GOVERNMENT BUDGET AND ACCOUNTING REFORMS IN THE UNITED STATES

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1. Introduction

American public budgeting and accounting is profoundly influenced by the federal system provided for by the United States Constitution. The federal government has its own fiscal laws and institutions. Federal budget rules are mostly codified in statutes and administrative regulations. Federal accounting rules are promulgated an advisory board sponsored by the principal federal fiscal officers and recognised by the auditing profession. Each one of the states has its own fiscal laws and institutions, which govern the state government itself and the local governments within its jurisdiction. Each state's budgeting practices are largely determined by its own laws and regulations, although a national advisory board has recently issued some voluntary guidelines. Professional influence has traditionally been much stronger in financial accounting for state and local governments. While these governments retain the legal authority over their accounting systems and internal reports, their external financial reporting has been subject to standards promulgated by complex institutional structures that combine technical expertise with a wide-range of political, economic and professional interests. In keeping with the federal and state/local distinction, the budgeting and accounting reforms at these two levels of government in the United States are addressed in separate sections of this paper.

The paper also observes the distinction between budgeting and accounting. Budgeting precedes accounting chronologically and provides accounting with the benchmarks to measure financial performance. The accounting system has other functions besides monitoring budget execution. One function is to provide data for the fair presentation of the government's financial position and operations to external users. Under the influence of this external orientation, government accounting and financial reporting has become more autonomous from budgeting. The separation has become so great that there now exist two distinctive professions and two bodies of knowledge. Consequently, budgeting and accounting are treated separately as well.

These lines of fragmentation create the four main sections of the paper (see Table 1). While there are differences among the 50 state and approximately 87,000 local governmental units, only the general pattern in the state and local government sector is covered in this paper. In case close examination magnifies the differences among the four cells in Table 1, the concluding section will attempt to detect some signs of harmonisation.

Table 1. The structure of American Government budgeting and accounting

	Budgeting	Accounting
Federal government	(1)	(3)
State and local sector	(2)	(4)

American public budgeting and accounting reforms have focused on changing institutions, processes and policies. An institution may be viewed as a coalition of interested parties working together to achieve a particular purpose. Coalition building is especially necessary in the American political system and government, because of the separation of powers and the extensive checks and balances between the legislative and Executive branches of government. Conflicts are almost inevitable not only because of differences of opinion, but they also result from the tendency of institutions to preserve their prerogatives in the governance structure. In order to mitigate the dysfunctional consequences of political conflicts, processes have been designed and changed to facilitate consensus building in policy-making in budgeting and accounting. Budgeting policies refer to the rules for the preparation, approval and execution of a budget. The term “budget policies” is reserved for decisions that affect the allocation and financing of the budget. We will focus on accounting policies promulgated by standard-setting boards, and not the rules of the thousands of state and local jurisdictions. In the United States, these policies include both measurement and disclosure rules that govern the form and content of financial reports, but do not prescribe systems and other means of implementation, e.g. the charts of accounts.

2. Federal budgeting reform

2.1. Introduction[1]

The budget of the federal government, accounting for almost one-fifth of the Gross Domestic Product (GDP) of the United States, is heavily influenced by both political and economic considerations. It is directly governed by a number of public laws that formally designate the decision-makers, prescribe their roles and, in recent years, specify its targets. This section examines federal budgeting reform in terms of the changes in the legal framework that provide for the institutions, processes and policies.

There are two types of federal budgeting laws. *Process-oriented* laws designate the players, assign their roles and specify the rules of the budgetary game so that the President and Congress can reach compromises more or less in time to keep the government functioning each fiscal year. The specific legal provisions reflect the political consensus regarding the proper sharing of the power of the purse. By and large, these laws have succeeded in erecting a relatively stable institutional framework for proposing and approving the federal budget. When disputes of a constitutional nature arise, the federal judiciary steps in to settle them when law suites are brought. The *outcome-oriented laws,* on the other hand, have been designed to achieve deficit reduction. Recent history shows they have had less predictable and successful results. In view of the complex interactive relationship between the federal budget and the economy, lower budget deficits cannot be preordained by law. Deficit reduction requires the facilitation of a strong economy that generates abundant government revenues.

There is another way to look at federal budgeting laws. The pre-1980 laws sought to exert *budgetary control,* while the post-1980 laws aimed at *controlling the budget.* Legislative budgetary control is reinforced by the machinery of government, including a compliance-oriented accounting system. It is, in short, an intra-governmental matter. In a mixed economy, controlling the budget - both on the revenue and spending sides - is much more difficult. Much depends on favourable economic conditions and the American public's attitude toward the role of government in the economy and in their lives. The federal budget is many things to many people. It is not only the government's financial plan. In the final analysis, it is the nation's blueprint for resolving conflicting values.

A remarkable feature of federal budgeting is the permanency of the institutions. New institutions were added, but old ones seldom faded away. This makes it difficult to understand the current or recent reforms without knowing past efforts. Similarly, it is also impossible to separating institutions, processes and policies. Institutions drive processes, which produce or are guided by policies over time.

2.2. The Constitution and early practices

The Constitution of the United States is rather concise with regard to the federal government's finances. It gives Congress the power to levy taxes and requires appropriations made by law before funds may be drawn from the Treasury. However, the Constitution does not provide a blueprint of the way in which Congress should exercise this power, nor does it assign a formal role to the President. Congress created a committee structure and devised rules to carry out its budget responsibilities. In the first half of the 1800s, these were handled mainly by the House Ways and Means Committee and the Senate Finance Committee. After the Civil War, both Houses of Congress set up Appropriation Committees. This arrangement enabled the House Ways and Means Committee and the Senate Finance Committee to concentrate on revenues. Congress also enacted the Anti-deficiency Act to regulate budget execution by: *i)* requiring apportionment - the allocation of appropriation by time period - to prevent overspending; *ii)* prohibiting government officials from incurring obligations in advance of appropriations; *iii)* forbidding spending in excess of appropriations or for purposes unintended by the appropriations. These injunctions remain the cardinal rules for fiscal conduct of federal government officials.

The early federal budgeting system permitted executive agencies to request funding from congressional committees without the President's control or even policy guidance. This practice continued until the early 1900s and caused President William Howard Taft to appoint a Commission on Economy and Efficiency. The commission observed and the President agreed on the need for a "national" budget, meaning one that covered the entire federal government. This precipitated a lengthy debate that eventually led to the passage of a comprehensive budget law for the federal government.

2.3. Foundation of the federal budgeting system

The legal foundation for the federal government's present budgeting system was laid initially in 1921 and modified in 1974 to redress a perceived imbalance of power. Two laws provide a stable institutional framework for preparing the ever weightier federal budget to meet ever expanding U.S. commitments at home and abroad during most of the 20th century.

Budget and Accounting Act (1921). Though 80-years old, the Budget and Accounting Act of 1921 retains a contemporary outlook because the system and institutions it established are still functioning. The act requires the President to submit a budget on behalf of the entire Executive branch and provides him with a budget staff to carry out this responsibility. All American presidents took advantage of the budget to set priorities, co-ordinate actions, and enforce policy. In the 1930s, President Franklin Roosevelt, recognising the value of the Bureau of the Budget, moved it from the Treasury Department to the Executive Office of the President. Later, President Richard Nixon expanded the agency's scope and renamed it the Office of Management and Budget.

Congress was quite specific about the information content of the budget in summary and in detail: appropriations requested and proposed revenues; estimates of expenditures and receipts for the budget year and the current year; the current year's appropriations; levels of indebtedness; past, current and projected financial condition of the Treasury; and other information about the financial condition of the government. The President is further required to explain how he intends to handle any budget surpluses or deficits, and is permitted to request supplemental appropriations. Federal agencies are required to comply with the President's information requests issued through the Bureau of the Budget.

The act's prescription for submission of the President's budget and the information contained therein has become a part of the permanent United States Code. While the dates and some details have changed, the essence of the system has remained intact. It is remarkable that the act envisioned an integrated (prospective) budget and (retrospective) accounting information system that the federal government is still using and enhancing.

During the next 50 years after the 1921 Act, the federal budget grew enormously as the federal government expanded its economic and social welfare functions domestically and acquired global military power. It also became a major fiscal policy tool of the Keynesian revolution in economic thinking about the government's role in managing the economy. It financed President Franklin Roosevelt's New Deal programs and America's expenditures during and after World War II. It similarly paid for President Lyndon Johnson's figurative War on Poverty and the real war in Vietnam. By the time President Richard Nixon assumed office, the power of the presidency had reached a historical height. Frustrated by having to fund an undeclared and unpopular war and by large presidential impoundment of funds over policy differences, Congress decided to reassert itself.

Congressional Budget Act (1974). The Congressional Budget and Impoundment Control Act were intended to strengthen the legislature's role by enabling it to produce a master budget and equipping it with the necessary analytical capability for the task. On top of the existing revenue and appropriation committees, each house of Congress added a Budget Committee and Congress as a whole gained a Congressional Budget Office (CBO). The centrepiece of the congressional budget process is the budget resolution, which sets ceilings for budget aggregate numbers. Procedurally, the act requires each standing committee of the House and Senate to review the President's budget proposal and recommend budget levels and legislative plans to the Budget Committee in each house. The Budget Committee then initiates the concurrent resolution on the budget to specify the desired levels for total receipts and for budget authority and outlays, both in total and by functional category (such as national defence, agriculture). As a direct consequence, the levels of budget deficit and debt are both set. The budget resolution allocates amounts of budget authority and outlays within each functional category to the committees having jurisdiction over the programs in each function. The Appropriation Committees are required to allocate the amounts to their constituent subcommittees. The budget resolution often contains reconciliation directives that instruct authorising committees to change the permanent laws affecting taxes and other receipts as well as entitlement programs in order to meet the goals contained in the budget resolution.

Upon the completion of Congressional action and the President's signature, the administration is charged with the faithful execution of the budget. Sometimes, the President declined to spend - or impounded - appropriated funds. Presidents may impound funds only under limited circumstances such as to provide for emergencies or to achieve savings. The Nixon Administration impounded funds on a massive scale and in order not to carry out policy objectives sanctioned by Congress. In response, Congress passed the Impound Control Act of 1974. The act requires the President to send special messages to Congress whenever he wishes to rescind or defer appropriated funds. For a proposed rescission to be effective, both the House and Senate must approve it within 45 days of continuous session. A presidential deferral takes effect and remains so unless it is overturned by an act of Congress.

In summary, budgeting is an unavoidable perennial political struggle, because without appropriations the federal government shuts down. The political price of public wrath over that outcome is high enough to encourage pragmatic compromises. The present federal budget system is the result of almost a century of returning the delicate balance of power between the Executive and the legislative branches. Even though the President enjoys the advantage of initiative afforded by the 1921 Act, Congress strengthened its institutional capability and created the vehicle for converting budgeting from an exercise of accumulation to one of division. These budget process "reforms" are essentially alterations in power-sharing agreements between the President and Congress. The next section describes another type of reform, one that sought to increase the responsiveness of the budget to Presidential leadership and policy.

2.4. Budget preparation reforms

In order to counter the insatiable appetite of the bureaucracy for ever-larger budgets, American Presidents from time to time exerted top-down control by decreeing new budget preparation methods. These do not require congressional approval. The most publicised efforts were President Johnson's Planning, Programming and Budgeting System (PPBS) and President Carter's Zero-Base Budgeting (ZBB).

The traditional federal budget at the present time consists of line items of proposed expenditures with appropriations by budget accounts and in terms of agencies. Such a budget format reflects the tight control of Congress over the administration. It tells what the government agencies are authorised to buy, such as personal services, materials, supplies, contractual services. PPBS challenged this annual, incremental line-item budgeting system in two ways: *i)* it lengthened the planning horizon to multiple years; *ii)* it sought to align resource requests to programs, i.e. the activities undertaken to carry out policies and achieve priorities. Even though PPBS as such is no longer required, it is still used by the Department of Defence and elsewhere, and its spirit lives on. Currently fashionable techniques like performance measurement, activity costing, and mission-budgeting are in some ways the reincarnation of the essence of PPBS.

The other budget preparation reform, ZBB, was conceived as an antidote to incrementalism, a budget practice that treats the previous year's base as given and focuses attention to the addition. In the extreme version of ZBB, nothing was sacred from budget cuts. Agencies were requested to justify every Penny. Priority-setting was enforced through the ranking of requests called decision packages". Eventually ZBB collapsed down the weight of the Paperwork it generated and did not survive longer than the Carter Administration. Similar to what happened to PPBS, the spirit of ZBB was revived in the Clinton Administration's National Performance Review, an exercise aimed at making government leaner and more effective.

In brief, reforms may be episodic but some of the basic values lived on. The current implementation of the Government Performance and Results Act, which requires strategic planning and output-oriented performance measures, echo the basic tenets of PPBS and ZBB. The other historical lesson is that no matter how rational and sophisticated the manner of preparing and justifying a budget, it did not prevent Presidents from submitting, and Congress from appraising, deficit budgets.

2.5. Deficit reduction measures

From 1969 to 1997, the federal government ran continuous budget deficits. As early as the 1970s, there was already concern over the effects of "uncontrollable" social welfare entitlement expenditures. However the amounts of deficits remained relatively small until the early 1980s. By then President Ronald Reagan's twin success in securing substantial tax cuts and increasing military spending pushed federal budget deficits to unprecedented levels. Congress reacted by making deficit reduction an explicit goal of budgeting laws, beginning with the Balanced Budget and Emergency Deficit Control Act of 1985.

Balanced Budget and Emergency Deficit Control Act (1985). Commonly called the Gramm-Rudman-Hollings Act, the Balanced Budget and Emergency Deficit Control Act of 1985 set out to balance the federal budget by 1991 by fixing progressively smaller deficit targets in the intervening years. If the projected budget deficit exceeded the specified target by more than the amount permitted, the cancellation of budget resources, called sequestration, would be triggered. The law was amended in 1987 to extend zero deficit targets to 1993 and to transfer the responsibility of determining sequestration trigger-point from the Comptroller General to the director of the Office of Management and Budget. History shows that, despite the threat of sequestration, the federal government continued to run budget deficits in each of the fiscal years covered by the law.

Budget Enforcement Act (1990). Since the 1985 and 1987 laws were unable to achieve their deficit reduction objective, Congress decided to try a different process through the Budget Enforcement Act (BEA) of 1990, which was extended several times. The chief innovation of the BEA is its recognition of the different nature of discretionary programs subject to annual appropriations and mandatory programs authorised by permanent laws. Discretionary spending, such as agency operating budgets, requires prior program authorisation by legislative committees and requires annual appropriation. The BEA sets dollar limits or "caps" on the total budget and on authority for discretionary programs. The caps are adjustable annually for: *i)* the difference between the actual inflation rates and the rates used in setting the discretionary caps; and *ii)* for emergency appropriations. Budget resolutions allocate budget authority and outlay amounts for discretionary spending. These amounts are further subdivided by appropriation committees to their subcommittees. If the appropriation acts for a year provide the amount of budget authority greater than the cap on budget authority, or if the amount of outlays associated with the budget authority is greater than the caps on outlays, the BEA calls for sequestration, or across-the-board cuts by a uniform percentage of most discretionary programs.

Unlike discretionary spending, spending for most entitlement programs - e.g. Social Security, health care for the elderly and the poor - are direct or mandatory because they are provided for in the laws that authorise these benefits to eligible individuals. Congress intentionally exempts these programs from the scrutiny of the annual appropriation process. The BEA does not prohibit spending increases for any discretionary program. It does, however, insist that such increases caused by legislation be deficit-neutral. That is, the increases will be "paid for" by decreases in some other program or by raising revenues. This compensatory mechanism is described as pay-as-you-go (PAYGO). Similar trade-off requirements apply to revenues: legislation decreasing one type of revenue must be fully offset by legislated increases in other revenue sources, or legislated decreases in mandatory spending. Change in mandatory spending or revenue caused by outside factors such as the growth of retired population or the expansion of taxable income are recognised but not subject to those types of control.

It appears that the BEA, reinforced by political leadership and facilitated by favourable economic conditions, had a measure of success in reducing the federal budget deficit and converting it into a surplus. The experience with GRH and BEA shows that budget deficits are reduced by political will, not by setting unrealistic goals. The threat of sequestration was not credible because Congress could - and did - undo the GRH Act's fixed deficit reduction targets. These were replaced by BEA's discretionary caps and PAYGO procedures. The more flexible and discerning approach of the BEA Probably contributed to its successful implementation. The larger explanation may be in the public's heightened sense of the approaching day of reckoning. When the electorate elevated deficit reduction to a priority, both Democrats and Republicans found the incentive to reach agreement to aim for zero deficit by the year 2002.

2.6. Lessons from federal budget reform

Several lessons may be drawn from federal budgeting reforms. First, the federal government had greater success in budgetary control than in controlling the budget, as evidenced by the 30 years of annual deficits. The federal government made itself worse off fiscally in order to make the public better off by providing politically popular benefits. Second, declaring fixed deficit reduction goals without considering the economy and the public expectations did not produce the desired outcome. Third, the conflicts and tensions in the budget process are the consequences of checks and balances, which have contributed to a moderate course of action. Fourth, projecting the costs of government benefits to recipients has become as important a budgeting exercise as deciding agency appropriations. Finally, changing budgeting institutions and processes did not necessarily deliver desired outcome, i.e. a balanced budget. The federal deficit or surplus depends greatly on the performance of the economy.

3. State and local budgeting reform

3.1. Introduction[2]

The federal budget preparation reforms described earlier have their roots in state and local governments, where budgeting reform has also been a continuous process. For example, New York City experimented with performance budgeting in the early 1900s and the state of Georgia tried zero-base budgeting in the 1970s. Even the Clinton Administration's Reinventing Government or National Performance Review effort was based on local governments' mission-driven budgeting. While the new tools and techniques have been similar at both levels of American Government, the evolution of their budget processes has been different. To understand and evaluate budgeting reform in state and local governments, it is important to recognise their distinguishing features.

American state and local governments are numerous and diverse. There are approximately 87 000 local government units in the 50 states. In addition to the multi-function general governments (e.g. cities and counties), there are single-function special districts that provide services such as elementary and secondary education, utilities, and parks and recreation. In general, these governments raise most of their own revenues, although the federal government provides considerable funding for some services, especially in urban areas. In the same geographical area, there are often overlapping jurisdictions that provide services, raise revenues, and borrow against the same tax base. Consequently while their services are complementary, they compete against each economically. This fragmentation has contributed to diffused accountability.

American local governments, as political subdivisions of the states, are subject to state laws regulating local revenue, spending and debt. They are often required to balance their budgets and are prohibited from borrowing money to cover deficits. Large local governments are often granted home rule with greater autonomy in fiscal matters. Property taxes are a main source of local tax revenue, while income taxes and sales taxes are the major state revenue sources. In order to limit tax increases, both state and local governments have increasingly resorted to more and higher user fees. Compared with the federal government, there is a greater correspondence between the taxes and fees paid and services received. Federal grants and contracts enable state and local governments to provide most of their health and social services to the poor.

State and local governments commonly have separate operating budgets and capital budgets. Subject to applicable debt limitations, they are generally allowed to issue bonds to finance capital projects. Private-sector bond rating agencies, such as Standard & Poors and Moody's Investors Service, evaluate the creditworthiness of the borrowers. Bond rating agencies consider, among other factors, the quality of management in determining bond ratings. As higher bond ratings lead to lower interest costs, governments have the financial incentive to improve their budgeting and financial management practices.

The budgeting systems of state and local governments share some common features. Their budget processes are generally led by the chief executive, who is assisted by a central budget office. Their operating budgets fund current services and are financed from current revenues, whereas their capital budgets are mostly financed by debt and intergovernmental grants. Under balanced budget laws, local governments must limit proposed expenditures to projected revenues. Deficits are to be financed through reserves or a combination of tax increases and service reduction. Finally, citizens have the right to examine government budget proposals, and to attend and speak at public hearings on local government budgets, although in practice they are often represented by interest groups or civic associations.

These practices are the results of reforms over a long period of time as discussed below.

3.2. Institutional reform

Nearly all of the institutional reforms in state and local budgeting occurred in the early decades of the 20th century. During that period, social reformers, often the business elite in major cities, sought to root out official corruption and reduce political patronage in municipal governments. They saw better budgeting as a way to improve government management. Reformers proposed the separation of administration from politics, for example, by creating the position of city manager, which requires professional qualifications and political neutrality. The demand for greater government accountability also led to the centralisation of management and the assignment of fiscal responsibility to the chief executive, such as the mayor or city manager. The chief executive was to prepare and present a budget for debate and modification by the legislature. The implementation of the approved budget would be the responsibility of the administration. Also during this period, there was greater division of labour in the finance function. Budgeting and accounting became separate functions. The tradition of independent audit was also established. This basic pattern of accountability, characterised by separation of powers and checks and balances, continues to this day in most state and local governments.

In the succeeding decades, this basic governance structure proved to be strong and flexible enough to accommodate other efforts to improve budgeting policies and processes.

3.3. Policy and process reforms

During the Great Depression in the 1930s, some state and local governments defaulted on their bonds due to reduced tax revenues but were still pressed to provide essential services. This created demands for better cost accounting methods and the use of performance measurement. In 1935, the Municipal Finance Officers Association (MFOA) advocated performance budgeting as a way to bring cost accounting data into the budget process. Fiscal problems also exposed weakness in budgeting and accounting procedures and the improper use of debt. State governments passed laws to restrict local borrowing and to require balanced budget and adherence to stricter accounting procedures.

The next major wave of budgeting reform occurred in the 1960s. As in the federal government, state and local governments experimented with the use of the budget as a planning tool. Initially, performance budgeting - tying dollars to agency performance -

was advocated and was combined with cost-benefit analysis to become the Planning and Programming Budgeting Systems (PPBS) system. In contrast to operational management and control, PPBS emphasised longer term planning and the clear identification of activities as a basis for resource allocation. The hope was that the comparison of costs and benefits would increase the rationality of budget allocation.

PPBS was succeeded by ZBB in the mid-1970s. While ZBB is identified with the federal government, it was first introduced into the government of the state of Georgia by then Governor Jimmy Carter. Its advocates saw ZBB was a tool to fight against incrementalism in budgeting. When government agencies took their current year's base for granted, policy-makers encountered difficulties in changing priorities and finding discretionary resources for new programs. Under the incremental budgeting system, legislatures similarly could only play a compliant role when review was limited to requests for additional amounts. Thus political leaders used ZBB to overcome bureaucratic inertia to change at a time when many local governments were facing fiscal strain. Fiscal crises forced governments to find ways to cut spending when raising revenue was no longer possible due to citizen propositions and referendums to impose limits on property tax. Such a climate was receptive for a new approach like ZBB, since it compelled government managers to justify the use of resources. However, when it was taken to the extreme of requiring justification for every budget dollar every year, the burdensome paperwork and time-consuming deliberations overwhelmed the capability of governments. The stress, need for sophisticated information, as well as the short-lived ZBB experiment became a symbol of impractical budgeting reform.

As in the federal government, even though PPBS and ZBB were abandoned as formal budgeting systems in most state and local governments, the need for strategic direction and rational economic choice remains. As these governments faced recurring pressures to cut spending, they responded by new techniques such as contracting out services and greater use of information technology ("electronic government"). This new breed of reform comes under the label "Reinventing Government," which is also the title of a popular book by Osborne and Gaebler. As their predecessors did, the current generation of reformers decry the dysfunctional bureaucracies and sought to give purpose to government. Their preferred budget tool is a results-oriented budgeting system that holds government accountable for accomplishments. This and other techniques are presumptuously labelled "best practices" by consultants eager to sell governments new solutions to old problems. Many of the prescriptions of *Reinventing Government* soon formed the basis for a federal initiative called the National Performance Review initiated by Vice-President Gore in the Clinton Administration. Upon closer examination from a historical perspective, this mission-driven and output-oriented budgeting bears a strong resemblance to PPBS and ZBB.

3.4. Lessons from state/local budgeting reforms

What lessons can be learned from a century of budgeting reform in American state and local governments? Some of them are captured in the *Recommended Budget Practices: A Framework for Improved State and Local Government Budgeting* recently identified by the National Advisory Council on State and Local Budgeting (NACSLB). Formed by the Government Finance Officers Association and seven other major public interest groups, the council issues what amounts to generally accepted budgeting principles. Since American governments have the legal authority to determine then- own budgeting practices, the council's recommended practices would complement but not replace budget laws and regulations. In recognition of the variation in size and complexity of American state and local governments, the council's recommendations are general. For example, according to the NACSLB, a "good" budget process:

1. incorporates a long-term perspective;
2. establishes linkages to broad organisational goals;
3. focuses budget decisions on results and outcomes ;
4. involves and promotes effective communication with stakeholders; and
5. provides incentives to government management and employees.

A major recommendation of the council was to involve *all* stakeholders - people with vested economic and political interests - in the budget process. While widespread participation might heighten conflict, the NACSLB believes that in the long run stakeholder involvement would lead to greater acceptance of budgetary decisions, which inevitably involves hard choices. Box 1 describes the 12 elements of a good budget process, which are elaborated by specific practices to provide guidance.

Box 1. **The 12 elements of the budget process**[3]

Establish broad goals to guide government decision-making
1. Assess community needs, priorities, challenges and opportunities.
2. Identify opportunities and challenges for government services, capital assets and management.
3. Develop and disseminate broad goals.

Develop approaches to achieve goals
4. Adopt financial policies.
5. Develop programmatic, operating and capital policies and plans.
6. Develop programs and services that are consistent with policies and plans.
7. Develop management strategies.

Develop a budget consistent with approaches to achieve goals
8. Develop a process for preparing and adopting a budget.
9. Develop and evaluate financial options.
10. Make choices necessary to adopt a budget.

Evaluate performance and make adjustments
11. Monitor, measure and evaluate performance.
12. Make adjustments as needed.

3.5. Summary on American public budgeting reform

American governments have engaged in four major types of budgeting reform: *i)* budget execution reform; *ii)* budget preparation reform; *iii)* budget institution and process reform; and *iv)* deficit reduction reform.

The goal of budget execution reform has been to make sure that public spending was legal and not wasteful. This kind of reform, usually initiated by the legislature, entailed improved financial record keeping, legal compliance audits and stringent internal control. Legislatures specified detailed line items in the budget and included specific restrictions in appropriations to limit administrative discretion. Thus legal compliance amounted to administrative obedience to legislative will. Budget execution can also be viewed from an economic perspective. American government auditing has long expanded to cover the evaluation of the economy, efficiency and effectiveness of government programs and operations. Such evaluations could not be confined to an examination of government operations; they often touched on the controversial issue of the scope and function of government. For instance, when more than half of the annual federal budget expenditure goes to providing social welfare benefits to individuals, value judgements permeate the evaluation of social programs.

Budget preparation reform attempted to marshal budgetary resources to achieve goals and carry out policy priorities. This kind of reform, typically initiated by the administration, steered budget discussions and requests to address the basic question: what is the money for? Sometimes new measures such as functional classification of spending are misinterpreted to be substitutes for the traditional line-item budget. They actually represent different ways of looking at the same dollar. Furthermore, they were built on the foundation of basic budgetary discipline. Otherwise, lump-sum appropriations would be an invitation to corruption, fraud and abuse.

The third type of reform changed the governance structure for making budgetary decision so that the pendulum of budget power settles near the centre. Historically, this kind of reform was undertaken in response to the dominance of one branch of government over the other. Many analysts have observed the political nature of the American government budget process. This is a natural consequence of the separation of powers, and of the checks and balances envisioned by the framers of the Constitution. The political struggles of competing forces prevented excesses from going on for too long and or doing lasting damage. This has accounted for the durability of the basic institutional framework over the past century.

The fourth type of reform aimed at reducing budget deficits. Most state and state governments have long been constrained by balanced budget requirements in constitutions or statutes. Lacking the power to print money, their deficits are limited by the willingness of the private-sector capital market to lend them money. The federal government is different. It can print money and its ability to borrow is finite but virtually limitless. Its awesome economic power, however, is matched by its unique responsibility for national defence and general welfare. When federal budget deficits reached hundreds of billions of dollars, Congress reacted by introducing fairly draconic measures such as across-the-board cuts if deficit reduction targets were not met. History has shown that those legislated targets were ineffectual. It took the capping of discretionary programs and forced trade-offs to bring the budget deficits down. While the government cannot be blamed for Americans' seemingly insatiable appetite for government benefits and programs, it does not deserve full credit for the disappearance of deficits in the late 1990s and the emergence of projected surpluses in the first decade of the 21st century. Unexpected growth in productivity arising from information technology, along with judicious monetary policy, produced the results surprising even to seasoned budget watchers. The fates of the public budget and the economy are tightly intertwined.

Today public budgeting reform remains a lively topic but its meaning is no more precise than in the past. Budgeting reform was initially equated with installing basic expenditure control mechanisms and accountability. Later it was expanded to making the budget a meaningful tool for decision-making and planning. Now, it becomes a part of improving government performance. While this puts budgeting in a broader governmental and societal context, it does not reduce the necessity of choice, which is at the heart of budgeting.

In view of the enormous importance of the public budget not only to government, but also to the society and the economy, it is not surprising that politicians want to maintain tight control. Admitting the political nature of the budgetary process and acknowledging the supremacy of elected officials in creating budgeting laws, most budget experts work on as technicians serving the will of politicians. In contrast, public sector accounting has a long tradition of professional influence, especially in state and local governments, as will be discussed in the next part.

4. Introduction

4.1. Federal accounting reform

The U.S. federal Government has long had a functioning budgetary accounting system that keeps track of the spending of budgetary resources in terms of obligations and outlays. The Anti-deficiency Act prohibits federal officials and employees from making commitments or expenditures in excess of appropriations or for unauthorised purposes. The effect of this old law was strengthened in 1982 by the Federal Managers' Financial Integrity Act, which held agency heads responsible for sound internal control to prevent fraud, waste and abuse. Today there is increased realisation that managing the government entails more than strict budgetary control. Competent public officials and financial managers make decisions and carry out transactions and activities to accomplish agency missions. The seed of the current institutional structure to provide information for decision making and monitoring the transactions and activities were planted early in the 20th century.

As explained in Section 2, the basic architecture of the financial system for the federal government was established by the Budget and Accounting Act of 1921, which created the Bureau of the Budget (BOB) and the General Accounting Office (GAO). As evidenced the title of the law, Congress intended a close relationship between budgeting and accounting. However institutional prerogatives encouraged by the constitutional doctrine of separation powers and the assertion of presidential authority in resource allocation, soon led to the fragmentation of the financial system. The General Accounting Office, headed by the U.S. Comptroller General with a 15-year term, belongs to the legislative branch of government. The Bureau of the Budget was transferred from the Treasury Department to the Executive Office of the President. As a consequence, in the budgeting and financial management area, the Treasury Department was reduced to the federal government's cash manager and bookkeeper. In contrast, the BOB and its successor, the Office of Management and Budget (OMB), by virtue of their proximity to the President, were recognised as the leading player in budget allocation decisions. A similar pattern has existed in individual executive departments and agencies. The budget office dominated the resource allocation process, and financial managers, including accountants, were relegated to secondary roles. This basic structure remained for several decades when the budget reforms dominated Washington. However latent tensions persisted.

American presidents since Franklin D. Roosevelt have regarded financial management, including accounting, to be an executive function that should be under the administration's control. However, Congress considered accounting policy to be an extension of its budget authority and oversight function. After all, the U.S. Constitution requires congressional appropriations before money can be drawn from the Treasury, which is required to provide periodic financial reports to Congress. Both of these requirements were used as justification for the legislative branch's involvement in making federal accounting policy. Specifically, the 1950 Budget and Accounting Procedures Act authorised the GAO to prescribe accounting rules and procedures to be followed by executive departments and agencies, whose accounting systems also had to be approved by the GAO. What Congress considered as its prerogatives was viewed by the Executive as legislative meddling in administration, leading not only to tensions but also potentially lost opportunity for improving the federal government's financial management.

Persistent and record levels of federal deficits, reaching close to $300 billion in fiscal year 1992, created a perception that the federal government's financial house was not in order. A sense of urgency emerged that more concrete actions were necessary than renaming the Bureau of the Budget as the Office of Management and Budget. In the 1980s, financial management, a routine bureaucratic function, became politically visible when frauds, waste and abuse were attributed to financial mismanagement. When investigations were conducted, a frequent finding was that the financial information from agency accounting systems was unreliable and inconsistent. This gave rise to the need for better federal accounting as part of improvements to federal financial management during the past decade.

4.2. Institutional reform

The creation of chief financial officers positions and the Federal Accounting Standards Advisory Board in 1990 provided the institutional foundation for policy reforms discussed in the next section.

CFOs.[4] The management side of OMB was strengthened by the 1990 Chief Financial Officers Act. The legislation designated a deputy director of the OMB as the Chief Financial Officer (CFO) for the entire U.S. Government and created similar CFO positions in executive departments and agencies. These officials form a CFO council for co-ordinating actions to improve financial management throughout the government. An Office of Federal Financial Management, headed by the Controller (not to be confused with the U.S. Comptroller General, who is head of the legislative audit office), was also established in OMB to spearhead the implementation of the act. The CFOs were charged with overseeing all aspects of financial management, especially the development and maintenance of integrated systems and the production of reliable financial information. The information would be used in part to prepare audited agency financial statements, whose form and content would be determined by the OMB and which would meet applicable accounting standards. These standards would be set through an interagency arrangement described below.

FASAB.[5] The 1990 CFO Act does not alter the traditional role of the Treasury in preparing the Annual Reports of the U.S. Government, or the GAO's status as the government's auditor. However, it added a complication to the already complex jurisdictional issue of who should set federal accounting standards. The act authorised OMB to determine the "form and content" of financial statements of federal agencies, but did not change the GAO's longstanding role in prescribing accounting standards. Fortunately, the secretary of the Treasury, director of the OMB, and the Comptroller General by 1990 reached an agreement to sponsor a Federal Accounting Standards Advisory Board (FASAB). The membership of FASAB was carefully calibrated to reflect the interests of all concerned: three from the sponsors, two from the federal agencies, one from the CBO, and three public (i.e. non-federal) members. Over the next decade, FASAB would recommend these officials to issue numerous accounting and reporting standards. The FASAB acquired greater stature and independence when its standards were recognised as generally accepted accounting principles by the AICPA in late 1999. At that time, the board's sponsors agreed to permit new FASAB standards to take effect unless they are vetoed by a sponsor during a 90-day waiting period.

4.3. Policy reform[6]

FASAB standards have affirmed the important role of accounting and financial reports in monitoring budget execution and in ensuring compliance and deterring fraud, waste and abuse. The board also believes that federal financial reports should assist their users in evaluating the operating performance of federal agencies, and in assessing the impact of the federal government's operations and investments on the financial condition of the nation. These objectives led the FASAB to recommend cost accounting standards in addition to financial accounting and reporting standards. Collectively the standards required the preparation and issuance of consolidated financial statements for the U.S. Government and its constituent component units under the full accrual basis of accounting.

Accrual accounting is not a new requirement for the federal government. As early as the 1950s, the Hoover Commission recommended accrued expenditures and this position was later supported by the President's Commission on Budget Concepts in 1968. The Bureau of the Budget and the Treasury Department attempted to implement the recommendation, but found that impractical. The FASAB's endorsement of the accrual basis has several new aspects. First, accruals would apply to the entire federal financial reporting model, and not selectively to particular programs or elements in the financial statements. Second, full accrual rather than modified accrual was recommended. This meant that the federal government's balance sheets would include present capital assets and long-term liabilities. Federal resources not recognisable as assets (e.g. national monuments) and federal responsibilities not recognisable as liabilities (e.g. social insurance benefits) would be reported separately in a "Stewardship Report." This approach acknowledges their importance and intractable conceptual and measurement problems.

The CFO Acts requires federal agencies to prepare, and submit for audit, financial statements for the entire organisation. The statements include: a balance sheet, a statement of net costs, a statement of changes in net position, a statement of custodial activities, a statement of budgetary resources, and a statement of financing. A statement of program performance measures is also required in compliance with another law. The experience at the agency level built the foundation for the release for the first time of audited government-wide financial statements for the fiscal year 1996. Even though the GAO issued a disclaimer with a long list of criticisms, it was a notable achievement in view of the size and complexity of the federal government.

4.4. Beyond accounting[7]

Federal accounting reform should be viewed in the context of cyclical waves of government management improvement reform. The results in the 1990s were made possible by activities in the previous two decades. During that period, GAO evaluations of government programs and operations often uncovered cost overruns and evidence of fraud, waste and abuse. Such information reinforced the popular American public distrust of government. Fighting waste in government is a favourite political campaign slogan to win public support for public office. Mounting deficits over three decades lent additional credence to the claim that the federal finances were out of control. Since accountants and auditors have a professional image of financial discipline and conservatism, their profile was raised in the latest round of financial management reform launched by the 1990 CFO Act.

Soon thereafter, the focus on finance was broadened to management by a series of legislation. In 1993, the Government Performance and Results Act required agencies to submit strategic plans and performance reports. The 1994 Government Management Reform Act required the audit of agency financial statements and the preparation and audit of financial statement for the entire U.S. Government. In 1996 the Federal Financial Management Improvement Act directed auditors to report on whether agencies were following systems requirements, accounting standards and the Standard General Ledger. These laws cemented a closer relationship between finance and management in general.

5. State and local accounting reform

5.7. Introduction[8]

As Section 3 indicated, each state, including its local governments, has its own fiscal institutions and laws. Even so, public finance professionals have been very influential in promoting good practices nation-wide. In the 1910s and 1920s, they sought to reduce corruption in municipal governments by advocating good financial record-keeping and other business practices. In the 1930s, the predecessor of the Government Finance Officers Association (GFOA) appointed a committee to codify municipal accounting practices. This effort continued intermittently for the next 30 years, resulting in a substantial body of professional guidance for government accounting, reporting and auditing in support of efficient financial management. After a series of municipal fiscal crises in the 1970s exposed poor accounting practices in some of the nation's large cities, changes were again made to the standard-setting institutional structure and to the accounting standards in order to improve the public accountability of government through full disclosure. These recent reforms are described below.

5.2. Institutional reform[9]

In 1974, the GFOA expanded its technical committee on accounting into a 21-member National Council on Governmental Accounting (NCGA). The NCGA drew its membership from the ranks of the fiscal officers of state and local governments as well as the federal government, the auditing profession, the financial investment community and the academe. The part-time members met monthly and relied on the GFOA for limited staff support. Around this time, a full-time Financial Accounting Standards Board (FASB) was established to set Generally Accepted Accounting Principles (GAAP) for business firms and non-profit entities in the private section. An arrangement like the FASB -with full-time members and staff along with adequate funding - became the goal of the organisations interested in improving state and local government accounting.

Also in the 1970s, many local governments and some state governments began contracting private-sector auditors - Certified Public Accountants (CPAs) - to perform financial audits in order to improve the credibility of their financial reports to the municipal bond markets. External audits usually evaluate financial presentations in terms of GAAP. However, NCGA standards were not recognised as GAAP by the AICPA, and the NCGA lacked the resources to substantially improve its work. Thus the search began in 1980 for an alternative standard-setting institutional structure.

The FASB wanted to preserve its status as the exclusive promulgator of GAAP and offered to set GAAP for governments. State and local governments were unwilling to submit to the authority of the FASB or a structure set up or dominated by the federal government. Unfortunately, due to their large number and diverse interests, state and local governments themselves were unable to create a standard-setting organisation with legitimacy, technical expertise and adequate financial support. Besides acceptance by the governments, such a body would need legitimacy from two other sources. The first was the AICPA, which as the professional association of auditors held the key to granting GAAP recognition. The second was the financial market as represented by the municipal bond rating agencies, which demanded financial statements audited by CPAs in accordance with GAAP.

After protracted negotiations, a Governmental Accounting Standards Board (GASB) was created in 1984 as a sister board to the FASB under the Financial Accounting Foundation, which was expanded by adding a number of trustees to represent the public sector. A broad-based Governmental Accounting Standards Advisory Council (GASAC) was also formed to represent not only the professional communities but also the political leadership, such as mayors, governors and state legislatures. To date, resource restrictions have limited the GASB to be essentially part-time with a full-time chairman and a full-time technical staff of a dozen professionals. The part-time members increased from four to six in number recently. After an interim period, the AICPA in 1986 granted the GASB standards the designation of GAAP. In the next section, we will examine how government GAAP have changed.

5.3. Polity reform

Until the mid-1970s, American state and local government accounting was dominated by budgetary practices. The budgeting system is organised in terms of funds, which are pools of financial resources to be used for specific purposes. Reflecting the separation between the operating budget and capital budget, the funds are similarly classified. The budget amounts were typically expressed in terms of cash and authorised obligations. In order to minimise conflicts with the laws that govern budgeting and financial management, and to meet the legal compliance objective, accounting principles required accounting and financial reports to respect legal provisions. So long as the reports are prepared for administrators and city council members, this approach was appropriate and probably sufficient. However, following the well-publicised municipal fiscal crises in the 1970s, external accountability received much more emphasis.

In response to calls for greater fiscal accountability, the NCGA in the 1970s adopted a number of measures. First, it declared that its nation-wide uniform standards would only cover governments' external financial reports, leaving the governments complete discretion to design special-purpose reports to meet legal requirements and management needs. Second, the multitudes of funds used in governments are classified into several generic fund types, which are then grouped as governmental fund types, proprietary (i.e. business-like) fund types and fiduciary fund types.[10] Third, proprietary funds were required to follow private-sector GAAP, and governmental funds would use the modified accrual basis and disclose comparisons with their budgets, if any, in year-end financial statements. Fourth, overview ("combined") financial statements, with each column representing one fund type, would qualify for "fair presentation" as required by GAAP. These statements and the detailed fund statements and other financial statistics would constitute the financial section of a government's Comprehensive Annual Financial Report (CAFR).[11]

When the GASB was established in 1984, it required the continued enforcement of existing NCGA standards in order to ensure continuity. In the next 15 years, the GASB adopted a total of 35 standards of varying breadth and depth on diverse topics. The most significant standards were Statement No. 11 that attempted to change the measurement method of governmental funds, and Statement No. 34, which substantially revised the structure and content of financial statements. These two statements are briefly described below.[12]

GASB Statement No. 11 was confined to dealing with the operating statement of the governmental funds, which report revenues and expenditures. The GASB decided that the flow of financial resources - instead of *current* financial resources - was the proper measurement focus for this financial statement, and an accrual basis - instead of the *modified* accrual basis - should be used. Instead of using cash receipts as a criterion for recognising revenue, the board was concerned with whether the underlying transaction had concurred and the government had demanded payment (in the case of taxes) or had a legally enforceable claim (in the case of fines, licenses and permits). Expenditures would be recognised to the extent of claims against the government's financial resources.

Furthermore, expenditures were to be categorised as capital expenditures *(i.e.* those giving rise to capital assets) or operating expenditures. The board reasoned that this approach would enable users to judge whether current-year revenues were sufficient to pay for that year's services consistent with the criterion of inter-period equity. Unfortunately, after its impacts on financial statements were assessed, the implementation of Statement No. 11 was indefinitely postponed.

The demise of Statement No. 11 led to further research and deliberations. Finally in June 1999, the GASB released a definite new reporting model in Statement 34. The statement requires governments to include both *government-wide* and fund financial statements as their basic financial statements. A management discussion and analysis is also required to give an overview of the government's financial activities.

The government-wide financial statements resemble the business and non-profit financial statements required by the FASB. They consist of a statement of net assets (formerly the balance sheet or statement of financial position) and a statement of activities (formerly the operating statement). Governmental and business activities are distinguished, while fiduciary activities are excluded. The financial statements will adopt economic resources as their measurement focus and use the (full) accrual basis of accounting. This means that capital assets, including infrastructure assets, will be included and reported in terms of their historical costs. These assets are to be depreciated as well and depreciation expense will be reported in the statement of activities. Depreciation is exempted for infrastructure which is part of a network (e.g. a highway system), if certain requirements to ensure their maintenance are met.

Statement No. 34 also requires fund financial statements for governmental and proprietary funds. Major funds are to be presented individually, while the other funds are grouped together for reporting. The measurement methodology would remain the same: modified accrual for governmental funds and full accrual for proprietary funds. The differences between the government-wide and fund financial statements are reconciled and reported.

It is likely that the merit of the new reporting model will be debated for the foreseeable future, as Statement No. 34 is gradually implemented. Several issues are involved. First, the addition of another set of financial statements could increase information overload and compliance costs. Second, collecting information about infrastructure is costly, and the value of information about its historical costs and depreciation expense is in dispute. Third, the contribution of the new reports to greater accountability and better decision-making has not been empirically demonstrated. Fourth, accruals could lead to greater divergence between accounting and budgeting, raising the contentious issue of funding long-term liabilities. For at least these reasons, the implementation of GASB Statement No. 34 will present great challenges to state and local governments and the GASB.

5.4. Observations on American government accounting reform

In the American federal system, the national government cannot dictate the accounting policies of the states and the thousands of local governments. In the past 25 years, each level of government has pursued government accounting reform at its own speed and in its own way, with no discernible co-ordination. However, as Sections 3 and 4 demonstrate, their approaches have converged in several ways:

- Government accounting standards are set by a quasi-independent boards with extensive inputs from all interested parties.
- The form and content of financial reports, rather than accounting mechanisms, are the focus of the standard-setting boards concerned with the government's demonstration of public accountability.
- Accounting and financial reporting standards are no longer dominated by budget concepts and practices.
- The accrual basis, which captures the long-term consequences of current decisions, is the common preferred measurement method.
- The financial status of the whole government is given priority in external reporting in order to provide a context for detail disclosures.
- Accounting numbers are accompanied by public officials' discussion and analysis of the government's goals and activities to facilitate user comprehension.

6. Conclusion

Three features characterise the American experience in reforming government budgeting and accounting. First, the reform process has been a long series of trial-and-error experiments. Second, institutional fragmentation has created a mosaic of similar initiatives in various places at different times. Third, in view of the above two characteristics, only limited conceptual harmonisation between budgeting and accounting has been achieved.

6.1. Reform as experimentation

Budgeting and accounting reforms have been a long drawn-out process in both the federal government and in state/local governments. Contemporary federal budgeting reform can be traced to the early decades of the 20th century. Major institutional reforms took place in the federal government, once every few decades, in 1921 and subsequently in the 1930s and 1970s. In the last 50 years, almost every decade had a "new" budgeting system associated with it: program budgeting in the 1950s; planning programming budgeting in the 1960s; zero base budgeting in the 1970s; and mission budgeting in the 1980s. It took almost 60 years - between 1930 to 1990 - to satisfactorily resolve the issue of who should set federal accounting standards. Once this was settled, it took another 10 years to come up with a fairly complete set of standards.

After settling in a relatively stable largely Executive-driven budgeting system, budgeting reform in the state and local government sector has a pattern similar to the federal government. Institution building in government accounting standard setting was arduous. It took five years of on-and-off negotiations to set up the GASB, and another 15 years passed before the GASB came out with a new reporting model.

Each reform was itself an experimentation. Regardless of whether institutions, processes or policies were the object of change, often the changes were not based on empirical evidence of costs and benefits, but on hopes or anticipation for a better way.

Sometimes revolutionary, sometimes evolutionary, the changes have continued for many decades with no end in sight. Thus it is best to view public budgeting and accounting as a continuous series of experiments.

6.2. Institutional fragmentation

The changes described in this paper were perhaps the response to the imbalances in the political system or conceptual framework. "When things are out of balance," a Chinese saying states, "they make sounds." The American system is particularly prone to internal imbalance because of its fragmentary character.[13] There are several types of fragmentation. The first type of fragmentation exists between the federal government and the states. Through the accountability provisions in federal grants and contracts, the federal government has influenced the budgeting and accounting practices of state and local governments. But these practices are implemented through the existing institutional structure of the states, which cannot be changed by the federal government. Tensions and conflicts are always a possibility because of the constitutional arrangement of federalism.

The second type of institutional fragmentation concerns the power sharing between the legislative and Executive branches. Legislatures have appropriation committees and staffs that check on executive budget proposals, second-guess economic assumptions and challenge spending priorities. While the process is messy, inefficient and ultimately political, that is an expected consequence of the separation of powers, and of checks and balances ordained in the Constitution of the United States and the constitutions of all states. Budgeting is generally a shared power between the legislature and the Executive in American Government, making it almost inevitably a political process. Financial management, including accounting and financial reporting, is generally regarded as an administrative function. But as we have seen, the American Congress has a tradition of attempting to micro-manage the government (at least from the administration's perspective).

The third type of institutional fragmentation is between the budgeting office and accounting office in the Executive branch of the same government. These two offices have different power bases and responsibilities. The budget director is usually an appointee answerable to the chief executive (the President, governor or mayor). A competent budget director is politically savvy, strategic and policy-oriented. The comptroller, or chief accountant, tends to be perceived as bureaucratic, operational and in charge of the details. In order to bring cohesion and effectiveness to the financial function, some governments have appointed chief financial officers; however the mandates of the CFOs vary. The budget director and comptroller have different rules to go by. The budget director is guided by the relevant laws and regulations of the government, or in the case of local governments, those of the states as well. Within the legal framework, there is room for innovations, such as a program budget to accompany the legally mandated line-item budget. The comptroller is obliged to keep the books in accordance to the applicable laws and regulations, he/she is also expected to follow national generally accepted accounting principles (GAAP) so that the financial reports can be given unqualified audit opinions. Inconsistencies and conflicts arise between law-based budgeting and GAAP.

While institutional fragmentation often produce inefficiency and conflicts, it also prevents any one of the contending forces from going to the extreme without encountering obstacles. The governance system in which American budgeting and accounting is embedded has the built-in capability to channel the conflicts into consensus most of the time, but not all the time.

6.3. Limited harmonization

While theorists can go on debating the merits of centralisation and decentralisation, as a practical matter, it is reasonable to assume that the current institutional structure for American public budgeting and accounting will persist for the foreseeable future. However, in view of the interdependency between the two levels of government, and between budgeting and accounting, harmonisation should be a long-term objective. In terms of the 2x2 scheme at the beginning of this paper, there are two types of harmonisation: vertical harmonisation between the federal government and state/local governments, and harmonisation between budgeting accounting (see Table 2). Institutional fragmentation will however slow or perhaps even prevent the harmonisation of American budgeting and accounting concepts and standards.

Table 2. Harmonisation possibilities

	Budgeting	**Accounting**	**Horizontal harmonisation**
Federal government	(1)	(3)	(1) and (3)
State & local sector	(2)	(4)	(2) and (4)
Vertical harmonisation	(l) and (2)	(3) and (4)	(1) and (2) and (3) and (4)

Presently there exists relatively greater conceptual convergence in federal and state/local accounting and reporting standards. Both the FASAB and GASB have favoured whole-government financial reporting under the full accrual basis, even though the GASB still retains fund financial statements in the new reporting model. Both boards also require the reconciliation of actual and budgeted financial results. Both lack the authority to set budgeting standards, and accept budgeting rules as the basis for making the comparison. In the absence of a necessity to reconcile their differences in the detailed standards, the conceptual harmonisation make be undertaken only as an academic (i.e. academician's) exercise in order to arrive at a more general model American governmental accounting.

A modest degree of conceptual harmonisation between budgeting and accounting at both the federal and state/local level has been achieved. The federal government is using the accrual basis in budgeting for the cost of credit programs (i.e. direct loans and loan guarantees) and in funding employee pensions. Some state and local governments are using the modified accrual basis instead of the cash basis in budgeting expenditures. The merits of accrual budgeting continue to be debated. The budgetary and financial consequences of accrual budgeting remain to be systematically estimated. Little is known about the degree to which budget standards and decisions are susceptible to the influence of accounting concepts and standards. Furthermore there does not exist an institutional mechanism for debating the issues because there does not exist a budgeting standards board for American governments.

As in the case of accounting, there does not exist a legal basis for the federal and state/local government to do their budgets in the same way. However, state and local governments depend in varying degrees on federal financial assistance, and have to estimate the amount, timing and uncertainty of such aid - a task made more difficult by different starting dates of the fiscal year. There are some encouraging signs that harmonisation, or at least experiences are exchanged. The federal government has looked at the states' experiences with line-item veto and biennial budget, for example. Again this seems to be an issue for professional and academic inquiries rather than governmental co-operation.

In conclusion, only limited conceptual harmonization can be expected from the system with so many separate institutions.

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NOTES

1. This section on federal budget reform draws from Chan (1999), Schick (2000), U.S. OMB (2000) and U.S. Senate Committee on the Budget (1993). Fisher (1975, 1991, 1993), Schick (1980a) and Trask (1996) discuss the historic contexts. Wildavsky and Caiden (1998) and Stein (1996) address related political and macro-economic issues.

2. This section on state and local budgeting draws on several types of sources. Hyde (1992), Gianakis and McCue (1999) and Gosling (1997) provide practices in general. Rubin (1998) describes historical evolution, and Briffault (1996) deals with balanced budget requirements. Schick (1980b) and Hammond and Knott (1980) analyses PPBS and ZBB. Peterson (1981, 1995) notes the limited abilities of cities to redistribute income. Osborne and Gaebler (1992) give examples of recent new management practices.

3. National Advisory Council on State and Local Budgeting (1998).

4. Bowsher (1995, 1987) discusses efforts by the GAO. Chan (1994) describes the background of the CFO Act; Jones (1993) and Jones and McCaffery (1992, 1993) critically analyse its implementation.

5. Bramlett (1991) and Bramlett and Rexford (1992) describe the formation of the FASAB. Steinberg (2000) provides a recent update.

6. Cuny (1995), Mautz (1991), and Rita and Eisenhart (1992) examine the nature of federal accounting standards, which are codified in FASAB (1997).

7. Philips, *et al* (1997) discuss the expanded role of federal financial managers.

8. Chan (2000) provides a comprehensive historic overview, while Remis (1981) examines the period from the 1930s to 1970s.

9. The transition from the NCGA to the GASB is discussed in Greathouse (1985), Chan (1985), Antonio (1985).

10. The governmental fund types consists of the general fund, special revenue funds, capital project funds and debt service funds. The proprietary fund types are made up of enterprise funds and internal service funds. The fiduciary fund types encompass trust funds and agency funds.

11. The nature of government GAAP is analysed in Johnson and Langsam (1991) for state and local government, and in Mautz (1991) for the federal government.

12. GASB Statement No. 11 (GASB, 1990) is critically analysed in Chan (1998). GASB Statement No. 34 (GASB, 1999) is described in Chan (2000b, 2000c).

13. This paper focuses on the professions of budgeting and accounting. Actually, others are involved as well. Most American governments have a treasurer, an auditor, some have an inspector general, and all have a legal department. Generally, the treasurer manages cash and investments. While the federal governments handle its financial transactions through the Federal Reserve Banks, state and local governments transact through commercial banks. Government auditors are usually appointed by the legislature, although some are elected officials. They may be authorised by law to audit the government or private-sector auditors may be engaged to perform external audits. Inspector generals, as the government's chief investigator, look into allegations of fraud, abuse and other illegal acts. The law departments make sure that all proposed transactions and activities, such as procurement contracts and grant applications, are in compliance with applicable laws and regulations. Chan and Miranda (1998) discuss the principles for designing a sound financial governance structure.