



**THE IMPLEMENTATION OF ACTIVITY-BASED
COSTING IN THE ACCOUNTANT GENERAL'S
DEPARTMENT OF MALAYSIA**

BY

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**A dissertation submitted in fulfilment of the requirement for
the degree of Master of Science in Accounting**

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ABSTRACT

The idea of public sector reforms is rooted in the concept of new public management (NPM). In this concept, the adoption of private sector management techniques in the public sector context is among the important mechanisms to increase the efficiency of the organization. Hence, this research aims to provide a useful insight into the process of implementing on of these private sector management techniques, namely the activity-based costing (ABC) system, in a public sector organization setting. In addition, this study attempts to provide insights on the critical factors that influence the success of the ABC implementation process. This study also examines the usefulness of the ABC system and the challenges faced in the process of implementing this system. Using a single case study approach, this research uses semi-structured interviews, documents review and a self-developed questionnaire survey to gain an understanding of the ABC implementation process and issues pertaining to its implementation in a single public sector organization in Malaysia, namely the Accountant General's Department of Malaysia (AGD). The findings reveal that the ABC information derived from the ABC system has limited use. Besides, the process of implementing the ABC system in the AGD faces several challenges and difficulties in respect to the technical and behavioural issues. This study makes a contribution to the empirical literature on the application of the NPM mechanism, particularly the adoption of a private sector management technique in the context of a public sector organization in a developing country. Apart from its contribution to the literature in this area, this study provides valuable insights for government agencies that will enable them to gain an understanding about the ABC implementation in the context of public sector organizations.

خلاصة البحث

فكرة إصلاحات القطاع العام متجذرة بمفهوم فكرة الإدارة العامة الجديدة (NPM). في هذا المفهوم، اعتماد تقنيات إدارة القطاع الخاص في إطار القطاع العام هو من بين الآليات المهمة لزيادة كفاءة المنظمة. وبالتالي، يهدف هذا البحث إلى تقديم نظرة مفيدة في نظام عملية تقدير التكاليف على أساس النشاط (ABC)، وهي واحدة من تقنيات إدارة القطاع الخاص في إطار تنظيم القطاع العام. بالإضافة إلى ذلك، تحاول هذه الدراسة تقديم رؤى حول العوامل الحاسمة التي من شأنها أن تؤثر على عملية تطبيق الـ ABC. تتناول هذه الدراسة أيضا فائدة نظام الـ ABC والتحديات التي تواجهها في عملية تنفيذ هذا النظام. باستخدام منهج دراسة حالة واحدة، يستخدم هذا البحث مقابلات شبه منظمة، استعراض الوثائق، و مسح استبيانات مطورة خصيصا للدراسة لفهم عملية تطبيق ABC والقضايا المتعلقة بتنفيذها في مؤسسة قطاع عام واحدة في ماليزيا، وهي قسم المحاسب العام (AGD). وكشفت النتائج أن معلومات الـ ABC المستمدة من نظام الـ ABC لديها استخدام محدود. الى جانب ذلك، واجهت عملية تنفيذ نظام ABC في AGD العديد من التحديات والصعوبات كالمشاكل مع القضايا الفنية والسلوكية. ساهمت هذه الدراسة في مجال تطبيق آلية الـ NPM، خصوصا في اعتماد أسلوب إدارة القطاع الخاص في سياق تنظيم القطاع العام في البلدان النامية. بغض النظر عن مساهمة هذه الدراسة في هذا المجال، تقدم هذه الدراسة معلومات قيمة للجهات الحكومية لفهم وتعلم طريقة تنفيذ الـ ABC في مؤسسة القطاع العام.

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 dissertation for the degree of Master of Science in Accounting.

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DECLARATION

I hereby declare that this dissertation is the result of my own investigations, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degrees at IIUM or other institutions.

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LIST OF ABBREVIATIONS

ABC	Activity-Based Costing
AGD	Accountant General's Department of Malaysia
e.g.,	for example
GFMAS	Government Financial Management Accounting System
i.e.,	that is
IIUM	International Islamic University Malaysia
MAS	Micro Accounting System
NPM	New Public Management
OBB	Outcome Based Budgeting
UK	United Kingdom
UKM	Universiti Kebangsaan Malaysia
US	The United State of America

CHAPTER 1

INTRODUCTION

1.0 INTRODUCTION

This chapter provides as an introduction to this thesis and consists of five sub-sections. Section 1.1 introduces the background of the study and is followed by the problem statement of the study in Section 1.2. Section 1.3 presents the motivation of the study and followed by the objectives of the study in Section 1.4. Further, the significance of the study is discussed in Section 1.5. Lastly, Section 1.6 describes the organization of the thesis.

1.1 BACKGROUND OF THE STUDY

In this new age of public sector reforms, the issues of efficiency and effectiveness of public sector organizations in terms of service delivery is becoming a major concern among researchers in the field of public sector accounting. In response to the criticism expressed by the public, many governments around the world have performed an extensive public sector transformation by adopting a new management accounting style in public sector organizations. The adoption of private sector management accounting techniques in public sector organizations is among the important elements of new public management reform in the public sector (Hood, 1991; Siddiquee, 2006). The new public management agenda that emphasizes the roles of private sector management techniques in public sector aims to increase the efficiency of government and public agencies in managing their resources and service delivery (Helden, 2005; Siddiquee, 2006).

Concerning the efficient management of public resources, one of the important

areas that needs to be strengthened is that of the cost management systems adopted by public sector organizations. This is because an appropriate cost management system will assist public agencies in the better management of public resources. The costing information produced by a costing system plays a central role in facilitating the decision-making, planning, and control processes within organizations (Guan, Hansen and Mowen, 2009). Therefore, public sector organizations are being forced to look into better costing techniques that can produce costing information that is more accurate (Brown, Myring and Gard, 1999). Following the recent developments under the agenda of public sector reform, many public sector organizations across countries have migrated from a traditional costing system to a more sophisticated form of costing technology through the adoption of activity-based costing (ABC) (Brown et al., 1999).

Activity-based costing was initially designed for the use of private sector, particularly manufacturing companies, as a new costing method to overcome the distortion in costing information produced by the traditional costing system (Cooper and Kaplan, 1988). However, as reported by Kaplan (1994), the ABC technique has also been utilized in the service sector since the 1980s. Later, the discussion on the use of the ABC application was expanded into the public sector context, where ABC adoption was perceived as a new accounting innovation to improve public management efficiency and effectiveness (Arnaboldi and Lapsley, 2005; Baird, 2007; Brown et al., 1999; Carmo and Padovani, 2012; Fortin, Haffaf, and Viger, 2007). Activity-based costing is a relatively new strategic management accounting tool and represents a contemporary costing method that traces the cost of activities through a cost driver to the cost objects (Guan et al., 2009). As claimed by past literature, ABC has benefits, particularly in terms of providing more accurate cost information for

better decision making, improving cost control and cost management, and providing opportunities to discover non-value-added activities (Baird, 2007; Cooper and Kaplan, 1991; Innes and Mitchell, 1995; Shield, 1995; Swenson, 1995;). Thus, ABC is an important accounting innovation and functions as part of the strategic management accounting tools that organizations can use to improve their performance.

The Accountant General's Department of Malaysia (AGD) is a government agency that plays an important role in facilitating the management of the accounts for the public sector in Malaysia. In 2013, the AGD spent around RM283.027¹ million to perform its services in handling the accounting procedures of Malaysian government ministries and agencies. The AGD was the first Malaysian government agency to implement the ABC system as their costing method to replace the traditional costing system known as the Micro Accounting System (MAS). The development of the ABC system started in 2006 after the implementation of the new government accounting system known as the Government Financial and Accounting Management System (GFMAS). By 2012, the AGD, including all its branches, had implemented the ABC system as its costing method.

Thus, this case study tries to explore and describe the process of ABC implementation specifically in the AGD by focusing on the technical aspects of implementation. In addition, the study also explores the behavioural issues and challenges pertaining to the process of ABC implementation. The investigation of the ABC implementation in this particular government agency takes the perspective of new public management (NPM) theory, which postulates that ABC adoption serves the purpose of improving organizational performance. Moreover, the study attempts to

¹Total spending RM283.027 represented by: RM213.056 million spent on operating expenditure and RM 69.971 million on development expenditure out of a total budget of RM295.217 million allocated to the Department. Source: *Annual Report for the Year of 2013*, Accountant General's Department of Malaysia.

examine the perceptions of the preparers and users about the usefulness of the ABC system. Thus, this case study will provide useful insights to improve our understanding of the process of implementing ABC in the AGD and to discover any issues and challenges encountered during the process.

1.2 PROBLEM STATEMENT

Researching in the context of public sector reforms in the NPM eras reveals the important roles and application of private sector management techniques to increase the public sector organization's efficiency (Hood, 1995; Siddiquee, 2006). However, there are relatively lack of comprehensive knowledge on the application of the private sector management techniques in the context of public sector organizations (Jakson and Lapsley, 2003; Pollit, 2002).

In the area of public sector reforms, the implementation of the new management accounting system, especially the new costing technique (i.e., ABC system) has been given greater attention by the past studies (Arnaboldi and Lapsley, 2004; Helden 2005). The adoption of the ABC system by the public sector organizations has raised much concern on the applicability of such technique in public sector context. Moreover, there was also concern on the issue of transferability of the private sector management technique in the public sector organization which were not an easy process (Arnaboldi and Lapsley, 2004).

Besides, the implementation of the ABC system in an organization deals with complex processes and surrounded by many technical difficulties and behavioural issues as been documented in the past literature (Anderson, 1995; Foster and Swenson, 1997; Krumwiede, 1998). The prolonged process of the ABC implementation has been reported by a number of prior studies (e.g., Anderson, 1995;

Arnaboldi and Lapsley, 2003). Further, investigations on the critical factors that would influence the success of ABC implementation process has been undertaken extensively by the prior studies (e.g., Innes and Mitchell, 1991; Shields, 1995; Foster and Swenson, 1997). For instance, past studies has found the critical factors in implementing the ABC system was to be related to the extent of top management support (e.g., Arnaboldi and Lapsley, 2003; Innes and Mitchell, 1991), adequacy of resources (Shields, 1995), role of external consultant (Innes and Mitchell, 1991), and the implementation training (Shields, 1995). The critical factors in implementing the ABC system should be given important concern by the organization in implementing the ABC system This is because, these critical factors would contribute to the success (or failure) of the ABC implementation in an organization (Krumwiede, 1998).

In relation to the implementation of the ABC system as a new costing technology in the public sector organizations, the complexities of the public sector organizations has become a major challenges that would deter the smooth process of ABC implementation (Arnaboldi and Lapsley 2003; 2004). The nature of the public sector organizations that are multi-service and have multifaceted operation increases the difficulties in implementing the ABC system apart from the complexity of the ABC system itself. Therefore, further investigation on the ABC implementation in the public sector organizations should be undertaken to enhance the understanding on the complex process of ABC implementation in public sector context. Majority of the past study was investigated the ABC implementation in a specific contextual setting (e.g., local government, healthcare sector) and focused in the developed countries (Arnaboldi and Lapsley 2003; 2004; 2005). Hence, a study of ABC implementation in other contextual setting, specifically in the developing country, would be useful to add empirical evidence on the ABC implementation in the public sector context. Thus, the

present study intends to provide useful information on the experience of the implementation of the ABC system in a public sector organization in Malaysia, as a developing country.

1.3 MOTIVATION OF THE STUDY

This study is mainly motivated by three issues. First, it is triggered by the recent changes that have taken place in the AGD. The AGD has adopted and implemented the ABC system as a new costing method to replace the traditional costing method used previously (i.e., the MAS). These changes that have been brought about by the implementation of this new sophisticated costing method might have a significant impact on this government agency performance. Further, it may reveal the effectiveness of the NPM agenda (adoption of private sector management technique) that serves the purpose to increase the public sector organization efficiency. This is because the AGD is among the biggest government agencies in Malaysia and it plays a central role in handling the accounting procedures for federal and state government organizations. Therefore, a study should be undertaken to gain an understanding of the implementation process of the ABC system as an accounting innovation in this particular government agency.

Second, the Malaysian government is creating a new public sector accounting landscape; by migrating from cash accounting to accrual accounting and a more comprehensive budgeting system, the outcome-based budgeting (OBB) by 2016 (Thomas, 2011). In this new accounting landscape for the public sector in Malaysia, the ABC system will be among the important management accounting tools to support the full implementation of the accrual accounting and the OBB. Thus, the ABC system will provide high-quality costing information to support the new Malaysian

public sector accounting landscape as noted by Thomas (2011). Hence, research on the early implementation of ABC in the AGD could provide some insights on the application of the ABC system in the Malaysian government setting. Therefore, this study attempts to highlight the implementation issues and challenges faced during the process of implementing the ABC system in the AGD.

Third, this study is also motivated by the relative lack of research on the implementation of the ABC system in public sector organizations in developing countries compared to that on the situation in developed countries. In addition, this study also attempts to investigate the actual adoption of and practices associated with a NPM mechanism (ABC system) in a public sector organization from the perspective of developing countries. Hence, it is hoped that the findings from this study can provide empirical evidence on the impact of this NPM mechanism in terms of improving the performance of public sector organizations from the perspective of a developing country.

1.4 OBJECTIVES OF THE STUDY

The present study generally focuses on examining the implementation process of ABC in the AGD, one of the key Malaysian government organizations. There are four research objectives (ROs) of this study as follows:

RO1: To explore and describe the implementation of the ABC system in the Accountant General's Department of Malaysia (AGD);

RO2: To examine the critical factors which would influence the ABC implementation in the AGD;

RO3: To provide insights on the usefulness of the ABC system in the AGD, and;

RO4: To discover the issues and challenges related to ABC implementation in the AGD.

To achieve the four research objectives stated above, four research questions (RQs) have been constructed as follows. These research questions are:

RQ1: How did the ABC implementation process take place in the AGD?

RQ2: What are the perceptions of the users and preparers on the critical factors which would influence the process of ABC implementation in the AGD?

RQ3: What are the perceptions of the usefulness of ABC among the users and preparers of the ABC system in the AGD?

RQ3: What were the challenges faced by the preparers and users during the process of ABC implementation in the Accountant General's Department of Malaysia?

1.5 SIGNIFICANCE OF THE STUDY

This study is expected to contribute in several ways. First, this study will contribute to the literature on ABC implementation in public sector organizations by providing some evidence from the Malaysian government context on the implementation of this NPM mechanism to improve the performance of a public sector organization. This is significant because there are only that few studies have explored the application of the NPM mechanism in terms of adopting a private sector management technique in a public sector organization from a developing country's perspective.

Secondly, this study will enhance our understanding of the implementation of ABC in the context of a government agency in practice and issues encountered during the implementation process. Finally, findings from this study are also important to the Malaysian government, the AGD and other government agencies as they will

highlight the important issues that might need to be addressed in implementing a new accounting system such as ABC. Thus, the results of this study can serve as a guide in improving the implementation process in other government agencies in the future.

1.6 ORGANIZATION OF THE STUDY

This study is organized into seven chapters. First, this chapter provides an introduction and overview of the study by describing the research background, problem statement, motivation of the study, research objectives, significance of the study, and organization of the study.

Chapter two discusses the literature review which presents a review of literature related to the area of research covered by this study, particularly ABC implementation and its application in the public sector context. Next, chapter three discusses the background of the AGD as the contextual setting of this study and highlights the historical development of the accounting system in this Malaysian government agency.

Subsequently, Chapter four discusses the relevant theory and framework used in this study to explain the research findings and help in answering the research objectives and research questions. Specifically, this chapter explains the NPM theory and the Arnaboldi and Lapsley's (2005) framework used in this study.

Then, Chapter five presents the research methodology of this study. This chapter explains the research method and research design of the study. In addition, this chapter also discusses the development of the research instruments and data analysis techniques used in this study.

Next, Chapter six discusses the results of the study. This chapter presents the results and the data analysis and also includes discussion of the findings. Finally,

Chapter seven summarizes the findings as well as the contributions of the study. This chapter also highlights the limitations of the study and suggests some future research directions.

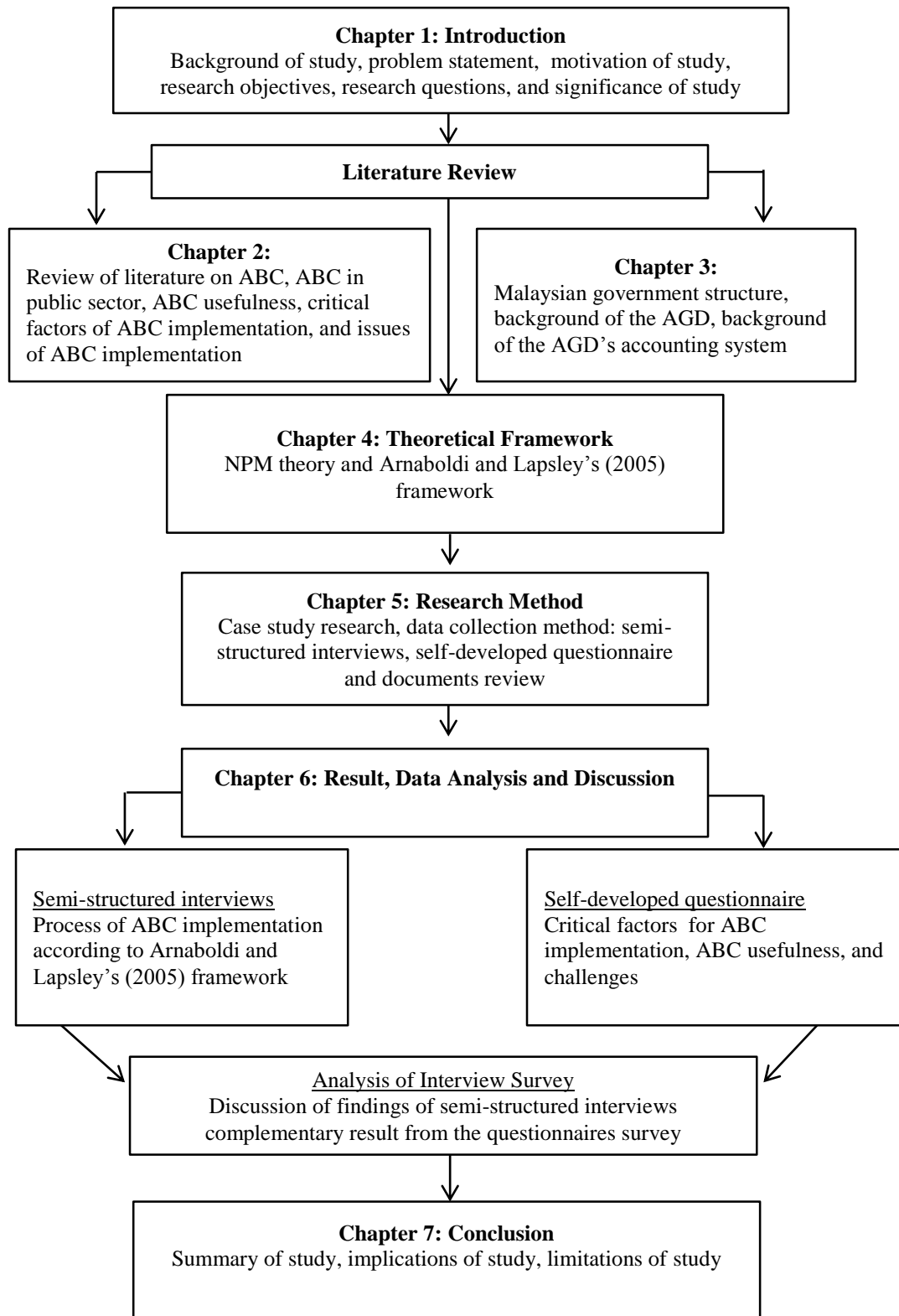


Figure 1.1 Structure of Thesis