outcomes of each program to be undertaken in the next year on budget documents. The programs must be evaluated as to their alignment with the vision and mission of the government unit. A program which does not support government unit strategy should not be allowed to be undertaken in the budget year. At the end of the period, the performances which are predetermined at the beginning of the budgeting process should be compared with the outcomes achieved by the entity. The result of the evaluation should be published to the public in order that society can measure the level of success of the entity.

The implementation of the new budgeting system simultaneously introduces the development of a performance management system, which corresponds to the third element (i.e. the performance management reform). The Law also states that the performance budgeting system cannot be separated from the performance reporting system, which requires the government agencies to publish and to evaluate their work (The-Indonesia-Republic-Government, 2003). The performance should be matched to the expected outcome which has been indicated on the budget document a year before.

The Indonesian government modified government financial reporting systems by passing The State Finances Law 17/2003 and The State Treasury Law 1/2004. Those regulations require governments (both central and local) present financial statements that are produced according to accepted accounting principles. The financial statements should include a balance sheet, a budget realisation report, a cash-flow report, and associated notes. Previously, governments only produced financial reports using a simple bookkeeping system. They could not be audited made public. The new laws state that governments have a responsibility to produce auditable financial statements. The Laws also state that financial statements must be in accordance with the Governmental Accounting Standard (GAS).

The fifth element is external public sector audits, including the function of examining government financial statements and reviewing service efficiency and effectiveness of the budget disbursement. The State Audit Law 15/2004 requires that government financial statements be audited by the Supreme Audit Institution of the Republic of Indonesia (Badan Pemeriksa Keuangan/BPK). The Institution is a state entity which has the same level of authority as the legislature (the Parliament) and the executive (the president). The Institution has the primary responsibility to audit all governments (the central, provinces and counties) and other state higher institutions, such as the Parliament, and the Supreme Court.

4. MARKET-ORIENTED SYSTEM

The market-oriented system is constructed based on the concept that reliance on market mechanisms will compel public service entities to focus on efficiency, effectiveness, and quality of service. The system views public institutions as sellers and citizens as customers. In the market system, to obtain a particular service, citizens must disburse some money. On the other hand, public service providers must set the right price and quality for services which they provide.

Customers must be provided with various alternative services offering different quality and cost, thus providing customers with choices to select the services that most suit their needs. Public services agencies will be encouraged to give the best quality and the lowest cost for the services the agencies provide. Under the market system, public service agencies are encouraged to compete with each other to provide the best service to customers.

Public service sectors are not treated as monopoly providers because monopoly curbs competition and innovation, and restrains customers in obtaining the best services with the lowest price. Because customers have freedom to choose their preferred service, the transaction between public service providers and consumers is "at arm's length". Public service providers not only must compete with other public service providers but also consider private sector organisations as competitors. The competition drives private and public sector entities exert a same standard of performance, such as standards for quality of service.

While the literature acknowledges that competition will not solve all problems in public sector, there is a view that it may provide some advantage to public sector organisations (Osborne and Gaebler, 1992), in terms of: (i) creating efficiency; (ii) eradicating monopoly of public service; (iii) forcing public service providers to respond to customers' needs; (iv) stimulating innovation; and (v) increasing public servants' work ethos. English, Guthrie and Parker, (2005) state that competition and quasi-market conditions are necessary for the implementation of NPM. Osborne and Gaebler (1992) describe four types of competition which have been implemented across the US: (i) competition between public sectors and private (business) companies in providing services (service provision); (ii) competition among private (business) companies in selling goods and services to governments and other public sectors; (iii) competition among public service agencies in providing services for the public; (iv) competition government agency providers within governments in providing goods and services for other government agencies.

In order to stimulate competition among public service providers, it is necessary that government agencies are treated as independent organisations although they still belong to government. Those organisations are called quasi-autonomous 'non-governmental organisations' or 'quangos'. The organisations may be cost centre or profit centre organisations. The performance of these organisations will be measured according to costs disbursed or profits generated as well as other measures, such as quality of service, for example, patients' waiting time in hospitals. In order to achieve a degree of competition, 'quangos' should import supposedly good commercial practices (such as performance measurement, auditing and business accounting systems) from the private sector. It is also important that 'quangos' rely on market solutions whenever possible to solve problems.

Creating 'quangos' also allows for a split between policy decision making activities (steering) and service provision (rowing). Osborne and Gaebler (1992) state that government should be 'steering rather than rowing'. Further, 'quangos' should be separated from the political arena. Governments basically focus on making policy and setting directions (e.g. setting long term plans, strategies, and priorities to handle important issues). Governments deal with citizens, communities, political parties and other stakeholders in order that a government policy will be accepted and can be implemented. Governments emphasise regulation setting, rather than operation activities, such as hiring more public employees and delivering directly services needed by the community (Osborne and Gaebler, 1992). These activities should be undertakend by 'quangos'.

In order to ensure separation of political and service provision activities, managers of 'quangos' should be appointed based on merit (e.g. expertise, skill, and experience), not because of political party affiliation. To build 'quangos' which can compete with private sector organisations, greater freedom from ministerial direction and from intervention is required because these might weaken management's ability to operate the organisations on a commercially competitive basis (Guthrie and Parker, 1998). Public sector managers should be given greater autonomy with their accountability being more internally oriented towards their own senior management and boards of directors rather than directly to government ministers.

General Service Providers ('Badan Layanan Umum'/BLU) in Indonesia are supposed to be government agencies with business entity like characteristics. General Service Providers (GSP) are government agencies which provide goods or services based on productivity and efficiency although the organisations are not aimed only at seeking profits (The-Indonesia-Republic-Government, 2004c). General Service Providers (GSP) should be awarded flexibility to implement business practices in financial management of the government agency (The-Indonesia-Republic-Government, 2005). These regulations mean GSPs can compete with other public service providers, both from the private and public sectors. In the central government, organisations which can be treated as GSP are tertiary universities, central hospitals, and training bureaus. In the local government, primary and secondary schools and local hospitals are organisations which can be considered as GSPs.

However, GSPs in Indonesia do not have the same fundamental characteristics as 'quangos' in NPFM. They differ as follows.

1. Government officers of GSP are not awarded flexibility to manage their business like a manager of a company. For example, government officers have to abideby at least 22 regulations (which consist of 5 laws, 1 government regulations, 1 president regulation, 11 finance minister regulations, and 4 regulation of the treasury general director). Additionally, they must adhere to many regulations in government financial reporting and budgeting systems. Inflexibility makes it difficult for GSPs to be competitive like a business entity.
2. GSPs are not fully separated from bureaucracy because they are still responsible for government budget and government-type financial reports. Those budgets and reports must be incorporated in ministry's budgets and reports. In addition, employees of GSPs are public servants.
3. GSPs are a part of ministries. They are accountable to public via parliament. The condition makes separation between political and service provision activities difficult to achieve. Because of the situation, GSPs may easily be influenced by political parties.

The characteristics of GSPs influence the concept of the public sector in Indonesia. Theoretically, Funnell and Cooper (1998) propose four features to identify public sector organisations: financing arrangements, ownership, management, and accountability arrangements. From a financing arrangements perspective, organisations which receive any funds from the government for financing recurrent operations and capital projects can be considered public sector. Ministries can be identified as public sector organisations because they receive government funds and have to integrate their budget into the government budgeting system. Second, from an ownership viewpoint, organisations which have assets owned by the government are public sector. Third, if the management of an organisation is controlled by government, the organisation can be categorised as public sector, viewed from a management standpoint. Finally, from an accountability arrangement point of view, organisations are identified as public sector if they are accountable to the public through parliament. Although some ‘quangos’ are not controlled by government, they can still be classified as public sector organisations because they receive funds from governments and must be accountable to the public.

The public sector in Indonesia is similar to those in western countries such as Australia, New Zealand, and the United Kingdom. Most public services are still controlled and financed by the government (either central or local), such as universities, schools, hospitals, orphanages, road maintenance and transportation, and fire fighters. For instance, universities are central government entities monitored by the Ministry of National Education. On the other hand, primary and secondary schools are classified as county entities. The organisation must prepare budget and financial reports in accordance with the rules released by the central government. Publication of budget and financial reports are a method to fulfill public accountability obligations.

In Indonesia, the term public sector refers to all organisations under government control. Therefore, the term ‘public sector’ and ‘government’ are used interchangeably to refer to an organisation owned and controlled by governments, and which does not merely consider profit as its goal. Consequently, the public sector in Indonesia cannot be discussed separately from government administration.

In the case that there are public services which have been privatised and managed as business companies such as power (electrical energy), railway and postal services, these companies are excluded from the public sector category. For those companies, generating profit is the main objective. In addition, employees of those entities are not public servants. These organisation are a private or business organisation although they are still controlled by governments, and sometimes still receive funds from governments in terms of subsidies or investments.

5. BUDGETING SYSTEM REFORMS

In the private sector, budgets are financial plans, which are used to allocate resources. In the private sector, budgets are targets, which reflect what the company hopes to achieve in the next year rather than how much (in monetary amount) the organization should expend or realise. Companies and other business organisations rarely publish their budgets to shareholders. Moreover, there is no obligation for companies to draw up budgets even though they usually do.

For governments it is not only mandatory to prepare a budget but also to publish it. In Indonesia, a budget needs to be approved and ratified by Parliament before it can be implemented and released to the public. The ratified budget is a legal document. Consequently, the executive must adhere to the budget in cash disbursements in the following year. Discrepancies from the budget, in terms of accounts and monetary amount, are equivalent to breaking laws.

The State Finance Law 17/2003 specifies the general rules of the budgeting process in Indonesia. Binsar Simanjuntak (2010), as the Head of Government Accounting Standard Setter Board, asserts that the Indonesian government should adopt the cash accrual system both in the budgeting and the financial reporting process. The Law defines government revenues as government rights which are recognised as the accumulation of net wealth values; on the other hand, government expenditures are government obligations recognised as subtraction of net wealth values. However, his interpretation differs rom Guthrie's (1998), which states that the accrual-based budgeting system includes non-cash expenses as depreciation or accumulated government servants' benefits on government budget accounts. Based on this view, the budgeting system in Indonesia has not yet adopted accrual based budgeting because it has not attached non-cash accounts to budgets.

van der Hoek (2005) identifies that there are three budgeting methods pertaining to expense recognitions: cash-based appropriations, commitment-based appropriations, and accrual-based appropriations. Cash budgeting or cash-based appropriations give the government rights to make cash expenditure over one year. Commitment-based appropriations give the government authority to make commitments and make cash payments according to these commitments without a predetermined time limit. Accrual-based appropriations cover the full costs of the operations of the government and increases in liabilities or decreases in assets. According to the State Finance Law 17/2003, the Indonesian Government only has a right to disburse budget appropriations on the current budget period. Accumulated expense from the previous period or advanced (pre-paid) expense for the next period cannot be recognised in the current budget. From van der Hoek (2005)'s perspective, the Indonesian budgeting system is a cash-based system.

Besides the cash budgeting method, the other budgeting principle adopted by the Indonesian government is performance budgeting. The stipulation of the performance budgeting principle is covered by the State Finance Law in 17/2003. The principle emphasises disclosures of expected outcome on the budget document. The objective of the system is to improve transparency and accountability by providing information about expected outcome from budget appropriations that will disburse in the next year.

Blöndal et al. (2009) criticise the Indonesian budgeting system because, they argue, on a practical level, the budgeting system is very rigid, in terms of both accounts and procedures. The rigidity limits flexibility in cash disbursement next year. The emphasis of the budgeting process is the line-budgeting system. Conceptually, the line-budgeting system requires very detailed input information, such as detailed accounts, instead of focusing more on expected performance and results (Blöndal et al., 2009). This means that there are many rules which regulate government agencies or the public sector in the budgeting process. These rules restrict flexibility to build individual systems compatible with the organisation's character and and to achieve the organisation's goals.

Furthermore, there is the chart of standard account, which homogenises accounts used by all Indonesian government agencies. The accounts are broken down to specific disbursements, such as: detailed accounts of government servant's salary (e.g. government servant's benefit, weekly or daily honorarium) and detailed accounts of machinery, equipment, vehicle, furniture, and building (The_Finance_Ministry, 2011). Budgets specify the monetary amount which can be disbursed by each government agency for each aforementioned account (line-items.

The accounts (line-items)are narrow and used to confine the government agencies' disbursement in the next year. On average, each government agency has hundreds of different accounts to be controlled over a year. The procedure was originally initiated to control government officers.

In addition, the Parliament is deeply involved in every stage of the budget process, from the earliest budget formulation stages to budget implementation. The Parliament has unlimited powers to amend the budget proposal submitted by the government. Sometimes, it amends the budget significantly. Its scrutiny tends to focus more on detailed line items than comprehensive budget policies and strategic priorities.

According to the Law 17/2003, a government officer can request permission from the State Treasurer or the Parliament to shift funds across the accounts; however the procedure is complicated (Blöndal et al., 2009).

Osborne and Gaebler (1992) warn of the impact of the line-item budget implementation. In order to avoid the complicated procedure of shifting accounts, public servants prefer to procure goods or services which were stated on the budget although they are no longer needed. Osborne and Gaebler (1992) note the system as an "attempt to prevent bad management made good management impossible".

Moreover, Blöndal et al. (2009) also identify that programs and activities are similar from year to year, and there are minor changes. The modifications only occur at the margins of the monetary amount for programs and activities. This is known as an incremental budgeting system. Government officers revise current year amounts of income and expenditure as the starting point for determining the budget for next year. The system does not consider whether a particular programs or activities are still required or whether the monetary amount currently estimated is reasonable. Once a program and activities are budgeted, they will be included in future budgets. Thus, only incremental changes in each account are considered. Attention is therefore focused on incremental differences between this year's budget and last year's budget rather than on the whole of the budget.

Since the traditional budgeting practices, such as line-item and incremental budgeting system, are not outcome-oriented and tend to allocate resources only by adding the previous budget with a fixed percentage (or at the margins) in government budgets, NPM reforms should eradicate those practices. Jones and Pendlebury (1984) argue that line-item budgeting should not be adopted in modern government administration, and be replaced by programme-based budgeting or other new budgeting approaches. Australian governments have replaced the long-lasting line-item budget with more beneficial budgeting methods in the late 1980s (Funnell and Cooper, 1998).

There is a contradiction in implementing a performance budgeting system in Indonesia. Normatively, the objective of adopting the performance budgeting system is to eradicate traditions of line-item budgeting and the incremental budgeting system. Although, the State Finance Law in 17/2003 emphasises the adoption a performance based budgeting system, the lower regulations (such as government regulations and president regulations) reinforce the practices of line-item and incremental budgeting system.

6. PERFORMANCE MANAGEMENT SYSTEM REFORMS

The State Finance Law in 17/2003 states that the performance-based budgeting system cannot be separated from the performance reporting system which requires that government agencies evaluate and publish their achievements over a year to the public (The-Indonesia-Republic-Government, 2003). Performance should be matched to the expected outcome has been indicated on the budget document a year before. From an NPFM perspective, this represents the implementation of the third element of NPFM. A performance management system comprises integration of non-financial performance indicators to the budget system. The system requires incorporation of both financial and management accounting systems as well as other economic information into an integrative system (Olson et al., 1998b).

A regulation that governs the performance reporting system is the President Regulation, Performance and Financial Reporting for Government Agencies No. 8/2006. According to the regulation, government performance reports should be released in order to comply with public accountability or to fulfil government obligations to be accountable to the public (The-Indonesia-Republic-Government, 2006a).

Two terms are often used interchangeably: ‘performance measurement’ and ‘performance management’. ’Pperformance measurement’ can be defined simply as the process of measuring performance, whereas ‘performance management’ comprises not only ‘performance measurement’ but also the stages that are used to motivate public servants to achieve organisational objectives. ‘Performance measurement’ includes measures based on key success factors, measures to track past achievements, measures of expected outcomes, measures of output, measures for detection of deviations, and measures of input (Radnor and McGuire, 2004). ’Performance management’ also involves training, team work, dialogue, management style, attitudes, shared vision, employee involvement, multi-competence development, and concepts of incentives and rewards (Radnor and McGuire, 2004). Performance reports are intended as public sector management instruments which have functions to motivate public servants in delivering public services.

'Performance management' was viewed as a set of techniques which can be used by managers and politicians to manage performance within public sector organisations. 'Performance management' is not only a process for ensuring that public service organisations and their employees are well placed to deliver the service, but also for creating performance criteria for awarding good performance based on societal, political and managerial judgment.

The Government Regulation Performance and Financial Reporting for Government Agencies No. 8/2006 merely regulates parties that must present performance reports, forms of performance reports, process of performance report preparation, and sanctions for neglecting the regulation. The regulation does not contain how the report is used to motivate and stimulate public servants' work ethos. **The** Indonesian performance reporting system can be categorised as performance measurement instead of performance management. NPFM reforms should develop 'performance management', further than 'performance measurement'.

7. FINANCIAL REPORTING SYSTEM REFORMS

Indonesia has adopted a full accrual accounting system since 2010 (The-Indonesia-Republic-Government, 2010), as stated by the Government Regulation of Governmental Accounting (GAS) No. 71/2010. However, governments (locals and the central) are able to utilise the cash toward accrual system to prepare government financial reports until 2013. The implementation of a full accrual accounting system will be mandatory for government financial reports which end at 31 December 2013 (Simanjuntak, 2010). GAS regulates that revenue, expense, asset, liability, and equity must be recognised on the 'accrual basis' (The-Indonesia-Republic-Government, 2010).

The Government Regulation No. 71/2010 replaced the preceding regulation No. 24/2005 which stated that Indonesia adopted the 'cash-toward-accrual' system from 2005 (The-Indonesia-Republic-Government, 2010). The system required that recognition of transactions and other financial events over a reporting period and preparation of financial reports (such as budget realisation reports and cash-flow statements) be based on ‘cash basis’. At the end of that period, the financial reports were adjusted with accrual transactions, such as depreciations and deferred expenses. Because of the aforementioned procedure, recognition of assets, liabilities, and equities were conducted at the end of period. According to the Government Regulation Government Accounting Standard No. 24/2005, the procedure was defined as the ‘cash-toward-accrual’ system which means that revenues, expenses, and other finances accounts were recognised on ‘cash basis’; on the other side, assets, liabilities, and equities were recognised on accrual based. The term of ‘cash toward accrual’ used in the Government regulation is similar to ‘modified cash accounting’ according tothe International Organisation of Supreme Audit Institutions (INTOSAI).

Before those Government Regulations (No.71/2010 and No.24/2005), laws introduced on a financial regulation basis were Indische Comptabiliteitswet (ICW) Stbl. 1925 No. 448 and Indische Bedrijvenwet (IBW) Stbl. 1927 No. 419 jo. Stbl. 1936 No. 445. These regulations were introduced by the Dutch Government when they colonised Indonesia prior to independence in 1945. A financial reporting system inherited from the Dutch required the Indonesian Government to maintain a simple booking which only recorded cash inflows and outflows. The system did not require a standardised general ledger, as used in generally accepted accounting practices. Financial reports only considered the funds disbursed over a year, and compared those disbursements to the budget. These were the only government financial reports produced by the system. The reports were entitled Budget Calculation Reports (Laporan Perhitungan Anggaran) and associated notes. In addition, there was no other report, such as balance sheets, cash-flow reports, and equity reports. In the period until 2005, there was no requirement for the reports to be audited by external independent auditors. The audit procedure, which was usually conducted in that time, was the compliance audit, which examined the compliance of government practices with government regulations.

From an NPFM perspective, Groot and Budding (2008) note that replacing traditional cash accounting with an accrual accounting system is an important idea in order to improve the financial reporting process, since it can be a basis for public service management to make decisions. Accrual accounting is defined as an accounting method by which transactions and other financial events are recognised when they occur, and not only when cash or its equivalent is received or paid. All elements of financial reporting are recognised under accrual accounting, such as assets, liabilities, net assets/equity, revenue and expenses.

Besides accrual, there are three methods (‘full cash’, ‘modified cash’, and ‘modified accrual’) which have been implemented into government accounting practices (Peter van der Hoek, 2005). ‘Full cash’ and ‘full accrual’ represent two ends on a continuum of possible accounting methods. The INTOSAI defines ‘full cash’ as the system which records transactions when funds are paid out of an appropriation authority or when funds are received. Conversely, ‘full accrual’ is defined as a system which recognises expenses as incurred, records revenues as earned, capitalizes fixed assets as owned, and liabilities as obligated. In the middle between those points are ‘modified accrual’ and ‘modified cash’.

‘Modified accrual’ is defined as a system which records expenditures when resources are received and revenues when they are measurable and available within the accounting period or shortly afterward. In contrast, ‘modified cash’ is defined as a system which recognizes transactions on a cash basis during the year and the setup of unpaid accounts and/or receivables at year’s end. Many countries have adopted accrual accounting with various degrees of ‘accrualisation’ (Peter van der Hoek, 2005), for example, adoption accrual without recognising depreciation.

‘Full accrual’ is a method which is largely accepted by commercial or business practice. On the other hand, modified accrual is a method which is essentially copied from commercial practice but with less emphasis on comprehensive statements of financial position. All transactions are recognised on a cash basis. The reports are also presented on a cash basis, but there are associated notes which explain the impact of accrual transaction on the reports. The model is also entitled ‘cash with accrual disclosure model’ of reporting (Carlin, 2005).

van der Hoek (2005) suggests that the ‘cash based accounting system’ does not provide information that governments need to operate efficiently and effectively. The cash system does not produce comprehensive information of the actual cost; especially when disbursement producing returns (earnings) over a number of years, such as investment expenditures. The cash-based system measures investments by the nominal value at the date of spending, whereas the accrual-based system calculates the costs of investments with the present value considering interest rate and expected earnings.

Hyndman and Connolly (2011) assert that information, which is produced by a cash-based system, pertaining to capital investment contains bias. Conversely, information provided through the accrual-based system contains better-informed decisions so it can be used to calculate the opportunity cost of capital. Information produced by the cash-based system can misrepresent the actual cost of government (Hyndman and Connolly, 2011).

Accrual accounting information should be useful in evaluating the government's performance in terms of efficiency, service costs, and performances (van der Hoek, 2005). The accrual-based system should be beneficial for management to make decisions (Blöndal, 2003; Lapsley et al., 2009; Hyndman and Connolly, 2011).

However the objective of adoption of an accrual accounting system in Indonesia is not for providing information as a foundation for management to make decisions. The government financial reports (which are accrual-based) are assumed to provide information which is more transparent and accountable. According to the Governmental Accounting Standard (GAS) (The-Indonesia-Republic-Government, 2010), government agencies must inform the public about efforts in systematic and structured reporting. According to the regulation, the reports should contain information which will be useful for the public to evaluate accountability, transparency, intergenerational equity, and performance of the agencies. For internal management of government agencies, the information can be used to evaluate the agency's performance, to plan, to manage, to control utilising assets, liabilities, and equity for public prosperity (The-Indonesia-Republic-Government, 2010). The objective of government financial reporting process, as written in the GAS is:

> "Governmental financial reporting should present information which is useful for users in evaluating accountability; and making economic, social, and political decision through:
>
> i. provide information about resources, allocation, and utilisation of financial resources;
> ii. provide information regarding sufficiency (adequacy) of current revenue for financing disbursement;

iii. provide information not only about how much economic resources which have been used but also performance which have been accomplished;
iv. provide information in relation to how to obtain funds for financing government activities, and how much cash is needed;
v. provide information about financial positions and long and short term revenue sources, such as from tax revenues and loans;
vi. provide information regarding financial position of the reporting entity, whether there is increase or decrease, as result from government operations and activities over the reporting period."

From the excerpts above, it can be concluded that government financial reporting is not intended for providing information which can be used by management to make decisions. The accounting information emphasises providing general purpose information for external users of government entities, such as the Parliament, supervisory bodies, and the public.

The adoption of accrual system in Indonesia may not produce information which is internally useful for management to make decisions because the government accounting system is built on a rules-based system. Theoretically, the rules-based system requires that entities should follow many detailed accounting rules in order to comply with generally accepted accounting principles (GAAP). An accounting standard setter promulgates a particular accounting rule for each specific entity and for each special case. There are many detailed rules which will be created. An entity should comprehend and adhere to all the detailed accounting rules.

Different from the rules-based accounting system which requires uniformity, the principles-based system provides entities with flexibility in treating transactions and accounts, and in interpreting comprehensive principles. The system does not require entities to follow specific rules. Standard setters only release a few general accounting rules, instead of detailed guidance.

The Indonesian accounting standard setter has released the government accounting standard (which consist of a conceptual framework and 12 statements), 11 technical bulletins, and two interpretations since 2004. Besides those accounting rules, the Indonesian public sector must adhere to regulations which are promulgated by the central government. For example, a state-owned university in Indonesia has to abide to at least 23 regulations (which consist of 5 laws, 8 regulations, 1 president regulation, 2 finance minister regulations, 4 national education minister regulations, and 3 regulation of treasury general director).

Some of the rules are very detailed and there is little opportunity for government entities to have flexibility. It makes the entities adopt a uniform accounting system, which may not be applicable in some circumstances. For example, there is a rule which standardises the chart of accounts used by all government entities; and regulates methods of how to record transactions on journals and post those on the general ledgers. The rules inhibit the accounting system from producing information which will be used by management in making decisions. Each case (problem) needs different kind information. Each manager has difference preferences on how information is presented. The standard of chart of account and other rules will limit managers to obtain particular information which is relevant to making decisions.

Rules-based systems restrain a range of ideas, innovation and flexibility which are needed to develop competitive public service providers; therefore the system is intended to be superseded under NPM reforms. Hood and Peters (2004) and Osborne and Gaebler (1992) note that the fundamental impetus of public management reforms was a replacement of rules-based system (and process-driven routines system) with results-oriented system. It is almost impossible to generate managerial reporting from the system because it offers rigid and strict procedures without flexibility. Olson, Humphrey and Guthrie (2001) note that adopting accounting techniques from the private sector tends to generate fewer public services with ever-higher unit costs; whereas the techniques deliberately emphasise efficiency and effectiveness. They refer to this phenomenon as the ‘evaluatory trap’.

8. AUDITING SYSTEM REFORMS

The final element of NPFM reforms is development of internal and external public service auditing systems. For implementing the element, the Indonesian government launched the State Audit Law 15/2004 and the Law of Supreme Audit Institution 15/2006 which introduced the Supreme Audit Institution of the Republic of Indonesia (Badan Pemeriksa Keuangan or BPK) as the only organisation with authority to conduct auditing in governments (locals and the central governments) and other the state higher institutions, such as the Parliament and the Supreme Court. The Laws also identify three types of audit which can be conducted by the Supreme Audit Institution: financial audit, performance audit, and audit for a special purpose. The Law also require audit reports be submitted to parliaments, and be publicly available (The-Indonesia-Republic-Government, 2006b, The-Indonesia-Republic-Government, 2004b).

Those Laws replace the Law of the Supreme Audit Institution No. 5/1973. Nasution, as chairman of the Supreme Audit Institution, states that the old Law did not provide adequate independence to the Institution to conduct audit procedure, and clear guidance to the institution to be accountable to the public (Nasution, 2008). In contrast, the new Law positions the institution at the same level of authority with the legislature (the Parliament) and the executive (the president).

As an integral part of the audit system reforms, the Supreme Audit Institution instigated two regulations: the state finance-auditing standard (the regulation No. 1/2007) and the code of conduct for government auditors (the regulation No. 2/2011). According to the auditing standard, financial auditing intends to provide reasonable assurance that financial reports have been presented adequately in accordance with generally accepted accounting principles.

Furthermore, the regulation also requires that auditing should be design to detect misdemeanour, fraud, and abuse (The-Supreme-Audit-Institution, 2007). Because corruption is a type of misdemeanour, the Indonesia state finance auditing intends to detect corruption and collusion practices in the public sector. For that reason, the audit report contains notes showing corruption by public servants. Nasution states that the Supreme Audit Institution has primary roles which have been performed: (1) collaboration with other government agencies in fighting corruption, collusion and nepotism; (2) improvement of transparency and accountability by adopting Government Auditing Standard (GAS) (Nasution, 2008).

The Supreme Audit Institution has adopted the ‘value-for-money’ audit or the performance audit which is defined as audit from economic, efficiency, and effectiveness to assess performance of government agencies (The-Supreme-Audit-Institution, 2007). There are sections in the audit report which explain the result of the performance audit. However, an emphasis on transparency and accountability as well as fighting corruption is different from public sector audit reforms in many developed countries such as Canada, Australia and New

Zealand. Reform in public sector auditing usually emphasises monitoring service provision functions and reviewing the efficiency and effectiveness (value-for-money) of public service organisations (Olson et al., 1998b; Pallot, 2003).

9. CONCLUSION AND DISCUSSION

By introducing several regulations from 1999 to 2012, the Indonesian Government has introduced formal regulations and systems which can be identified with elements of NPFM. However, the reform lacks consistency between the upper and the lower level regulations. The lower levels should relate and refer to the upper ones. The situation means that NPFM in Indonesia does not comply with generally accepted theoretical (normative) precepts of the public sector.

General Service Providers (GSP), with 'quango' like status are not awarded flexibility like those in the private sector. Inflexibility subdues competition among government agencies in providing the best service to customers. Failure to create a 'quango' may mean government service agencies cannot be isolated from political influence. Because of these difficulties, the market-oriented system is difficult to implement in Indonesia.

Indonesia still adopts a line-item and incremental budgeting system, although formally, the State Finance Law 17/2003 states that Indonesia should have adopted performance budgeting system since 2004. However, because lower level regulations which detail the Law are inconsistent with the stipulations stated on the Law, the line-item and incremental budgeting system continues.

In developing a financial reporting system, the Indonesian government adopted the full-accrual-based method as a basis to prepare government financial reports. Adopting the-full-accrual method is intended to fulfil governments' responsibility to be accountable and transparent. This does not comply with NPFM's generally accepted precept which states that adoption should be useful for management decision making. Another weakness in developing a financial reporting system is adoption of a rules-based system. The system may create inflexibility for government officers in managing government agencies. The rules-based system is a practice which is intended to be discarded by public sector reforms (Hood and Peters, 2004; Osborne and Gaebler, 1992). This creates a 'paradoxical effect'.

Indonesia's adoption of NPFM like reforms has taken a confusing path. Research to is needed to help Indonesia overcome this confusion aimed at the construction of an alternative framework underpinning the Indonesian reforms. also It may also examine the possibility that these confusions are unintended consequences because the Indonesian government has misinterpreted the meaning of NPM principles.

Second, this confusion does not mean that the Indonesian reforms have failed. This article does not intend to evaluate the degree of success or otherwise of public sector reforms in Indonesia. This is difficult to establish because (i) the evaluation depends on the individual context and stakeholders' viewpoint (Bowerman, 1998); (ii) it need a consensus to determine a result, in term of meaning and terms, which is used to measure the degree of success (or failure); (iii) the direct relationship between efforts (reforms) to outcome (output) is ambiguous and disputable; (iv) there is time uncertainty regarding impacts of public sector reforms and (affected) organisations or society (Pollitt and Bouckaert, 2011). Furthermore, the functionalism perspective, which considers benefits of public sector reform, in term of efficiency and effectiveness, is not the only method to measure success and failure of such reforms. Motives to conduct the reforms may not intend to achieve such benefits. Pollitt (Pollitt, 2001b) proposes institutional theory to examine alternative motives that drive a particular public sector reforms. This may be the subject of future research.

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