

The Presentation Formats of Malaysian Local Authorities' Financial Statements

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Abstract - Malaysian local authorities play a crucial role in providing services to the community. However, the performance of local authorities has been subjected to various criticisms which include poor services rendered to the locals and the inefficiency of local authorities' management¹. Malaysia is experiencing rapid development with a vision of becoming a fully developed nation by 2020. In order to achieve this, an efficient financial management system is required in all government agencies including the local authorities. The efficiency depends on the effectiveness of the financial management and the quality and reliability of the financial reports prepared. A study was carried out to compare the formats of financial statements adopted from 2004 to 2008. 75 local authorities (out of 96 local authorities in West Malaysia) responded by sending their audited financial statements. The trend analysis revealed that the local authorities were not consistent in the formats adopted.

Index Terms - Local authorities, public sector accounting, financial reporting analysis, accounting transformation, Malaysia.

1. Introduction

The Malaysian administrative system is divided into three major levels of hierarchy: Federal Government; State Government; and Local Government (Local Authority). Although the Local Authorities are the lowest in the Government hierarchy, they are very close to the community. Thus, the Local Authorities need to be efficient in managing its financial situation and continuously improve its financial efficiency as a commonly desired goal. The efficiency of the financial management system depends on effective financial management and the quality and reliability of the financial reports prepared by the organisation.

Local authorities in Malaysia serve as an important mechanism to further the policies and to facilitate the implementation of relevant strategies and programmes of the Federal and State Governments². The audited financial reports of the local authorities are the means for the local authorities in determining their accountability to their stakeholders³. The audited financial statements included in the report provide a wealth of information to anyone with an interest in the government's economic condition⁴.

In recent years the media has taken an active role in highlighting many issues that concerned the public interest, which demand the local authorities to be more accountable. A study indicated that Malaysia's Local Authorities financial position is weak because they are not able to acquire additional revenue to provide services demanded by the

community. Consistent with the study, public has now raised the issues in the newspapers questioning Local Authorities financial management and the uses of the public funds⁵.

Prior study had identified that the local authorities in Malaysia are primarily practicing four Accounting Standards: International Accounting Standards (IAS); guidance issued by the Ministry of Housing and Local Government; self created accounting practices; and Federal Treasury Circular. This led to inconsistency in the presentation of the financial statements which makes it difficult to make comparison between local authorities⁶.

The purpose of this study is to find out whether this practice still exists in the local authorities. Thus, the specific objective of the study is to compare financial statements format adopted by the local authorities from 2004 to 2008

2. Methodology

A total of 75 local authorities had responded to the researchers' request by sending their Audited Financial Statements for the year ended 2004, 2005, 2006, 2007 and 2008 (see Table 1) with a total of 375 audited financial statements being submitted for analysis.

Table 1: Number of local authorities responded

STATES	TOTAL NO.	NO. RECEIVED
Johor	14	8
Kedah	11	11
Kelantan	12	10
Melaka	3	2
Negeri Sembilan	8	2
Pahang	11	11
Pulau Pinang	2	1
Perak	15	10
Perlis	1	1
Selangor	12	12
Terengganu	7	7
	96	75

Analyses of financial statements were carried out with a focus on the Statements of the Financial Position and

Statements of the Financial Performance. Format of the Statements of the Financial Position and the Statements of the Financial Performance were analysed according to their presentation. There is no specific requirement for the local authorities' financial statements to be presented in certain format. The analysis of format would determine whether there is any uniformity in their presentation of financial statements.

This research draws on Luder⁷ contingency model of accounting change when interpreting what happened in Malaysian Local Authorities between 2004 and 2008. This model is 'an extension of the classical contingency theoretical approach to variables of collective behaviour'⁸, the basic purpose of which is 'to explain why governmental accounting innovations took place in some countries and not in others'⁹.

3. Framework for Analysis

A. Luder's Model Of Governmental Accounting Change

The subject of the model is the transition process linking two conceptually different accounting systems to each other, and how the contextual situation affects this transition process. Luder remarked that. Even though the countries studied by showed that it is information needed that determines the

appropriate accounting system, environmental factors might also affect the possibility and speed of changing the existing accounting system.

The contextual variables (independent variables) may be classified, according to their functions in the innovation process, into three categories: 'stimuli'; structural variables; and implementation barriers (see Fig 3.1). Stimuli are events which occur at the initial stage of the innovation process⁷. These events 'create a need for improved information on the part of the users of accounting information and increase the producers' readiness to supply such information' (p108)⁷. The structural variables consist of characteristics of the social environment (which are structural variables external to the government) and characteristics of the politico-administrative system (which are internal structural variables). These structural variables influence the basic attitudes of users and producers of information towards improved public sector accounting information. The implementation barriers are environmental situations that prevent the implementation of the innovation process, thus hindering the creation of an improved accounting system which is in principle desirable.

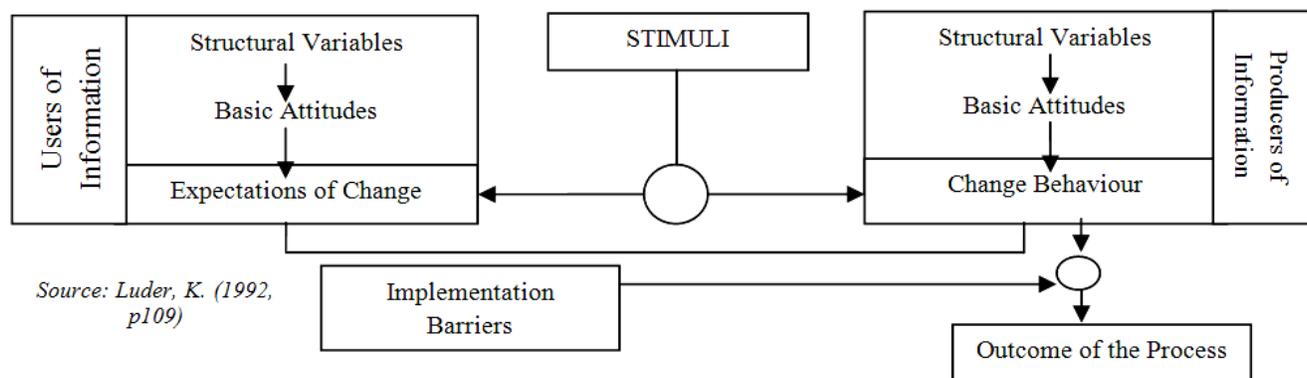


Fig 3.1: Contingency model of public sector accounting innovations

The behavioral variables are divided into two categories: the expectation of change from users of information; and the change of behavior from the producers of information. The users' expectations of changes are influenced by two factors: their basic attitudes; and the stimuli that exist at the beginning of the change. These two factors also affect the willingness of producers of information to make changes.

The dependent variable in this framework is the 'conceptually different accounting system' adopted (p3)⁸.

The outcome of this variable depends on the situation described above. If there is strong influence for change, then a change or improvement in accounting systems might be achieved. If not, then innovation is less likely to be successful.

4. Analysis of Result

Analysis of Format Presentation

1. Statements of Financial Performance

'No clear rules and regulations spelling out the form and content of the statement of accounts that should be prepared by the local authorities were laid down either before or after the independence of Malaya'(p11)¹⁰. There has been no development in the regulatory reform since then. This study attempts to determine whether in practice there has been any improvement with the local authority presentation of financial statements. The trend analysis revealed that the local authorities were not consistent in the formats adopted and disclosure of information. Table 2 shows there were 6 formats adopted by the local authorities.

Table 2: Formats adopted by local authorities from 2004 to 2008

FORMAT	2004	2005	2006	2007	2008
A	22	22	22	22	24
B	8	6	6	6	5
C	8	10	10	10	9
D	26	26	26	16	16
E	9	9	9	19	19
F	2	2	2	2	2
Total	75	75	75	75	75

Format A and D are the two formats commonly adopted. They are almost similar except that the items of revenue and expenditure are more detailed in Format D.

Table 3: Explanation on the different format of Statement of Financial Performance

FORMAT A	Disclose breakdown of all income and expenditure with notes for each item.
FORMAT B	Disclose total income and total expenditure with notes but no breakdown items in the Statement.
FORMAT C	Disclose the breakdown of income according to the types of revenue: Direct Tax; Indirect Tax; Non-Revenue Receipts; and Grants or Contributions from Government. Breakdown of all expenditures are disclosed. In addition, Development Expenditure is included as operating expenditure, even though disclosed under a separate heading.
FORMAT D	Almost similar to Format A. The difference is that, some of the revenues and expenditures had been grouped and classified under specific headings with notes.
FORMAT E	Almost similar to Format C. The difference is that, the items under the types of Revenue: Direct Tax; Indirect Tax; and Non-Revenue Receipts are grouped under each heading with notes. No item on Grants or Contributions from Government. For expenditure, most of the items had been grouped under specific headings and details are disclosed in the notes.
FORMAT F	Almost similar to Format C. The difference is that, the expenditure on development and capital assets are disclosed and included as part of total expenditure. The statement shows the surplus (if any) being transferred to the <i>Kumpulan Wang Terkumpul</i> or reserves.

It shows that uniformity in presentation is not present. Interviews with some local authorities revealed that the change of format might be due to recommendations by the external auditors or influenced by peers from other local authorities or directives from top management.

When there is no uniformity, comparison between local authorities within a state or among other states is not possible. Though, they are not operating in a competitive environment, comparison between the financial performances of the local authorities would gauge how well the local authorities are fulfilling their objectives. The local authorities can place themselves at par with the other local authorities that are performing well. They can also learn from the mistakes made by other local authorities and improved themselves.

Since there are no accounting standards imposed on them, local authorities adopt modified accrual accounting, modify

according to their needs. Thus, there is a variation in the presentation format of the Statements of Financial Performance. As different treatments were used the problem of comparison among local authorities arises.

Uniformity within states (2004 – 2008)

Table 3 shows that out of 11 states only 5 states have uniformity in adopting the format. (Perlis was excluded as the state has only one local authority). In Kedah 10 out of 11 of the local authorities had moved from different format to Format A in 2008. Thus, all 10 are uniform in presenting the Financial Performance except for Alor Setar City Council that had moved to Format D from Format A.

Selangor is one of the states that had adopted various formats of the Statements of the Financial Performance within the timeframe of 2004 to 2008. As at 2008, five different formats have been adopted: Format A and Format F had been adopted by two local authorities respectively; four local authorities adopted Format B; and Format C and Format D were adopted by two local authorities.

Nevertheless, there are also local authorities within the states that are adopting uniform formats. Local authorities in Johor and Melaka for example are adopting Format A, whereas local authorities in Pahang are adopting Format D, and those in Perak are adopting Format E.

Table 4: Format comparison between states

States	A	B	C	D	E	F
Johor	√					
Kedah	√			√		
Melaka	√					
Negeri Sembilan	√			√		
Pulau Pinang			√			√
Pahang				√		
Terengganu		√	√			
Perak					√	
Kelantan	√				√	
Perlis					√	
Selangor	√	√	√	√		√

Format uniformity among states

Based on Table 4, it can be seen that there is no uniformity among the states in presenting their Statements of the Financial Performance. For example, Johor and Melaka adopted Format A, whereas Perak and Perlis adopted Format E.

Even though local authorities in Johor and Pahang adopted uniform format within their states, comparison between the two states were not possible as Johor adopted Format A whereas Pahang adopted Format D.

II. Statement of Financial Position

In 2004, it was found that there were three types of Statements of Financial Position format adopted by the local authorities. Table 4 shows in 2004 and 2005, 71 local authorities adopted Format A, three local authorities adopted Format B and only one local authority adopted Format C. Nevertheless by 2008, all the 75 local authorities had adopted a uniform format, that is, Format A.

Table 5: Format adopted by the local authorities

FORMAT	2004	2005	2006	2007	2008
A	71	71	73	73	75
B	3	3	2	2	0
C	1	1	0	0	0
TOTAL	75	75	75	75	75

Even though there is no uniformity in the Statements of Financial Performance format, either within the states or among the states, the 75 local authorities tend to be uniform in adopting the Statements of Financial Position format. Unlike the private sector where companies must comply with the Malaysian Financial Reporting Standards, the local authorities do not have such regulations. It is high time that a uniform accounting standard to be enforced to all local authorities.

5. Conclusions

The examination of the statements of the financial position and the financial performance of the local authorities showed that there are differences among them. Most of the local authorities are not keen to change their format of reporting. According to Luder, for change to occur the existence of a stimulus is not necessarily required. A change in the basic attitudes of producers of information towards a greater willingness to innovate can also result in a change of accounting information. This will occur only if the structural variables influencing the behavior of producers of information are conducive to change⁷.

In the case of the local authorities examined, implementing a uniform accounting standards or full accrual accounting would require the employees be sent for training, new financial systems, and investment in computer facilities and systems. This would have required larger sums of money than the local authorities were prepared to spend. The existence of these barriers slows down the process of change.

In order to enhance the quality and uniformity of financial reporting of Local Authorities throughout Malaysia, harmonisation of the financial reporting format is a priority. It is important that initiatives towards the adoption of one single set of financial reporting be made as soon as possible. The announcement made by the government in March 2011, to

move from modified cash accounting to full accrual accounting in 2015 had raised concern among local authorities. It is hoped that the announcement would caused the local authorities to take necessary actions to ensure that they are ready to embark when the time comes.

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