



PERFORMANCE MANAGEMENT SYSTEM IN A
MALAYSIAN LOCAL GOVERNMENT: A NEW
INSTITUTIONAL SOCIOLOGY PERSPECTIVE

BY

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ABSTRACT

Key Performance Indicators, also known as KPIs, help an organization to define and measure progress towards organizational goals. It is one of the examples of private sector practices that have been developed and implemented in public sector organizations to improve the performance of public services. The system is supposed to assist the government in meeting its objectives as well as to make it become more accountable. This explanatory case study intends to investigate the implementation of KPIs in a Local Government (LG) in Malaysia. New Institutional Sociology (NIS) is used to understand the various institutional pressures faced by the organization during the process of developing and implementing KPIs. Supposedly, KPIs were introduced to inculcate a high performance culture. However, it has been found that KPIs are used as a complementary tool to the existing PMS; Annual Work Target (AWT) practiced within the organization. AWT has become shared values within the organization, and still suffers from several drawbacks. The study also discovered that the new PMS has brought several changes to the individual, departments, and the organization itself. In addition, the study was able to discover and point out the changes in organizational behaviour among the organizational members through the implementation of KPIs. This study gives a new insight to the Public Sector Accounting research by exploring the development and implementation of KPIs in a LG as well as the organizational changes within the organization.

ملخص البحث

مؤشرات الأداء الرئيسية، المعروف أيضا KPIs، تساعد منظمة على تحديد وقياس التقدم المحرز نحو تحقيق الأهداف التنظيمية. هو واحد من الأمثلة على ممارسات القطاع الخاص التي تم وضعها وتنفيذها في مؤسسات القطاع العام لتحسين أداء الخدمات العامة. ومن المفترض في النظام لمساعدة الحكومة في الوفاء بأهدافها، فضلا عن جعله يصبح أكثر خضوعا للمساءلة. هذه الدراسة الإفرادية تفسيرية تعتمز التحقيق في تنفيذ مؤشرات الأداء الرئيسية في المحلية الحكومة (LG) في ماليزيا. ويستخدم علم الاجتماع المؤسسي الجديد (NIS) لفهم الضغوط المؤسسية المختلفة التي تواجه المنظمة أثناء العملية وضع وتنفيذ مؤشرات الأداء الرئيسية. وأدخلت KPIs المفترض، لغرس ثقافة عالية أداء. ومع ذلك، فإنه تم العثور على أن مؤشرات الأداء الرئيسية وتستخدم كأداة تكميلية للدورة الشهرية الحالية؛ هدف العمل السنوية (الهجوم الجوي) يمارس داخل المنظمة. الهجوم الجوي أصبحت القيم المشتركة داخل المنظمة، ولا تزال تعاني من عيوب عدة. واكتشفت الدراسة أيضا أن الدورة الشهرية الجديدة قد أحدثت تغييرات عدة للفرد، والإدارات، والمنظمة نفسها. وبالإضافة إلى ذلك، تمت الدراسة قادرة على اكتشاف ونشير إلى التغييرات في السلوك التنظيمي بين أعضاء التنظيمية من خلال تنفيذ مؤشرات الأداء الرئيسية. هذه الدراسة يعطي نظرة جديدة لبحوث "محاسبة القطاع العام" باستكشاف وضع وتنفيذ مؤشرات الأداء الرئيسية في ال جي، فضلا عن التغييرات التنظيمية داخل المنظمة.

APPROVAL PAGE

I certify that I have supervised and read this study and that in my opinion; it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a thesis for the degree of Master of Science in Accounting.

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DECLARATION

I here declare that this dissertation is the results of own investigation, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for my other degree at IIUM or other institutions.

Farhana binti Hasbolah

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GOVERNMENT: A NEW INSTITUTIONAL SOCIOLOGY PERSPECTIVE**

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This study is dedicated to My Family;

To Mama and Abah who constantly encouraged, supported and committed to their
daughter's education,

And to Farah who believed in her twin sister's ability in facing academic challenges
and become a better person the way she is today.

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LIST OF ABBREVIATIONS

AWT	Annual Work Target
BSC	Balanced Scorecards
DPM	Department of Prime Minister
GLC	Government Transformation Programme
IP	Investigation Paper
KPI	Key Performance Indicators
LA	Local Authorities
LG	Local Government
MHLG	Ministry of Housing and Local Government
NPAS	New Performance Appraisal System
PMS	Performance Measurement System
PM	Performance Measurement
SOP	Standard Operating Procedures
TQS	Training and Quality Section

CHAPTER ONE

INTRODUCTION

1.0 BACKGROUND OF STUDY

Performance Management Systems (PMS) have always been used in either big or small organizations to evaluate the employees' performance and to ensure the organizational effectiveness. PMS include the process of evaluation, suggesting further improvement, and rewarding the individual performance (Fryer, Antony, and Ogden, 2009) within the organization. Similarly, there are no exceptions to public sector organizations when it comes to measuring the performance of civil servants and their service delivery.

The performance appraisal system is one of the PMS exercised in many government agencies to improve the productivity, quality, timeliness, responsiveness, and effectiveness of public agencies and programmes. In general, performance appraisal can be defined as "an evaluation and grading exercise undertaken by an organization on all its employees either periodically or annually, on the outcomes of performance based on the job content, job requirement and personal behavior in the position" (Yong, 1996). The role of performance appraisal is to assess the employees' current or past performance relative to his or her performance standards. Robins & Coulter (1999) suggested that the performance appraisal has two major roles – administrative role and development role. First, the system provides information for salary adjustment, promotion, and layoff, and second, it fulfils its development purpose when the information is used to diagnose training needs and career planning.

In Malaysia, civil servants have been evaluated on a formal Performance Appraisal System (PAS) since year 1992 when the government introduced a new

remuneration system to replace the salary system, which was based on the Cabinet Report 1976 (Rusli, Azman, and Wan Khairuzzaman, 2007). The new system – New Performance Appraisal System (NPAS) – emphasized the aspects of employees' flexibility and the performance of the civil servants. Under the system, the Annual Work Targets (AWT) were introduced and used in government agencies as the indicators for the employees' performance. However, the system only lasted for nine years as the system was criticized for its weaknesses and shortcomings, such as the assessments were too rigid and not relevant (Public Service Department, 2007).

In 2002, the government replaced the NPAS with the Malaysian Remuneration System (MRS) as the performance management system. These two PMS –NPAS and MRS – are performance appraisal systems exercised within Malaysian government agencies in which the performance and salary adjustment are linked with one another. The tools were used to evaluate the annual performance of civil servants individually and also to reward the excellent performance under salary progression and promotions. However, the MRS has also been the subject of some criticisms. Many civil servants are not satisfied with the assessment made by performance evaluators to assess the AWT performance. The performance evaluators were accused of not following the scheduled assessments set for the AWT and the evaluation guidance provided by the department was described as unclear (Public Service Department, 2007).

In essence, there is no significant difference between NPAS and MRS except that the salary schemes have been revised (Harian Metro, Oct 11, 2011). In 2011, the government introduced a new remuneration scheme called the New Civil Remuneration Scheme (NCRS) to transform the civil servants so that they were more dynamic and responsive, and moving towards being performance oriented. The new

scheme is expected to replace the MRS with the aim of increasing the minimum salary for civil servants.

Civil servants are being held accountable, answerable, and responsible to deliver a high quality of services specifically to the citizens. It requires them to answer to the citizens in terms of justifying the allocation and utilization of the resources used. Local government (LG) is the third tier of the Malaysian government and its services have a direct impact on the level of satisfaction of citizens because they are the major stakeholders of the LG. In addition, the LG operates as the provider of the services. The greater the level of citizens' satisfaction in the local government services the better the perception of good quality service delivery and service providers (Scott & Vitartas, 2008).

According to Scott and Vitartas (2008), the relationship between the service provider and the service user is recognized as the relationship of demand and supply between the duty bearer and the rights holders. The delivery of services by the LG to maximize the satisfaction of rights holders is similar to the relationship between the principals and the agents in delivering good service. The public can respond to the level of the quality of services by expressing their opinions through complaints, feedback or survey forms to the LG. Complaints are one of the measurements of dissatisfaction concerning the service offered and actually signals the LG to improve its services. If one LG can provide a high quality of services, it can become an example for other LGs in Malaysia.

Performance measurement systems (PMS) are used to improve the performance of civil servants. According to Radnor and Barnes (2007), performance measurement (PM) is defined as quantifying, either quantitatively or qualitatively, the input, output or level of activity of an event or process. PMS has been widely used in

private and public organizations. In an LG, the development of effective and efficient performance indicators is crucial to maintain the performance of the organization. PMS has four main aspects of measurement (Fryer, Antony, Ogden, 2009); i.e. deciding what to measure, how and when to measure, interpreting the data, and communicating the results. LGs are required to develop both short- and long-term strategic plans to direct their achievements throughout the current years and future years. These strategic and operation plans help LGs to lead their directions towards the mission, vision, and objectives of the organization. The performance for the year will be assessed by top management in order to measure how far they have achieved and what they have targeted for the particular year (Rusli, Azman, Khairuzzaman, 2007).

Therefore, the strategic plans consist of planning, activities, and measures, as well as some initiatives to deliver services to meet and satisfy the demands from the public and to meet the stakeholders' expectations. The performance under the strategic plans is measured using strategic objectives known as Key Performance Indicators (KPIs) for the LGs to ensure their objectives are being met. KPIs are developed to be comprehensive with financial and non-financial indicators, and, at the same time, to play their roles in motivating employees and management to achieve the same goals (Kloot, 2009). Most LGs incorporate a "Back to Basics" programme into the strategic plan, where it provides mandatory and obligatory services (Kuppusamy, 2000). The mandatory services include services provided by every local authority while the obligatory services comprise additional services that are provided according to the needs and expectations of the locals and the ability of the local government itself.

The KPIs are then translated into the Balanced Scorecard (BSC) to clarify the strategic objectives, to communicate those strategies throughout the organization, to

link the strategic objectives to long-term targets, and to obtain feedback to learn about and improve the strategies. At the state level, the BSC will be used to measure the performance of the LGs to improve the state's performance. All elements in the BSC, such as financial, customers, internal business process, and learning growth are monitored closely by the State's Chief Minister.

1.1 MOTIVATION OF STUDY

Employees were evaluated on a yearly basis based on PAS (NPAS, MRS, and NCRS) using AWT. The evaluation process started in January and ends in December each year (Public Service Department, 1996). The AWT starts with the annual departmental planning in which all programmes and activities for the year are planned at the beginning of the year. The programmes and activities are the objectives and goals of the organization for the year. Then, the performance target will be determined to lead the employees to achieve the pre-determined goals. During the year, employees are required to implement the activities as planned. According to Public Service Department (2007), two assessments will be made throughout the year – midyear performance and year-end performance. The midyear assessment is to monitor the progress of the programmes and activities planned and the evaluation at the end of the year is to compare the actual performance and the pre-determined targets. The AWT assessments are made to measure the performance of the departments and individuals.

One major issue in these PMSs is that the evaluation and assessment does not represent the real performance of the civil servants. The issues can be discussed in terms of the officers being evaluated, the PMS itself and the assessment officers. First, the AWTs were not prepared at the beginning of the year, instead, it was prepared for

the midyear assessment purpose. There was a lack of monitoring of the preparation of the AWT by the Head of Department and top management. As a result, the AWT could not satisfy its objectives to evaluate the performance accurately. Second, the evaluations made by the assessment officers only reported the performance for that particular year and ignored the performance from previous years. In other words, individuals and departments were assessed annually and the salary adjustments were made based on the reported performances. Third, the assessment could be biased as individuals were assessed by their superiors, where the assessment officers did not actually follow the AWT scale performance but used their own judgement and assumptions.

In 2004, during the Government Linked Companies (GLC) Transformation Programme, ten colour-coded books were introduced¹. The government initiative was to make the GLCs as competitive as other profit making organizations. The programme was introduced with the goal of transforming the GLCs into high performing entities. KPIs were also launched simultaneously with the GLC Transformation Programme as a tool to measure the performance of GLCs. Ten initiatives was developed for the development of GLCs for 2005 and 2006. Each initiative was elaborated upon in the coloured books with each focusing on a different aspect, for example, the Green book focussed on board effectiveness, the Silver book on social obligation, the Red book on procurement procedures, the Purple book on capital management, the Orange book on human capital development, and the Blue book on performance management. Other initiatives were developed to strengthen the directors' capabilities, to enhance the monitoring and management of GLCs', to

¹ http://www.pcg.gov.my/trans_manual.asp

improve regulatory environment, and to enhance the operational improvements (GLC Transformation Manual, 2005).

Although the earlier focus of the transformation programme was on government-linked companies, the LGs were also affected. The government viewed that despite the AWT, the performance of civil servants was still at an unsatisfactory level and did not reach the optimum level (Rusli, Azman, and Kamaruzzaman, 2007). As a result, a circular was issued and directed at government agencies in 2005 to shift from using AWT to the new performance measurement system (PMS) – Key Performance Indicators (KPIs)². This circular came with guidelines and explanations about strategies, approaches, and steps to develop KPIs in the organizations. LGs are among the government agencies that were affected by the circular. However, during the issuance of the circular, not many LGs had initiated to develop and implement KPIs. In the Ninth Malaysia Plan, Dato’ Seri Abdullah bin Ahmad Badawi, the former Prime Minister, stressed that LGs should improve the quality of their services by using KPIs to monitor performance. By 2010, it was expected that all government agencies would be using KPIs. In addition, the performance of public service delivery of LGs would be strengthened through a systematic rating system, inspection, and audit.

The intensification of the performance culture in government was further stressed through the Government Transformation Programme (GTP). The fifth Prime Minister of Malaysia, Dato Seri Najib Tun Razak emphasised the performance of civil servants through transparency and accountability (EPU, 2006). Each ministry has its own KPIs to be achieved in order to improve the effectiveness of the Malaysian

² No. 2 of 2005 - Guidelines for establishing key performance indicators or Key Performance Indicators (KPIs) and implementation of performance measurement in government agencies. Issued on April 7, 2005.

government. All Ministerial KPIs are related to the six major policy areas – crime prevention, reducing government corruption, increasing access to quality education, improving the standard of living, upgrading the rural infrastructure, and improving public transportation. The performance of the ministries and its ministers are regularly assessed by the Prime Minister’s Department every six months to ensure the KPIs are on the right track. Reviews are made and evaluation of performance is stressed through the areas identified as the KPIs for each minister.

One of the focus areas for the Ministry of Housing and Local Government is to increase the service efficiency in service delivery in LGs. The use of KPIs in LGs is the means to achieve the objectives of the ministry to inculcate better performance delivery. Although public sector organizations are always asked to implement KPIs to improve the performance and service delivery, how the KPIs are developed and whether they have achieved their objectives is another issue. Although there are studies on the implementation of PMS in GLCs in Malaysia (see Norhayati & Siti Nabiha, 2009), literature on the evolution of PMS in LGs in Malaysia is still very scarce. An in-depth study on the evolution of PMS in LGs warrants attention, as it could provide explanation as to whether the government driven PMS is successful in bringing changes. The development and implementation of KPIs in LGs can be understood by looking at details of the process from the study

Therefore, the main research question of the study is **“How have KPIs been developed and implemented in a Malaysian local government?”** Following the general research question, the study hopes to find answers to the three specific research questions that have been extended from the general research question. These research questions are developed based on prior literatures on performance management (Armstrong, 2000; Fryer, Antony, and Ogden, 2009; Otley, 1999;

Fitzgerald et al., 1991; Radnor and Barnes, 2007; Neely, 1998; Winstanley and Smith, 1996; Bennett, 2002; Halachmi, 2011; Scott and Vitartas, 2008; Brennan and Douglas, 2002; McAdam, Hazlett, and Casey, 2005; Yongvanich and Guthrie, 2009; Jochem, Menrath, and Landgraf, 2010; Pilcher, 2005; Cavalluzzo and Ittner, 2004; Phusavat and Anussornnitisarn, 2009; Ghobadian and Ashworth, 1994; DiMaggio and Powell, 1983; Nor Aziah and Scapens, 2007):

1. How does a local government develop KPIs for its organization?
2. How are KPIs implemented and used in the local government?
3. What are the challenges and obstacles encountered during the development and implementation of KPIs in the local government?

1.2 SCOPE OF THE STUDY

This study focuses on the process of developing and implementing KPIs in the LG. It provides a detailed analysis of the process of developing indicators, targets, and measurements to be used in the KPIs as their PMS. In implementing KPIs in the organization, there might be challenges encountered by the organizational members. Institutional theory is applied in the study to explain how the LG responded to the forces and pressure undertaken by the local government in developing the PMS. The implementation of the PMS in the LG was taken into consideration as a result of the effective and efficient PMS. The local government selected for the study is Orchid, a pseudonym. The choice of the local government will be discussed in the methodology chapter.

1.3 RESEARCH METHODOLOGY

This study is considered as an explanatory case study to answer the developed research questions (Smith, 2003). It focuses on the reasons or causes of the organizational change in the organization. The development and implementation of KPIs provided a change throughout the organization. Orchid City Council (Orchid) is one of the LGs in Malaysia has been chosen as a case study.

The Orchid obtained a 4-star rating out of 5-star rating from the Ministry of Housing and Local Government in 2009. The Local Government's Star Rating System was introduced by the ministry in 2008 to facilitate the ministry's monitoring and tracking of the local government's performance, and to encourage them to strive for better organizational management and service delivery. The system is expected to evaluate the level of achievement of service delivery to the local citizens (efficiency), competitiveness, and effectiveness. The study investigates the development and implementation process of the PMS in the Orchid, external and internal pressures of the process, and challenges to the LG.

The primary data were collected through semi-structured interviews. The interviews included top management, particularly, Deputy Mayor, Directors, Deputy Directors, Head of Departments, and KPI Secretariat from various departments and divisions. A total of 22 interviewees were interviewed during the course of the study. An in-depth interview approach for the semi-structured interviews was chosen to allow interviewees to reflect on the issues with which they are familiar. Data from interviews were transcribed and analysed to obtain the information and answers for each research question.

The secondary data were collected from the documentary analysis of annual reports, the five-year strategic plans, PMS circulars, PMS-KPI manual, minutes of