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Budget Reporting in Local Government: Problem or Solution?

Budgeting practice in Victorian local government has been criticised by the ICAA, which has developed a standardised budgeting model. The Victorian government has prescribed standardised financial and budget reporting following a decade of reform in the public sector. This paper examines whether the criticism of local government budgeting is valid, and whether standardised models are appropriate, particularly in the context of ambiguous outcomes and lack of input-output relationships, criticism of the adoption of accrual accounting in the public sector, and a focus on the implementation of a flexible best-value regime designed to suit local conditions.

In 2001 the Institute of Chartered Accountants in Australia (ICAA) undertook a survey of local government budgets in Victoria. Budgets are generally held to be an essential element of a council's financial management and control system, but the ICAA concluded in its report that:

- the quality and content of Victorian council budgets is variable but generally poor, indicating that the sector has not effectively embraced the notion of accountability. Financial projections are based on outdated methods which incorporate revenue and expenditure measurement techniques which do not comply with generally accepted accounting principles and are therefore inconsistent with annual financial reporting;
- budgets are not used to convey important messages to stakeholders;
- budgets do not convey clear messages to the reader and use little innovation in presenting information;
- budgets contain large volumes of irrelevant detail;
- budgets do not have linkages to corporate (long-term, strategic) and business (annual operating) plans;
- budgets are short-term in focus and do not address the longer-term issues of financial management and strategy;
- budgets do not focus on balance-sheet issues; and
- the outdated "rate determination" basis of budgets is now irrelevant to councils. (ICAA 2001. p. 19).

In an attempt to overcome the perceived weaknesses in local government budget preparation and financial management, the ICAA in 2003 issued a set of guidelines and a model budget to guide Victorian local governments. Updates in 2004 and 2005 ensured that changes to Victorian legislation and regulations — Local Government (Best Value Principles) Act 1999, Local Government (Democratic Reform) Act

2003, Local Government (Finance and Reporting) Regulations 2004 — were incorporated into the model. The question arises of why, today, local governments still require this level of assistance to prepare reports which are considered basic to good financial management. Why, given a decade and more of change designed to bring local government into line with modern business practices, do Victorian local governments still require assistance with something as basic as budget preparation? Do explanations lie in the differences between public and private sectors, to the extent that business-sector-derived practices ignore and threaten some important features of local government budgeting practice? Have managers in local government chosen to use budget technologies which provide useful information for managing in the sector, even though this may appear to those versed in the private sector to be inappropriate?

VICTORIAN LOCAL GOVERNMENT

Local government in Australia is controlled by the individual state governments, and must comply with specific legislation in each state. Without responsibility for education, health and housing, local governments in Australia have a minor role compared with those in other countries such as the UK. However, local governments do play an important role in providing micro-economic infrastructure and social services for their communities, with expenditure representing 2.3% of GDP in 2002/03 (LGNR 2005). Local government has four sources of revenue: charges for services, rate revenue, general grants from the federal and state governments either direct to local governing bodies or through the Grants Commission, and specific-purpose grants such as those for road construction. Revenue sources determined by individual councils are charges and rates, but the reforms discussed in this paper have limited the councils' ability to determine rates and charges. In 2002/03, rates revenue was only 45% of the total revenue raised by local government in Victoria (LGNR 2005). This percentage is not consistent throughout the state: urban councils have a higher reliance on rate revenue, while rural councils have a lower reliance, being eligible for higher levels of state and federal grants and subsidies.

THE VICTORIAN STATE GOVERNMENT IN POWER OVER MOST OF THE 1990s BELIEVED IN SLIMMING DOWN "OUTSIZE" GOVERNMENT AND IN MICROECONOMIC REFORM.

The characteristics of local governments vary widely. Local governments include those located in older suburban areas, those in newer outer suburban areas, those in outer suburban and semi-rural areas, purely rural areas, remote areas and regional cities and towns. Their populations range from very wealthy to lower socio-economic groups and those suffering extreme hardship in rural areas hit by drought. The needs of the local communities in these widely varying councils also vary widely, requiring different services with different emphases. For example, in some communities, English and two or three other languages are the medium of communication; in others more than 50 languages in the local community may require vast amounts of translation and publication.

One of the imperatives for change in all levels of government in the 1990s was the ideological position that the private sector is more efficient and effective than the public sector. The private sector is seen as using better management practices, such as accrual accounting, and driving down the cost of services by focusing on profit. This is the underlying premise of the New Public Management (NPM). The academic and the professional literatures include abundant articles and journals with special editions devoted to NPM and the New Public Financial Management. The Victorian state government in power over most of the 1990s believed in slimming down "outsize" government and in microeconomic reform (Hood 1995). The market model was adopted in which competition and quasi-markets are introduced into contracts between the public sector and private sector suppliers (Guthrie *et al* 2003). The driving force was cost, and the emphasis was on small government.

Hood (1995) proposed that public-sector reform is dependent on motive and opportunity. In Victoria, both motive and opportunity were present. The then government's stated ***motive*** was resource savings, creating a local-government sector which was smaller and more efficient than before. It was expected that creating fiscal stress by cutting rates and imposing rate caps in local government would lead to resource savings, better performance and the adoption of better management practices. In contrast, other authors note that the problems of government will not be solved by "spending more or spending less"

(Osborne and Gaebler 1993, p. xviii). The state government also had the *opportunity*. It had defeated a demoralised and incapacitated government to come to power in a landslide, and comfortably retained power at the following election. It believed it had a mandate for extensive public-sector reform. However, while the state government could and did force changes in some areas such as the accounting regulations and adoption of AAS 27 *Financial Reporting by Local Governments*, it could only encourage, not force, the adoption of other internal management processes and practices (Van Helden 2000, Kloot and Martin 2002). The internal practice of budgeting, which appears not to have changed, is the subject of this paper.

VICTORIAN LOCAL GOVERNMENT CHANGES 1990–2004

The changes experienced by Victorian local governments are arguably the most significant in any public sector in Australia. The overriding aim of the reforms imposed on local governments has been to improve microeconomic efficiency and sector effectiveness. In 1991, the Municipal Accounting Regulations were updated. The previous regulations were highly prescriptive and did not allow for modern business practices; for example, six pages of detailed regulations explained how to bank money received, but did not allow for EFT or credit card payments. The new regulations were much more in keeping with modern accounting, business and management practices. They were far less prescriptive, allowing for decisions to be made by professionals within councils. In 1992/93, AAS 27 became operative, further modernising the accounting practices used in local government and bringing them much closer to private-sector practices. In reports published by the Office for Local Government using annual report data (among other data sources), local governments were "benchmarked" across a number of categories which used annual report data. Much of this data was not really comparable, as different local authorities used different classifications for revenues and expenses. In addition, geographic and socio-economic differences were inadequately factored into the comparisons. However, the reports were used as a catalyst for substantial further change.

In 1994/95, following a change of state government, several significant structural changes were introduced. First, following a round of compulsory amalgamations resulting in fewer but larger councils (210 local governments were reduced to 78), rates were cut (by about 10%) and capped by the state. This placed many councils under fiscal stress. They could no longer simply increase rates at their discretion to pay for the services needed by their communities. Moreover, they needed to find savings simply to stand still, due to the mandated rate revenue cuts. The fiscal stress was designed to encourage councils to become more efficient and use more business-like practices in managing their organisations.

These changes were followed by the introduction of compulsory competitive tendering (CCT), which placed further fiscal stress on councils as they worked hard to develop the expertise and processes necessary for the successful implementation of CCT. The objective of CCT was to make councils more efficient in their operations by having them compete with the private sector for the right to supply services in line with councils' service objectives. CCT required that 50% of accrual expenses were to be put to tender. If accruals such as depreciation were high, close to 100% of cash expenditure had to be subjected to tender in some councils. The state government had not finished, however. It introduced a much more rigorous form of compulsory benchmarking, through a series of surveys and analyses which were then reported to local government CEOs, who needed to explain and improve their relative performance. These surveys included the Community Satisfaction Measurement Program, in which councils were compared in a number of dimensions, some of which were not readily comparable given different socio-economic and geographic locations. Smaller reforms included the requirement for all local governments to produce corporate or strategic plans, and to prepare annual reports for their ratepayers.

All of these changes were taking place against a background of significant change in both the state and federal government sectors. In the Victorian state government sector, there was a strong emphasis on privatisation and corporatisation, aimed at improving internal efficiencies. For example, the power industry, previously a state government monopoly, was split into smaller units and sold to the private sector. The public transport industry was also franchised to private operators.[1] The water supply was corporatised, but not fully privatised. At the federal level, examples of sales to private interests include the national airline, airports, part of the major telecommunications business, and the commonwealth employment centre.

Following another change of state government in 1998, best value was mandated in place of CCT (Local Government (Best Value Principles) Act 1999). Best value requires that councils choose suppliers not only on the basis of cost (the resource efficiency premise underlying CCT), but also on the basis of achieving community outcomes specific to the needs of the local community. Under best value, considerations of public interest should be taken into account in decisions relating to outsourcing and service provision (Guthrie *et al* 1999). Best value essentially requires that services be delivered to clear standards of cost (similar to CCT) and quality (as determined by community consultation).

In 2003 the Victorian government amended the local government act (Local Government Democratic Reform Act) to include standardised financial reporting to improve accountability of local government and transparency of decision-making. Accounting has been seen as an important mechanism which can strengthen processes of democratic governance (Johnsen and Lapsley 2005). The 2003 act further entrenched accrual accounting, and mandated financial management practices similar to those which apply in the state government. Standardised reporting practices have been adopted for most areas of state government,[2] and are consistent with a renewed focus on governance and accountability in both the public and private sectors. These changes mirror those introduced at federal level in Australia. Through the associated Local Government (Finance and Reporting) Regulations of 2004 the state government requires local governments to prepare a set of standardised financial reports. Strategic-level financial plans, detailed budgets and annual reports for the previous year are prepared as standardised statements in standard formats. To be consistent with these new state government requirements, the ICAA amended its model budget in the 2005 version.

Interestingly, the focus by the Victorian state government on standardised reporting by local government to enhance comparability and benchmarking is in conflict with its focus on best value. If best value is designed to enhance local autonomy and focus on important outcomes specific to local areas, the insistence on a standardised reporting format appears to be designed to enhance centralised control by the state. Standardised reporting also mitigates the development of financial (and other) management practices specific to the circumstances of individual councils. Collecting and analysing "comparative" data across councils may be intended to communicate best practice (Bowerman *et al* 2001) but it may also distort the position of councils with different socio-economic and geographic environments. Under the best-value regime, it would be expected that councils would develop services that reflect the needs of their communities, and they are required to develop service plans in consultation with local communities. It could thus be expected that the different services and dimensions which develop in different local councils would give rise to differences in reporting, but there is no place for such differences in the standardised reports.

FINANCIAL REPORTING AND MANAGEMENT CHANGES

Financial reporting has been the focus of much of the NPM reform in Australia. The adoption of accrual accounting has been seen by some as a panacea to increase transparency and accountability in the public sector. However, there is research to suggest that accountability will be enhanced by the attitudes of public-sector managers, not just financial reporting (Kloot and Martin 2001, Sinclair 1995). In addition, there has been substantial disquiet over the wholesale introduction of accrual accounting into the public sector (Barton 2000, Carlin 2005, Carnegie and Wolnizer 1997, Guthrie 1998, Guthrie *et al* 2003). There is a large body of literature on the benefits and costs of accrual accounting in the public sector.

Carlin (2005, p. 314) notes that accrual accounting in the public sector is held by its proponents to be useful in enhancing accountability and transparency, in driving greater organisational performance through improved resource allocation, and in identifying the full cost of government activities, again leading to greater efficiency and better resource allocation and performance. Those who argue for the use of accrual accounting in the public sector also contend that accounting is sector-neutral — there should be no difference between the public and private sectors (Newberry 2001). The opposing argument is that the public sector is not the same as the private sector. It has public-interest responsibilities and community-service obligations which are by their nature loss-making. They are thus not amenable to private-sector reporting practices which focus on profits. In addition, financial structure is not relevant (gearing is not an indicator of vulnerability), solvency is not relevant (the parliament can appropriate moneys) and the capacity for adaptation is not relevant (the ability to sell assets is limited) (Guthrie 1998, p. 5). Public-sector accrual accounting reports are also seen as misleading (Carlin 2005) and some authors note that business accounting is rife with problems which cause financial misallocation of private-sector resources, so it should not be expected that accrual accounting in the public sector will be immune from these problems (Guthrie 1998).

There is also some evidence that a lack of rigour in defining community-interest outcomes, combined with a propensity to insert cash figures into accrual accounts, raises doubts about whether the reports are appropriate tools for management purposes (Carlin and Guthrie 2001a, 2001b). Financial management, as opposed to financial reporting, is thus not necessarily enhanced by accounting reforms implemented to date.

While the debate continues over the appropriateness of private-sector accounting standards for the public sector, local governments need to use the current accounting standards in place for more than a decade under AAS 27, and interpret them as best they can in reporting to the state government and to ratepayers. The ICAA's initial research in 2001 pre-supposed that the use of accrual accounting reports in the budgeting process is a superior technology, despite the misgivings of many authors. Given the many concerns raised about the uncritical adoption of accrual accounting in the public sector, it is notable that there is some evidence that the federal government is moving away from a total reliance on accrual accounting (Guthrie *et al* 2003). History may thus record that many local governments, by not adopting accrual accounting as a basis for budgeting, achieved better outcomes for their communities than those that did adopt it.

Newberry (2004) contends that the use of private-sector accounting practices in the public sector is driven by an accounting profession which claims that accounting is sector-neutral when it is not. She suggests that large accounting firms (whose principals are often members of ICAA) have had a major impact on introducing private-sector biases such as efficiency into a public sector which should lean towards social and welfare obligations. Christensen (2005, p. 447) provides further evidence of the non-trivial role of management consultants such as the large accounting firms as change agents, bringing public-sector practices into line with private-sector practices as an inherently "righteous objective". Throughout the long period of change affecting local government, consultants were employed by individual councils and by peak bodies such as the Municipal Association of Victoria and the Local Government Managers Association to instruct, develop new systems and processes and generally guide local governments through the changes. In addition, after the restructures, many of the new, larger councils had hired accountants[3] and managers with private-sector expertise. The combined result of the changes and influx of managers and staff with private-sector expertise could have been expected to bring a new perspective to the management practices of local governments, including practices such as the use of budgeting as a tool for planning and control.

To assist local governments to meet state government requirements for financial management and reporting, the ICAA developed its 106-page (2005 version) model budget, which includes model budgets in financial terms, model financial reports, detailed model commentaries and model analyses of the budgets, along with a model executive summary, a glossary of terms, and a model strategic planning framework. The model budget is essentially a template of the state government requirements, updated to include 2003 and 2004 legislation and regulations, with a raft of "how to" instructions. If the ICAA research and models are taken as a guide to more general management practices, the extensive changes in the local-government sector, resulting in many different structures, processes and practices, appear not to have impacted on one of the most basic management tools in any meaningful way for a number of local governments. However, if the sector now has accountants and managers who have the expertise to prepare budgets according to the ICAA's standards, is there another explanation? We contend it may be that managers are consciously choosing to use different techniques.

In contrast to the ICAA findings of poor budgeting practices, other research suggests there has been substantial change in some aspects of management practices in Victorian local government. Kloot and Martin (2002) demonstrate that there has been significantly more adoption of modern management practices in Victoria than in states which have not been subject to the same reform agenda. In other research, Kloot and Martin (2001) demonstrate significant feelings of accountability to the community by managers in local government. Local government managers perceive accountability as broad, not limited to financial and/or budget accountability, and owed to multiple stakeholders, echoing Sinclair's 1995 findings.

The model budgets published in 2003–05 also rely on accrual accounting techniques, although the budget could be seen as a management accounting technology rather than a financial reporting technology. It is likely that budgets used for internal purposes in ambiguous and ill-defined environments such as local government would not be tightly linked to financial reporting objectives. There can be a world of difference between practices adopted to manage internal and external reporting systems — a current example is the balanced scorecard of Kaplan and Norton (1996). Reporting social indicators, if they can be developed for ambiguous environments, may be far more relevant for local government reports than a string of accrual accounting indicators.

THE PURPOSE AND PRACTICE OF BUDGETS IN LOCAL GOVERNMENT

Kloot *et al* (1999) explain that budgets authorise expenditure by local government officers: once the budget is adopted by council, officers may spend on items contained in the budget up to the authorised limits. In the past, budgets determined the rate revenue to be raised. In the current climate, however, the budget is no longer the major determinant of the rate revenue required, but is only one input into that decision. Expenditure budgets are adjusted to be consistent with the revenue limits determined by state government policy and funding. Budgets are also a performance reporting device for the state Office of Local Government (specified by the Local Government Finance and Reporting Regulations 2004). In management terms, budgets provide a means of achieving control over activities, a means of coordination of operations, and a device to communicate expectations to employees and other interested parties.

These functions are consistent with those recommended in the 2004 "Research Report on Budget Reporting" by IFAC's Public Sector Committee. IFAC suggests that a budget report should provide financial transparency, a major contributor to good governance and accountability. A budget report should also provide authorisation of spending through approval by the legislature (the council in local government) and serve as a key tool for financial management and control. OECD (2000) principles for financial management and control suggest that budgets are used to assist in the control of aggregate spending and debt, to facilitate strategic prioritisation of expenditures, and to encourage better use of resources to achieve outcomes and produce outputs at the lowest possible cost. The OECD principles are consistent with the notion of budgeting as an internal management technology, not just an external reporting device.

It is not always easy to demonstrate that budgets achieve their purposes. For example, despite the focus on better financial management, and a new focus on risk management (Guthrie *et al* 2003), local governments have apparently been slow to implement changed internal management processes. In some cases, councils apparently satisfy the reporting purpose and requirements, but do not adopt the internal management practices which are usually thought to underpin such reports, and which would achieve control and coordination. For example, Kloot *et al* (1999) report on corporate[4] planning processes: "The minister wanted a corporate plan by April 1995 so we took an old one, changed the heading and dressed it up a bit and gave it to him." The preparation of corporate plans to be sent to the minister is compulsory, but clearly not all local governments subsequently use corporate plans in planning and managing their activities and operations. Some develop business plans, which are the annual operating plans, quite separate from corporate plans, which are the long-term strategic plans. In the normative literature, annual business plans are derived from the strategic plan. In Kloot *et al* (1999), it was perceived that in local government there was a need for tighter links between corporate and business plans. The ICAA research indicates that this was still the case in 2001.

One of the stated aims of the ICAA model budget is to show how a budget should be driven by the strategic planning framework (ICAA 2005, p. ii) and forms part of the long-term financial plan for strategic resource management. In 1999 councils did not fully utilise the benefits of corporate planning because of a lack of management accounting expertise (Kloot *et al* 1999).[5] Organisational ability was lacking, in both personnel ability and technical ability (Andrews 2004). Council staff did not have the skills and knowledge to undertake complex financial modelling and budgeting needed for business planning. However, as noted above, hiring and the use of consultants disseminated knowledge and skills in the sector. If there is the expertise and knowledge to prepare budgets which serve as useful management and reporting tools, then managers in local government may be making other choices by using different budgeting techniques.

From another perspective, for many years budgeting was a highly political process and also an incremental process. Over several decades, once an item was in the budget, it was often there for the foreseeable future. There was also an expectation that if there was an expenditure blow-out, rates could relatively easily be increased to cover the excess expenditure. These practices have since been modified (Kloot and Martin 2002). While budgeting is still, and probably will always be, a political process, fiscal stress and new service requirements have resulted in incrementalism no longer predominating. However, there may well be local government employees who maintain the old practices in smaller councils with fewer resources to spend on staff training. The problems of both political and managerial acceptance (Andrews 2004) of more rigorous evaluations of services have largely been resolved, but again there may be limited adherence to old practices. Councils, through their best-value processes, question expenditures and processes before finalising their budgets. In addition, simply increasing rates to meet expenditure blow-outs is no longer feasible in most councils. Expenditure has to be much better managed to prevent blow-outs as far as possible, or by moving resources from one service to another if there is an unavoidable cost increase in a specific area. Kloot *et al* (1999) found some evidence that budgets would be changed *ex post* to remove variances, another practice which needed to be changed if budgets were to be treated as serious operating technologies, and again this has largely been eliminated through hiring better qualified staff. However, there may still be some retention of these past poor practices which result in the problems described by the ICAA's 2001 report.

Financial stringency was imposed by the state government, following which it was expected that the budgeting functions of financial management and control, and coordination, would assume greater importance. Practices which would improve financial management could reasonably be expected to be implemented. This was clearly the government's intention in imposing the controls. However, fiscal stress does not necessarily lead to change in entrenched management practices (Van Helden 2000). Given the parlous financial state of many councils with rate caps and cuts, it could have been thought that Victorian councils would seek out "better" practices. The amalgamations of these financially weakened local governments in Victoria, which created larger units with stronger rate bases, may however have mediated the immediacy of financial failure, and with it the urgency to change. On the other hand, it may be that councils *are* changing (Kloot and Martin 2002) to adopt practices to reduce the threat of financial failure and better manage financial risk.

The findings of Van Helden (1998) suggest that the application of NPM at state level should encourage the implementation of modern budgetary practices, as the expertise and philosophy flow from the centre to the councils. Certainly, the state government has increased its control and monitoring of local government. It requires much more local consultation and local reporting, and at the same time has increased the quantum and quality required of local government reports to the state department which monitors local government.

Despite the changes detailed above, it seems that local government has yet to change its budgeting practices to those thought to be best practice by proponents of private-sector models. This may be due to the requisite expertise not yet permeating local government in general terms, or there may be other influences on the use of private-sector budgeting practices in the public sector.

In 2001, the ICAA was concerned that budgets use revenue and expenditure measurement techniques that do not comply with GAAP. However, local governments, in common with other public-sector organisations, have problems in measuring the relationships between revenue, expenditure and outcomes. The measurability of outcomes in government remains questionable, despite many attempts at technical advancement. Performance indicators may be available for some activities, but others require social indicators (Seal 2003) and these are much less amenable to measurement. Even the objectives of some activities may not be easily definable. Hofstede (1981) suggests that where activities are routine and mechanistic, and outputs are measurable, a cybernetic model of control is appropriate. In cybernetic control models, a simple comparison of actual performance against budgeted performance leads to either continuing in the same mode (the actual performance was close to target) or reworking the plans and/or the practices (the actual performance was not close to target). According to Carlin and Guthrie (2001), proponents of NPM argue that there is a causal relationship between current and subsequent performance. In such situations, budgeting as applied in the private sector is certainly appropriate. However, where outputs are non-measurable, non-routine, ill-defined or ambiguous, non-cybernetic or political models of control are necessary (Hofstede 1981, Kloot 1997, Seal 2003). Budgeting systems as proposed by ICAA are largely creatures of cybernetic control models, and would not be the major control element in ambiguous environments such as local government. Carlin (2003) reports on research which shows serious deficiencies in defining outputs and outcomes in accrual output-based budgeting (AOBB) systems, detracting from the credibility of expectations of performance improvement through using AOBB.

It has been noted that local government budgets are not necessarily linked to financial reporting; it is possible to report on budget outcomes without using a strict financial reporting framework. Budget reports can consist of *ex-ante* budgets at the start of the period, and *ex-post* reports comparing the actual outcomes to the adopted budget outcomes. For internal management reporting purposes, such reports do not need to be linked to a financial reporting framework, as budgets may be much more operational or physical in nature than financial. The budgets may be cash-based around physical aspects of operations, and not focused on financial reporting results (income statement and balance sheet) except at the highest level.

Local governments can be criticised for the use of cash budgeting rather than budgets based on accrual accounting, but this is not necessarily valid criticism. Guthrie (1998) notes the paradox in measuring cost in inflated accrual terms while allocating cash resources, regardless of whether the budget is in accrual or cash terms. Cash is the resource allocated, so accrual budgeting will not increase accountability as it is not cash and thus outcomes will be different to budget — cash — resources allocated. IFAC (2004) suggests that it is possible to retain the cash or near-cash basis for budgetary control and use the accrual basis for preparation of the general purpose financial reports (p. 13). IFAC suggests that cash as a basis for budget preparation is retained by many jurisdictions because cash information is more readily available, cash systems are simpler to implement and costs are lower because of the lower level of accounting skills required. IFAC notes, however, that inconsistency between accrual accounting reports and cash-based budgeting can confuse the readers of the financial statements. The report notes that accrual-based budgeting may be adopted when accrual reporting is in use to increase consistency of overall reporting.

While the state government is requiring councils to report detailed budgets, there is criticism that budgets contain too much irrelevant detail. Although this criticism may be justified from the point of view of a non-expert user wanting to ascertain general trends, the detail may be necessary for managers attempting to achieve the council's objectives. Indeed, IFAC (2004) recommends that the budget needs to be comprehensive, and governmental activities should encompass all of the expenditures by government for all budget-dependent entities. Thus, the IFAC recommendations may be in direct conflict with recommendations to reduce the detail, a conflict not easily resolved.

The short-term focus of budgets in many local governments has been criticised, and we agree that a budget should be linked to the long-term strategy of the individual council. However, we question whether a long-term focus for an annual budget is realistic. Professional accounting journals such as ***Financial Management*** (CIMA) have published articles suggesting that setting long-term budgets can be harmful for organisations, as budgets reduce an organisation's flexibility and ability to respond to rapid changes in its environment. Local councils may in fact be more responsive to changes in their local communities if their budgets are more short-term than long-term, provided they are prepared in the context of a strategic plan. There is an inherent dilemma in the choice between long-term or short-term budgeting. It can be argued that budgets, as part of a government financial management system, should facilitate strategic prioritisation of expenditures across policies, programs and projects for allocative efficiency and equity (OECD 2000). This perspective of financial management goes beyond the annual budget cycle. Policy, planning and budgeting need to be linked in a medium-term framework (IFAC 2004). Such a view supports the ICAA position that budgets are deficient in having a short-term focus. Further, the criticism that budgets are not linked to business and corporate plans constitutes a worrying continuation of past problems in local government budgeting.

An important purpose of budgeting is to communicate and convey important messages to stakeholders. This raises questions of which stakeholders, and whether there are other techniques to convey the messages. Budgets do convey important messages about operating decisions to managers and staff, and about authorised expenditure for these stakeholders. Budgets also convey important messages about local government spending to ratepayers and others. The 2005 ICAA model budget notes that readers not trained in financial management should be able to gain an understanding of the council's financial planning strategies. We contend that there are other more relevant and useful ways to convey important messages to external stakeholders such as the local community. For example, a report by the Victorian Best Value Commission (2002) determined that best value, with its focus on community consultation, is seen as non-prescriptive and flexible. It is seen as encouraging a culture of local responsibility and focusing on local employment options, particularly in rural and regional areas. Further, best value is reportedly a management tool consistent with best practice and continuous improvement, which allows for alignment with corporate strategy. The process of community consultation in itself conveys many messages to the local community. The Best Value Commission noted that while levels of community consultation varied in scope and implementation, in all cases there is room for feedback to the community. The budget may or may not be a major part of the feedback provided for the community.

The thrust of the Best Value Commission's comments is on local responsibility and accountability. The commission's favourable report on best value's early implementation suggests that councils are performing satisfactorily across a number of dimensions, including costs and by implication budgeting. This is in contrast to the prescriptive model-budget approach. The 2003/04 Victorian local government legislation focusing on standardisation and prescription for financial reporting is also at odds with the commission's report. Mandating standardised practices and reporting for all seems a heavy-handed approach to "improving" the practices of a few.

CONCLUSION

The widely varying characteristics of local government suggest that there is room for individual councils to choose from a variety of budgeting practices. Without an analysis of the needs of different types of local councils, industry-wide prescriptions cannot be made with any confidence in their overall applicability. There is a need to balance efficiency and effectiveness outcomes to achieve best value for differing local communities and this may not be achieved by prescriptive, private-sector practices. Local governments may indeed be acting in the best interests of their communities in using individual technologies to prepare budgets to best suit their own environments, rather than using a standardised "one size fits all" model of budget preparation. There is in fact little evidence to suggest that the current practices are not serving local communities.

Local government bodies have largely emerged from the detailed and highly prescriptive procedures of the past to a regime where they have the authority to provide for the good governance of their local communities. Good governance lies in satisfying the needs of the local community in a transparent and accountable manner with a high degree of probity. There are no longer standard services and requirements on local governments: each decides what is in its community's interest and will undertake to deliver appropriate services as long as these are not expressly prohibited by legislation. In this environment, standardised reporting and prescriptive model budgets and financial reports appear to be turning back the clock and taking away from the emphasis on local governance and competence.

Future research could examine what drives budgeting practices and how they relate to the strategic and operational framework of individual councils. There is a need to know not only what is being done — the ICAA's focus in 2001 — but also why it is being done. Research could focus on the outcomes from different budget technologies, the expectations of local communities, and any disconnect between the two. Practices which appear to those focused on a private-sector accounting regime to be wrong may in fact be appropriate for specific local conditions and circumstances. The ICAA's model budget can be a learning tool for local governments, but it should be seen as only part of a wider package of options from which each local government can choose those that best allow it to serve its local community.

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NOTES

1 In 2004 it was recognised that some of these privatisations had failed. One of the private train and tram operators walked away from its investment, leaving the government to operate its trains and trams. The trains and trams were subsequently taken over by the remaining private operator. One of the private power generators was close to bankruptcy, and power shortages are still predicted as possible in the near future.

2 For example, the health networks are required to report using standardised practices and categories even if the categories do not apply; eg, dental services do not have the same operational requirements as major teaching hospitals but are required to report using the same categories.

3 Not all councils employed even one qualified accountant before the 1994/95 reforms. One council, a $70 million enterprise, had not employed a qualified accountant until early 1996.

4 In local government, strategic plans are often called corporate plans as strategic plans are historically land-use plans.

5 A later study by Kloot and Martin (2002) found an increase in the use of modern management practices.

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Two articles published in *Australian Accounting Review* have been recognised in the results of the International Federation of Accountants' Professional Accountants in Business (PAIB) 2006 Articles of Merit Award Competition. "Performance Measures in Supply Chains", by Kim Langfield-Smith and David Smith (*AAR* 15, 1: 39–51) was selected as the winning article in the competition and "A Case Study on Organisational Performance Measurement Systems for Customer Intimacy", by Suresh Cuganesan (*AAR* 15, 1: 52–60) was judged to be an article of outstanding merit.

The two articles are among ten judged to be of outstanding merit and which are published in the PAIB 2006 *Articles of Merit* booklet (available on the IFAC website — www.ifac.org).

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