

**THE REFORM OF GOVERNMENTAL ACCOUNTING:  
A Discussion of Lüder's Financial Management Reform (FMR) Model**

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**ABSTRACT**

*Tulisan ini bertujuan menelaah Model Reformasi Manajemen Keuangan (Financial Management Reform /FMR model), yang disebut juga dengan Lüder's Contingency Model. Model ini telah dijadikan konsep dasar untuk menjelaskan reformasi akuntansi pemerintahan di banyak negara. Kajian ini berusaha menganalisa bagaimana teori tersebut dibangun dan berkembang, serta mengevaluasi relevansinya dalam menjelaskan reformasi akuntansi pemerintahan terutama di negara maju. Dengan pendekatan analisa deskriptif, studi ini menyajikan hasil telaah terhadap berbagai publikasi studi banding akuntansi pemerintahan internasional yang berhubungan dengan penerapan, pengembangan, aplikasi dan isu kritis seputar FMR Model.*

*Hasil temuan menjelaskan bahwa FMR/ Lüder's Contingency Model memiliki peran sangat penting dalam penelitian-penelitian tentang reformasi akuntansi pemerintahan di banyak negara. Ini merupakan satu-satunya model yang paling berhasil dalam menjelaskan teori dan konteks dari reformasi akuntansi pemerintahan di suatu negara. Namun penelitian yang komprehensif dengan menggunakan Model ini baru dipakai untuk komparasi reformasi akuntansi pemerintahan di negara-negara maju.*

*Model ini sendiri masih memerlukan perbaikan karena belum mampu menjelaskan arti 'reformasi' atau 'inovasi' itu sendiri, 'dari mana berubah' serta 'kemana berubah'. Kemungkinan Model ini akan terus berkembang dimasa mendatang sesuai dengan temuan-temuan baru selama penelitian.*

*Keywords: Contingency Model, FMR Model, Governmental Accounting Reform, Accounting Innovation*

**1. INTRODUCTION**

Various attempts at developing theories and frameworks have been made in order to understand the accounting changes in the public sector (Lapsley and Pallot, 2000; Hopwood, 1984). One of the models is "Lüder's Contingency Model", also known as Financial Management Reform (FMR) Model. Developed by Lüder in 1992 the Model aims at presenting a theoretical, contextual explanation for governmental accounting reforms. This "Contingency Theory" attempts to explain the transition from traditional government accounting to a more informative system through interactions of various social, political and administrative factors including its implementation barriers. However, the initial model itself

has undergone modifications overtimes (Lüder, 1992; 2002). This phenomenon has made the Contingency Model itself a subject of research.

### **Objectives of the Research**

To answer “how the FMR has been developed and used as the reference to explain the governmental accounting innovations”, the paper will (1) discuss the establishment and the background behind the introduction of the Lüder’s FMR Model, (2) review the presentation of the model and its development from the initial model to the latest version, (3) analyse the application of the model, particularly based on the experience of industrialised countries.

### **Methodology and Limitations**

This is a desk research, the discussion based on secondary data such as electronic sources, CIGAR journals, government publications, legal acts and regulations, published and unpublished official documents. The descriptive interpretation of evidence by researcher might not entirely free from intellectual subjectivity. Thus, the presented results are tentative at best. However, I believe this limitation does not invalidate the discussion.

## **2. THE ESTABLISHMENT AND DEVELOPMENT OF LÜDER’S FMR MODEL**

From early eighties onwards world public sectors have undergone a thorough financial, organizational and managerial reform. Government accounting reform is part of this New Public Financial Management reform - NPFM (Larbi 1999; Pallot 1992). The direction of reforms is argued to be the shift of accounting basis in the government from cash to accrual (Jones and Lüder, 2003). However, the accrual mode itself is implemented in different ways, thus, appeared in many forms across countries or jurisdictions.

Various research have been devoted to know how to understand the reform and what factors were involved in the processes accounting reform. K.G Lüder is among the governmental accounting researchers that attempt to pursue the answers. In doing so, he developed a contingency model in 1992. The model was a result from a series of international studies undertaken in nine countries between the mid 1980’s and the early 1990’s. The study was primarily led to understand the “why” of government accounting changes.

### **The Basic Version of the Development of FMR Model**

The basic version of the Model was published in 1990 in German. It was a product of a series studies on government budgeting and accounting systems reform issues and practices in some industrialised countries. The research results proposed that the differences were resulted from the differences in the national politico-administrative background. Therefore, the proposed Contingency Model aims at specifying contextual and behavioral variables involved and their influence on the outcome of the governmental accounting innovation process (*Appendix 1 displays the initial version of Contingency Model*).

The first three contextual variables (*stimuli, social environment of the government and the characteristics of the political administrative system*) would influence the basic

attitudes and behavior of both users and producers of government financial information. Particular situation would trigger changes. For example, financial scandals or government financial crisis could be stimuli for dynamic interactions between users and producers on the way to the governmental accounting reform. Nevertheless, the achievement of the expected outcome could be prevented by the *implementation barriers* such as problems in organisational characteristics, the legal system, the qualification of accountants and the size of jurisdictions.

However, the evidence obtained from the application of this initial model was fairly weak. Lüder (2002:2) comments, "Conduciveness of environmental factors to government accounting reform, however, is certainly not a sufficient and may be not even a necessary condition for successful implementation of such a reform". Hence, a need for modifications and extensions of the model is unavoidable.

There is also the dichotomy of users (citizens, members of parliament and others) and producers (politicians, managers and accountants) of accounting information. However, some players may play different roles simultaneously. For instance, an administrative actor was a citizen that received the service from the government while he/she was also a politician (Nowak and Bakalarska, 2005:99) Thus, the simplification of the dichotomy of users and producers has been modified in the further version of the Contingency Model.

Further development of the model is stimulated by evidence from new studies (Lüder, 2002). As seen in *Appendix 2*, the change of the model was not radical. Some new features were introduced. These include a broad additional behavioural variable of two different groups of political and administrative actors. "Dominating doctrine" was also inserted as stimuli. The adjustment was also made by Godfrey et al. (1996) based on the result of observations in developing countries. International institutions, donors and agencies did play a significant role in the processes of accounting reform in many developing countries by stipulating demands over the use of the money and control over the direction of the reform. However, the barrier was also resulted from the demands of international donors which were contrary to the needs of a country.

The improvement was also taken by Jaruga and Nowak (1996). They suggested a new component, namely "the consequences of the innovation". The consequences were the effect of reform to change the behavior of public, including the behavior of political and administrative actors. In addition, the structural variables were also expected to change in a long-term. This idea proposed a gradual phase of accounting reform, not a single process, in which the previous stage of reform stimulated new reform (Lüder, 2002:3).

In 2001, Godfrey et al. cited in Lüder (2002) has also proposed a new extended version, namely a "diffusion-contingency model". The model is modified by an implementation variable that plays a role in helping to identify the innovation decision process. Budaus and Buchholtz (1996) have also identified "hard" (Procedures and instruments) and "soft" factors (change of behaviour and attitude) as the elements that channel the reform process. Another contribution (Yamamoto, 2000) has sharpened the specification of the contextual variable "political system" and "administrative culture". The first one has been defined as governance while the later has been called management.

Furthermore, Pallot (1996) also identified "implementation process". He put forwards that a better management of the process has a strong impact to the successful implementation of the reform. A further development by Laughlin and Pallot (1998) has included "epistemic communities", expertise or professional who possess the knowledge in the relevant field of study, as one of its variables.

**The Financial Management Reform Process Model (FMR)**

The recent FMR Model (Lüder, 2002:18, Jones and Lüder, 2003:40) has been resulted from all above modifications, extensions, discussions, and new ideas generated from research on different countries, particularly from Australia. This Model still includes the contextual variables specifying the institutional arrangement of the country. However, it attempts to correct the dominance of the context over behaviour of the previous Contingency Models. It has now introduced “feed back loops” that are distinguished from “lines of influence” and “lines of impact”. They represent the “consequences for the real world”, therefore, attempting to relate the behaviour and attitude of the main actors in the process to the outcome of the reform. Consequently, it considers the possibility of a multi-stage reform process. This complete revision is featured in *Appendix 3*.

**Stimuli** are events that trigger the reform (Jones and Lüder, 2003:44). These include:

**Table 1 Stimuli for Accounting Reform**

<b>ProbleProblemsms</b>	<b>Requirements by</b>	<b>Opportunities</b>
▪ Fiscal/economic crisis	▪ Donor agencies	▪ Software availability/renewal
▪ Financial scandal	▪ Public sector management approach	▪ Availability of general accepted accounting concepts
▪ Fragmentation of governmental financial management	▪ Auditors	▪ Change of parliamentary majority
▪ Securing public sector reputation	▪ Capital market	

*Source: Lüder and Jones (2003: 44)*

**Institutional Arrangements** contains a broad category of variables. Firstly, “*legal systems*” adopted in a country may affect the flexibility of the governmental accounting system. These may cover civil law and common law in which each system has its own model of governance. These systems has different degree of compromise with the electoral system and the flexibility of budget law. Secondly, “*state structure*” model also influence the reform process. The structure of a country may appear in form of “unitary or federal”, “cooperative federalism or competitive federalism”, “one chamber parliament or two chamber parliament”, “the division of power between the electorate, the government and the directly elected bodies.

Thirdly, the form of “*administrative structure*” of the state also has its impact on the reform process. The choice between “decentralized or centralized”, “concentration or fragmentation of financial functions” and other types of national-subnational power, organisational and financial relation has a degree of influence in implementing the reform. Furthermore, the qualification “*civil service*”, especially the accountants plays a vital role in smoothing the reform. The shortage of the accounting expertise in a particular area will be a serious obstacle to the reform process. Eventually, the national “*culture*” (social, political and administrative) prevailing in a country would equally decide the extent of reforms. Culture is a climate for the reform.

**Reform Drivers** include government commissions, professional associations, audit institutions, standard setting bodies, consulting firms and scholar networks. They are professional groups which contribute to the reform in particular issues through discussions, publications, and advocacy or campaign. **Political Reform Promoters** include politicians, usually members of government, play a central role in the all administrative reform. With respect to governmental accounting reform, the main key players in the process are commonly the minister of finance and the prime minister. Likewise, members of parliament can also be reform promoters. However, it requires a strong political power to impose the ideas which is sometimes opposed by the executive.

**Stakeholders** are groups consist of the general public, the parliament, lines department and agencies (the administration) and the statistical office. Another component that can be clustered as stakeholder is audit institutions, when it is considered not the reform drivers. While the reform drivers have a common agreement toward the reform, the stakeholders have various perceptions. Some agree and the remaining perhaps not, depends on the benefit they perceive. **Implementation Strategy** can be defined narrowly as “the last phase of the reform process” (Jones and Lüder, 2003:48). It is the process of realisation the reform concept. The implementation of reform may take the following forms: authoritarian vs. participative, centrally guided or not, one or multi-steps, with or without pilot testing, considerable vs. minimal user discretion, the duration of implementation period, with or without the involvement of systematic staff training and the involvement of advisory board.

### **THE APPLICATION OF LÜDER’S CONTINGENCY MODEL**

The FMR model has been mainly applied in industrialised countries. Among them are the United States (Chan, 1994), New Zealand (Pallot 1996), Japan (Yamamoto), Australia (Christensen, 2001), Portugal (Jorge, 2005). Other researchers have also applied Luder’s contingency model in order to analyse the innovations of governmental accounting in some developing countries. These include Sudan (El-Batanony and Jones, 1996), Kenya, Tanzania and Uganda (Godfrey et al., 1996), India (Khumawala, 1997), and Nigeria (Adeyemo, 1998), Argentina and Chile (Perez and Hernandez, 2005).

#### **The Application of the Model to the Developed Countries**

*Table 2* shows governmental accounting reform in developed countries at national and local level. Only six out of nine of the observed countries have been undergoing the accrual accounting reform at the national government level. Whilst Spain, Finland, Sweden and UK have commenced the reform since the 1990s, Switzerland and France just started after 2000.

**Table 2 Reform Waves of National Accrual Accounting**

<b>National Government Reform Wave</b>		
<b>1990s</b>	<b>After 2000</b>	<b>Not yet started</b>
Spain Finland Sweden	Switzerland France	Germany Italy the Netherlands

UK		
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*Source: research*

**Stimuli.** *Table 3* provides a number of stimuli that triggered the governmental accounting reform activities at national level, including the cases where those stimuli present.

**Table 3 Stimuli for Accounting Reform (at National Level in the Observed Countries)**

<b>Problems</b>	Fiscal/economic crisis	France, Finland
	Financial scandal	European Commission
	Fragmentation of governmental financial management	Switzerland, France
	Securing public sector reputation	Spain, France, UK
<b>Requirements by</b>	Donor Institutions	
	Public sector management approach	Switzerland, Finland, UK
	Auditors	European Commission
	Capital market	
<b>Opportunities</b>	Software availability/renewal	Switzerland, UK
	Availability of general accepted accounting concepts	
	Change of parliamentary majority	

*Source: research*

Fiscal or economic crisis, budget deficits, high and growing public debt, low or even negative growth of GDP and high employment are the cause of reform for France and Finland. Utilization of different model of accounting and financial reporting is the cause for Switzerland and France. Improving the country's image as 'modern progressive' is the case for Spain, France and UK. The requirements by donor institutions are clearly not the case in any of those countries. The arise of New Public Management has persuaded many countries, especially Switzerland, Finland and UK, to reform the way of presenting and handling budget and its accounting procedures. The adoption of accrual accounting system as the influence of software availability is a stimulus for Switzerland and UK.

**Institutional Arrangement.** In the observed countries, national governments have played an imperative role in the process of setting accounting norms and rules. Norms and rules become more details as they move down to the lower hierarchy. Such a hierarchy of accounting law is presented in *Table 4*.

**Table 4 Hierarchy of Accounting Law**

Binding Nature	Instruments	Institution
<b>Mandatory</b>	Statute law	Parliament
	Ordinance	Cabinet/minister [requires parliamentary authorization]
	Administrative regulations	Ministry [without the involvement of legislature]
	Directive instruction	Ministry
<b>Voluntary</b>	Recommendation, guidelines	Ministry or government internal body or government external body

Source: Jones and Lüder (2003:41)

**Key Players.** Ministry of Finance, their heads, the cabinet as well as prime minister are regarded as the central political reform promoters in the national governmental accounting reform in European countries, particularly in Spain, Sweden and the UK. While initiating the reform, finance ministers in these countries have also involved in the enforcement process. They are considerably powerful because not only their plans need no approval of the cabinet instead of prime minister only, but also responsible for both national and local government accounting such as in Spain and France. However, finance ministers in countries such as Germany, the Netherlands and Switzerland have relatively weak positions due to a federal structure, a need to obtain cabinet approval for the reform and no central agencies in charge of accounting. They are still considered as vital national reform promoters, but unable to instigate a thorough reform. Furthermore, Parliaments in these countries are likely observers in governmental accounting reform.

**Reform Concept.** The reform process in these observed countries is heading toward some form (full or modified) of accrual world. The reform concept is then all features related to the accrual-based accounting system. The reform also includes the choice of measurement focuses, valuation bases, three disclosure issues (statement of financial position, operating statement and cash flow statement), and consolidated financial statements. These are shown in the following tables.

**Table 5 Measurement Focuses**

<b>Liabilities</b>	<b>Assets</b>			
	Monetary assets	Monetary assets + receivables	Monetary assets + receivables + most physical/	Monetary assets + receivables + all physical/ Intangible assets

			Intangible assets	
Borrowings	Germany Netherlands			
Borrowings + payables			Italy	
Borrowings + payables + most provisions			Finland	France
Borrowings + payables + all provisions			Spain Switzerland	UK Sweden

*Source: research*

**Table 6 Valuation Bases**

Countries	Valuation bases		
	HC (Historical Cost)	CC (Current Cost)	HC/CC
Switzerland			X
Germany	X		
Spain	X		
France			X
Finland			X
Italy	X		
The Netherlands	X		
Sweden	X		
United Kingdom		X	

*Source: research*

**Implementation Strategy.** The current implementation strategy to accrual accounting reform at national governments in the respective countries is presented in *Table 7*.

**Table 7 Implementation Strategy**



		<b>Switzerland</b>	<b>France</b>	<b>Finland</b>	<b>UK</b>
<b>Central Guidance</b>	Yes	X	X	X	X
	No				
<b>Implementation period</b>	Short	X	X	X	
	Long				X
<b>Transition Mode</b>	Single-stage	X	X	X	
	Multi-stage				X
<b>Experiment (parallel operation)</b>	Yes		X		X
	No	X		X	
<b>Intensity of staff training</b>	High				X
	Low			X?	
<b>Advisory board</b>	Yes		X	X	X
	No	X			

*Source: Jones and Lüder (2003:49)*

The table shows the strategy of realizing the reform concept. Centrally guided accounting reform (i.e., terminology, a uniform chart of accounts, clear and uniform recognition and valuation values, and uniform packages across the government) has dominated all the respective national governments. Regarding the implementation period, France for example, has bravely chosen a short implementation period of 5 years. Furthermore, the stage approached is the model adopted by the UK government by introducing departmental accrual accounting before the comprehensive central government accounting as well as accrual accounting before accrual budgeting. The UK national government as well as French has also applied the experimentation in operating the new system in parallel to the old system such as in the preparation of financial statements. While the data on the intensity of staff training was not adequately obtained, the UK national government reform has significantly involved the staff training.

### **The Application of the Model to the Developing Countries**

Most of the studies in governmental accounting change were undertaken on developed countries. Only few studies did attempt to apply the Contingency Model to developing countries. The comparative research that covers a substantial number of developing countries, however, has not yet been developed. Although the studies did contribute to the literature, the result is still relatively inadequate to reveal a substantial picture of developing countries governmental accounting reforms. The studies on developing countries to some extent have clearly confirmed the elements in variables proposed by the FMR Model. One distinctive feature discovered in the

developing countries is that the requirements by the donor institutions are usually appear as the important stimuli for the reform following the financial or economic crisis.

### **THE DEBATE OF THE RELEVANCE OF THE FMR MODEL**

Although the FMR Model at present has served as the primary theoretical foundation for Comparative International Governmental Accounting Research (CIGAR), it is not free from limitations. It has been constructively criticised due to its shortcomings. *First*, the development of the Contingency Model was basically aimed at understanding the “why” of government accounting, particularly the “why” of the reforms. It only offers more explanations about the reform process, especially about the favourable and unfavourable combination of observed contextual variables within a country, that drive the change of accounting system from the traditional mode towards performance and resource accounting and budgeting (Jorge, 2005:29). This perceived weakness relates to the “black box” (Chan et al., 1996) or the lack of explanatory power to the whole innovation process. As explained by Mellemvik and Monsen (1995), although the environmental conditions are similar, the changes in accounting system may differ. Moreover, technical differences in reform approaches could not entirely be clarified by the differences in environmental conditions (Budaus and Buchholtz, 1996). There is a greater possibility of the incompleteness of the elements in the variables. Therefore, the inclusion of further additional variables and its elements as well as the specification of certain environmental compositions that are conducive to the reform concept implementation would be useful in improving the explanatory power.

*Second*, Lüder’s Contingency Model is also called “the Contingency Model of Governmental Accounting Innovations” as its purpose is to assess the conduciveness of environmental factors to the implementation of governmental accounting innovations. Not surprisingly, there are enormous meanings of “innovation” provided by different sources. The meaning includes “the act of introducing something new”, or “the introduction of new idea, method and device”, and “change that creates a new dimension of performance” (Hesselbein, 2002). Therefore, Chan et al. (1996) have ever demanded the clarification of the use of central term “innovation” as the incorporation of that word may mean anything in the governmental accounting changes. In dealing with the arbitrary definition of “innovation”. The term “innovation” is also also considered to be equal to as “reform”.

*Third*, the Contingency Model is developed “to explain the transition from traditional government accounting to a more informative system” (Lüder, 1992:108). CIGAR literature, however, has not clearly explained the term “traditional government accounting”. It then has been widely interpreted as “cameral accounting” which is traditionally applied in governmental organisations. The emergence of accrual accounting replacing the cameral accounting in the governmental sector of many countries has been considered as the direction toward a more informative system. Thus, the change from a cash-based governmental accounting system to one based on accrual has been generally regarded as the concept of innovation. This has attracted a considerable critic. Monsen and Nasi (1998:286), for example, have argued: “...accrual accounting with its matching concept cannot in general be properly applied in the governmental context. It is true that it can be applied for certain activities where the linkage between sacrificed and revenue earned is

*direct or close enough...but usually this is not the case in governments... Hence, the adoption of accrual accounting as the main accounting model in governments does not represent an accounting innovation”.*

The discussion on the validity of accrual accounting as a concept of innovation has gone further. Ellwood and Wynne (2005:158) identify accrual accounting “*as part of one approach to the management of public services that may be considered to have value within certain circumstances and on certain preconditions*”. The value of accrual accounting, therefore, should be assessed in context as it is not universally appropriate for all governmental organisations. In the case of developing countries, for example, as argued by the UK DFID (2000), a move towards accrual accounting is not primarily regarded as a better concept of reform. It is due to significant shortcomings in the management practices of the respective developing countries which provide an unfavourable base for the reforms. Before shifting it governmental accounting system to the accrual mode, these countries should first ensure the availability of effectiveness fundamental technical and government elements. However, the meaning of reform has likely remained ambiguous, particularly “what is changing from” and “what is changing to”.

### **CONCLUSION AND RECOMMENDATION**

The FMR Model has played an invaluable role in the history of Comparative International Governmental Accounting Research (CIGAR). Not only has the model provided a theoretical, contextual explanation to the governmental accounting reforms, but also served as a reference to understand what factors contribute to the favourable and unfavourable of the reform process. A number of studies have applied this Model in developed countries. This is possibly due to the dynamic development of governmental accounting in the developed countries as well as many leading CIGAR researchers are concentrated in the industrialised nations. The findings from national and across-country comparisons have contributed to the development of the Model itself. In fact, since the first initial model was founded in 1992, the Model has been undergone modifications until its latest version introduced in 2001.

Although the Model has served as a common framework to explain the transition from traditional government accounting to a more informative system, the Model suffers from a lack of explanation to the meaning of “reform” itself. It has not yet had clear explanations of “what is changing from” and “what is changing to”. Accrual mode that is believed as the direction of reform has a variety of forms and practices. This implies that the meaning of “innovations” toward a more informative system remains ambiguous. These limitations suggest a continuous improvement in the conceptual theory of the Model. Also, if the debate about the relevance of the Contingency Model is to be moved forward, a better conceptual framework for governmental accounting reform research needs to be developed. More importantly, this Model can be used this Model in order to have a better understanding of governmental accounting reform in Indonesia, which is now taking place both at national and local level.

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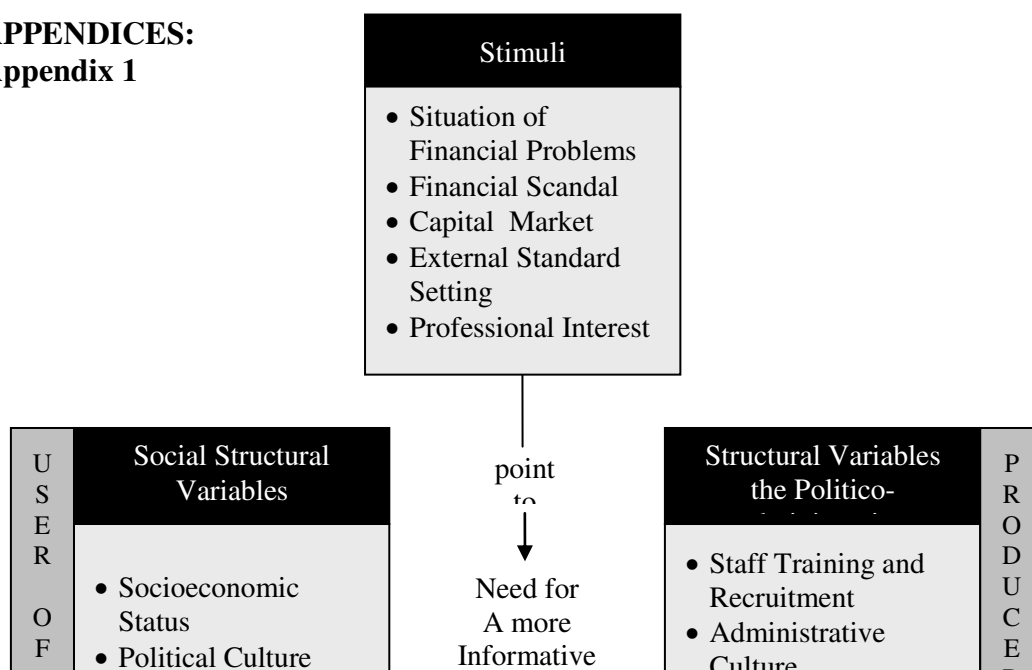
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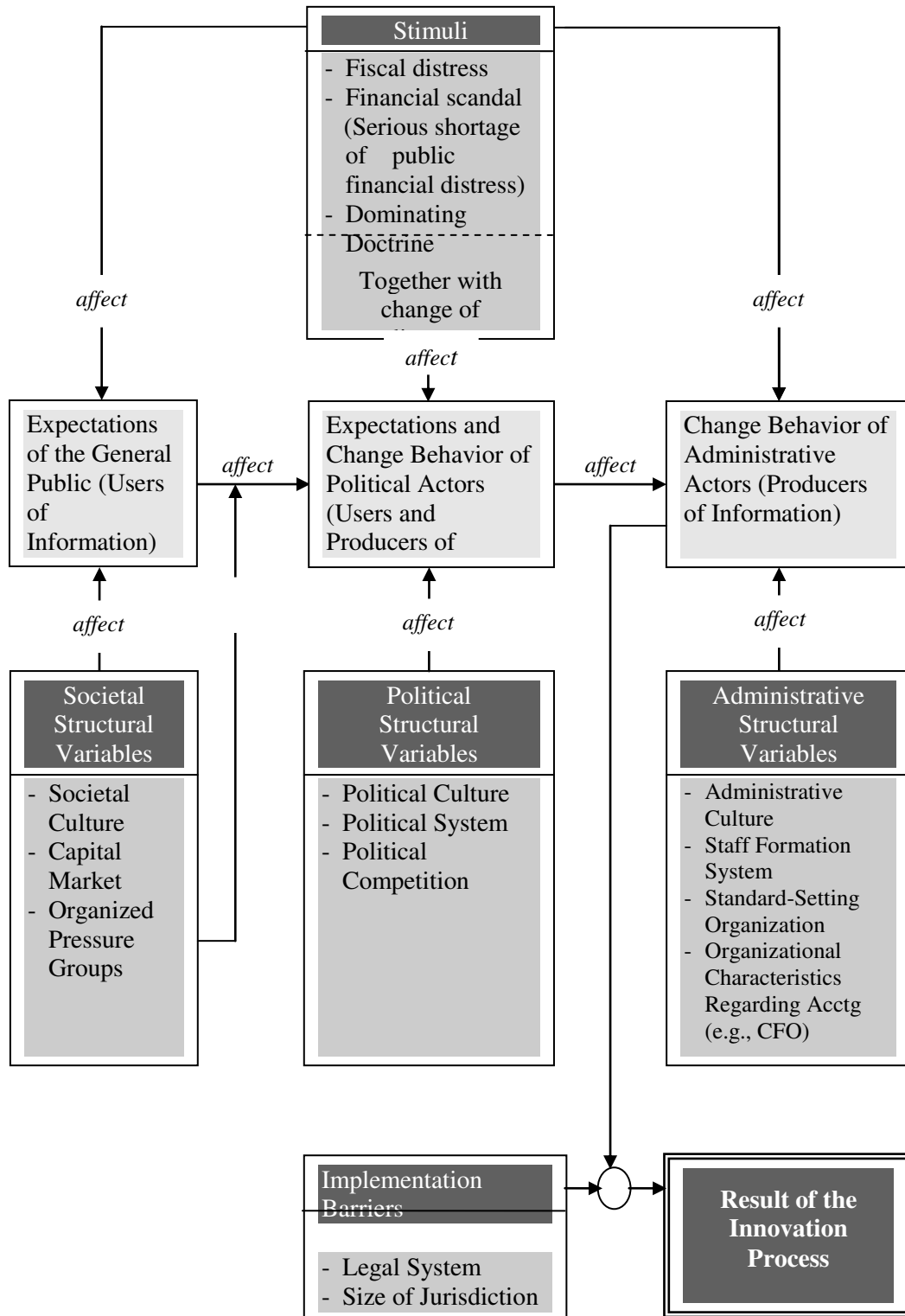
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**APPENDICES:**

**Appendix 1**



**Appendix 2**



**Modified Contingency Model of Governmental Accounting Innovations**

**Appendix 3**

