

January 2000

## **Powerful friends: the institutionalisation of corporate accounting practices in an Australian religious/charitable organisation**

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## Powerful friends: the institutionalisation of corporate accounting practices in an Australian religious/charitable organisation

### Abstract

The profile of accounting in the nonprofit sector has been raised substantially in recent years, due to profound changes in the institutional environment in which organizations in that sector operate. One of the factors that has resulted in the adoption of corporate-style financial management techniques, including accounting, in the nonprofit sector, has been the need for such organizations to achieve financial legitimacy. This can be achieved by means of their accounting practices, as they demonstrate a level of financial accountability that proves them to be legitimate recipients of funds from the public, from governments, and increasingly from the corporate sector. Although many nonprofit organizations are implementing more sophisticated accounting systems, little or no attention has been paid to the impact of those changes on individual organizations. Based on a year-long qualitative research study of an Australian religious organization with a large charitable services operation, this paper highlights the substantial impact the adoption of accrual accounting and corporate-style reporting had on its organizational culture, structures and practices. As the profile of accounting increases in similar organizations, and they face challenges in terms of organizational practices and mission imperatives, there will be a growing recognition that accounting technologies imported from the corporate sector may not be entirely appropriate for organizations whose agenda is something other than making a profit.

### Keywords

institutional theory, nonprofits, accounting, religious organisation, charitable organisation

### Disciplines

Business | Social and Behavioral Sciences

### Publication Details

This article was originally published as Irvine, HJ, Powerful friends: the institutionalisation of corporate accounting practices in an Australian religious/charitable organisation, *Third Sector Review*, 6(1/2), 2000, 5-26.

## **Powerful friends: the institutionalization of corporate accounting practices into an Australian religious/charitable organization**

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The profile of accounting in the nonprofit sector has been raised substantially in recent years, due to profound changes in the institutional environment in which organizations in that sector operate. One of the factors that has resulted in the adoption of corporate-style financial management techniques, including accounting, in the nonprofit sector, has been the need for such organizations to achieve financial legitimacy. This can be achieved by means of their accounting practices, as they demonstrate a level of financial accountability that proves them to be legitimate recipients of funds from the public, from governments, and increasingly from the corporate sector. Although many nonprofit organizations are implementing more sophisticated accounting systems, little or no attention has been paid to the impact of those changes on individual organizations. Based on a year-long qualitative research study of an Australian religious organization with a large charitable services operation, this paper highlights the substantial impact the adoption of accrual accounting and corporate-style reporting had on its organizational culture, structures and practices. As the profile of accounting increases in similar organizations, and they face challenges in terms of organizational practices and mission imperatives, there will be a growing recognition that accounting technologies imported from the corporate sector may not be entirely appropriate for organizations whose agenda is something other than making a profit.

## INTRODUCTION

The recent introduction of the Goods and Services Tax (GST) in Australia has raised the profile of accounting in third sector organizations, and has given visibility to a trend that has been developing over recent years. That trend is an increase in the spread of “countings and accountings” in the third sector, as a result of a spillover of financial management practices from both the corporate and government sectors. Whether or not this is appropriate, or the means by which it is being accomplished is appropriate, is the subject of this paper.

According to Booth [1995: 50], institutional isomorphism<sup>1</sup> means that management control practices from the commercial sector have been adopted by the voluntary sector, by means of the requirements of funding operations, institutionally acceptable practices and solutions, and professional networks. In addition, the growing and increasingly complex relationship between governments and religious/charitable organizations<sup>2</sup>, overlaid on general societal trends, has made pressures for conformity to acceptable financial management practices enforceable and essential. Since religious/charitable organizations are highly dependent for funding on both corporations and governments, they are vulnerable to pressures to conform to the management and accounting practices of those organizations.

The conventional view that accounting information acts like a mirror which “neutrally and objectively records the ‘facts’ about what has happened” in an organization, fails to recognize the notions that accounting projects an image [Roberts and Scapens 1985: 453 – 454], and that it is a socially constructed practice. Organizations can harness this image-creating potential for their own ends, with the profile given to accounting “less likely to reflect intrinsically necessary technical work processes than environmental constraints, resources, or

opportunities” [Meyer 1986: 346]. The rationalization of activity in any cultural setting contributes to the spread of accounting technologies, and the third sector is not immune to these trends.

This paper first introduces briefly the organization that was the subject of this study. Secondly, it examines the institutional environment in which third sector organizations, particularly religious/charitable organizations, currently operate in Australia. It focuses thirdly on the institutionalization of accounting practices in society, and fourthly considers the impact that the introduction of financial management practices from the for-profit sector had on one organization. It concludes by highlighting the implications of these trends on other similar organizations.

## **THE ORGANIZATION**

Hearts and Hands<sup>3</sup> is a large religious/charitable organization operating within the Australian context. It has a high profile, a good image, and is a successful fundraiser, relying heavily on government funding, corporations and the general public for the funds necessary to continue its operations. Its charitable work includes drug and alcohol rehabilitation, homeless shelters, counselling, childcare, women’s and youth refuges. Administration, including accounting, traditionally has been carried out by ordained members, but increasingly professionals are taking up these functions. The fieldwork stage of the study [Irvine 1999] took twelve months, with more than 100 interviews conducted, meetings attended, and reports and the minutes of meetings studied<sup>4</sup>. In the interests of anonymity, this introduction is brief.

## **THE INSTITUTIONAL ENVIRONMENT**

Shifting social environments [Mackay 1993] have led to huge social changes in Australia over the last forty years, resulting in an increase in social problems.<sup>5</sup> This is happening at a time when the current political discourse favours economic rationalism and a “user pays” philosophy. The dilemma for charitable welfare organizations is that while welfare needs have grown enormously, government funding is being increasingly linked to performance and organizations are having to look towards the corporate sector to provide funds in order to continue their operations.

### **Religious/charitable welfare organizations**

An Industry Commission Report [1995: 4] described the nonprofit charitable sector, in its role in delivering social welfare, as “a crucial partner with business and government, with which it is both complementary and contrasting”. The report stressed quality of service, together with increasing emphasis on fundraising, a “professional” relationship with governments, and greater management and financial accountability. It foreshadowed what is proving to be a more demanding role for charitable organizations. As their profile in the community grows, due to political initiatives and agendas, and their reliance on corporate donors grows, they are expected to achieve higher levels of efficiency and effectiveness. Organizations that do not attain these levels will be eliminated from the arena of welfare delivery.<sup>6</sup>

Religious/charitable organizations represent a substantial subset of the nonprofit community. Forced to take their place alongside and to compete with secular charities, they have had to

embrace modern management techniques as business and professional groups, and governments, exercise influence over their practices and demand certain levels of performance. In spite of this, they have their own unique set of parameters, including a primary purpose of achieving “social and spiritual aims”, a relationship with other nonprofit organizations which has been more cooperative than competitive, a greater use of volunteers, and a spiritual dimension which distinguishes them from secular enterprise [La Barbera 1991: 217]. That they play a major role in society is undisputed [Jeavons 1994: xiii], and they are particularly vulnerable to the need to promote an image which appeals to members or donors.<sup>7</sup> Their challenge is to set a balance between efficiency and effectiveness objectives, striving towards achieving their mission by means of operational objectives that are supported by financial procedures, rather than allowing the financial objectives to drive the organization [Parker 1998: 50, 52]. Meeting this challenge is difficult, given changing expectations about philanthropy and government funding.

## **Philanthropy**

Funding for religious/charitable organizations will come from the government, private donations, and, increasingly, ought to come from the business sector, according to the Australian Prime Minister. He called for corporate Australia to develop a “philanthropic tradition” as a recognition of its obligation to contribute to the community [Cleary 1998: 1]. Drawing on an economic argument, and the notion of “mutual obligation”, the Prime Minister suggested that because they depend for their success on thriving communities, businesses ought to contribute more than they were currently contributing (less than 5% of total donations) to charities. In spite of some high profile corporate donors, Australia undoubtedly lags behind the USA and Canada in corporate sponsorship [Lamont 1998a: 4]

and the sophistication of the philanthropy “industry”. Nevertheless, it appears to be heading in that direction, with “the serious business of fundraising (increasingly) taking place in the glass towers of corporate Australia” [Lamont 1998b: 4].

Attitudes to philanthropy encompass a variety of images, including its spiritual aspects [Bloom 1995] and its creativity as a positive community force [Martin 1994: 172]. It does have some pitfalls however [Martin 1994]. Hall [1990] suggested that with boards drawn from the business world, there were “intrinsic conflicts” between “the goals and managerial cultures of nonprofit and business enterprise” which had been exacerbated by the increasing professionalization of nonprofit management. While religious/charitable organizations are expected to provide a service, they are also expected to maintain and honour the ideas by which they were formed and which provide the inspiration for their service. Society’s expectations of philanthropic organizations are high, but are even greater if such an organization has a religious base, partly because the outward expression of religious values is an “essential facet” of their mission [Jeavons 1994: 58]. The tension, therefore, is to balance pragmatism and idealism, to balance the sacred and secular, to embrace financial accountability by adopting management and financial techniques from business and government, and yet to maintain actions that are appropriate for a caring, religious/charitable organization, whose concern is not primarily profit and financial considerations. As changes have occurred in the government funding environment, achieving this balance has become a great challenge for religious/charitable organizations.

### **Government funding**

Over the last two decades, following several reviews of the public service in Australia,



significant reforms have been implemented [Funnell and Cooper 1998: 80; Everingham 1998: 33; Adams 1997: 99; Guthrie and English 1997], which have placed Australia at the forefront of a world-wide trend towards managerialism in public sector management [Hopwood 1990a; Van Peurse and Pratt 1998; Hopwood 1990b; Budäus and Buchholtz 1996; Guthrie 1998; Guthrie and Humphrey 1996]. The effect of these changes has been fundamentally to redefine both the nature of public service “business”, and the way that “business” is carried out [Adams 1997: 99]. The new culture is based on “results-oriented management” [Shand 1990: 80], with a significant re-construction of the notion of accountability. It now encompasses more than a simple concern with regularity and legality in government processes (fiduciary accountability), being linked with the concepts adopted by the new public sector managerialism, such as economy (the control of inputs), efficiency (the relationship between inputs and outputs) and effectiveness (the “achievement of policy outcomes”) [Funnell and Cooper 1998: 33].

Because of these changes, the government funding environment has undergone considerable upheaval in recent years [Lyons 1997a: 206 – 207], with the community sector now being involved in a national ‘market’ of community services. The Australian government’s call for competition for government funding indicates a shift in its underlying philosophy, a reflection of the changing managerial culture that has been institutionalized within the public sector.<sup>8</sup> As the emphasis has shifted to follow economic rationalist principles, government funding has been linked to outputs rather than inputs [Ryan 1997: 23, 29; Melville and Nyland 1997: 49]. Service providers are now obliged to deliver service to the public in a way that is consistent with “administrative norms”, and to be accountable to the government, by means of constant monitoring of their activities [Meltz 1997: 191].

These new arrangements pose certain challenges for religious/charitable organizations that are dependent on government funding. The uncertainty surrounding the shift in funding arrangements leaves organizations unsure of the nature of their new relations with governments. As greater accountability is demanded, the possibility of a master/servant relationship could be resisted by organizations committed to maintaining their own distinctive mission [O'Neill 1997: 133 – 134]. The introduction of competition to a sector that has traditionally met needs in areas where markets have failed, also represents a huge culture shift [Lyons 1997a: 212], especially when confidentiality clauses in contracts prevent organizations from comparing or discussing funding agreements [O'Neill 1997: 136]. On a practical level, religious/charitable organizations are now faced with the necessity of providing increasingly complex documentation of financial and non-financial information, which places substantial burdens on them when their administrative resources are usually already “stretched” [O'Neill 1997: 130; Ryan 1997: 33].<sup>9</sup> The potential loss of autonomy of religious/charitable organizations that rely on government funding is a real concern to many organizations, in some cases providing a challenge to the fulfillment of their mission. The introduction of contracts and output-based funding, as examples of the new managerialism, highlight the potential conflict between the accountability due to the government as a funder and the accountability due to the organization's own objectives and philosophy [Robbins 1997: 76].

In all these changes, based on economic rationalism, managerialism, and public sector reforms, accounting has played a significant role. Cooper [1997: 30] suggested that “the ideology of capitalist neo-classical economics works through accounting and prevents other ideologies from being expressed”, and that accounting practices themselves and the major professional accountancy firms, have helped to develop the “climate of commercialization”

within the public sector environment, which has filtered through to organizations dependent on the public sector for funding.

## **ACCOUNTING IN SOCIETY**

Perceived to be a rational, calculative instrument, accounting represents an institutional pressure whose adoption by every organization is mandatory. Questions about accountability, technological expertise, rational decision making, and scrutiny of performance, all find expression in the craft of accounting. Institutional expectations are “powerful elements in the environment (which) can create demand for expanded accounting” [Carpenter and Feroz 1992: 622, referring to Meyer 1986]. “An ancient practice with a distinctive modern power” [Hoskin and Macve 1994:67], accounting’s emergence in the form in which it is now practised is not just a practical response to entrepreneurial challenges or a means of making rational decisions, but “a powerful new way of ‘writing the world’” [Hoskin and Macve 1994: 91]. Accounting claims a legitimacy that sets it apart from “political interests and intrigue”, since “the elegance of a single figure provides a legitimacy that, at least in certain Western societies, seems difficult to disrupt or disturb” [Miller 1994: 2 – 3]:

By avoiding discussions of moral and accountability issues, claims about the neutrality and apolitical nature of accounting practices and disclosures and the processes by which new practices and disclosures are required can be maintained. Yet, these actors deceive themselves [Young 1996: 509].

A link between calculative techniques and broader macroeconomic policies was highlighted by Tomlinson [1994] in a study on the rise in the concept of productivity as an economic factor in the UK. Accounting has played a major role in the way productivity has been measured. It has been institutionalized into everyday management activity at a micro level,

and at a macro level has provided the means by which macroeconomic goals have been measured [Hopwood et al 1994]. Accounting can be seen as a partner with government in the measurement and counting of values that are subject to macroeconomic policy. Similarly, the idea of efficiency and the discourse on "national efficiency" in Britain and the USA between 1900 and 1930, according to Miller and O'Leary [1994], created an environment in which cost accounting developed and flourished. As efficiency was promoted as a component of desirable social order, accounting provided a means by which it could be made visible, not only at an organizational level, but at an individual level [Miller and O'Leary 1994: 100]. It became more than a technical modification, but a new way of governing people and economic activities, and a central plank in political argument.

The partnership between accounting and corporations has provided another arena in which the impact of accounting's calculative techniques has been studied. Corporate structure and accounting control systems paint a portrait of the "budget-driven, line management-dominated approach to substantive industrial relations" which has emerged in many large British companies. While it has the appearance of being an "innocuous" technical activity, accounting has the capacity to integrate organizations at every level. It is capable of being "tactically mobilized" by management to further their own ends, and therefore is implicated, in a political sense, in the power relationships of the firm [Armstrong 1994: 191].

Accounting, therefore, can be viewed not as "some technical, context-free phenomenon" [Laughlin 1995: 82] but rather as a "social symbol", a form of invented language that aids in the spread and enforcement of values, within the organization, and the wider society [Dirsmith 1986: 358]. It offers more than legitimacy. Once introduced, accounting is a remarkable tool, capable of redefining organizational agendas. It can be seen as a process

of “organisational construction”, as “organisational realisation and enablement” [Hopwood 1989: 145]. It offers economic explanations of organizations and their activities, and has become "centrally implicated in the modern form of organizing” [Hopwood 1983: 287]. Management accounting and control systems have been described as playing a role in the production, regulation, and transformation of the *social fabric* of organizations, i.e. not only does accounting possess technical aspects, but it also affects the world we live in, in wide ranging ways [Macintosh and Scapens 1991: 131; Macintosh 1994; Miller 1994].

As new financial management practices have been embedded in the public sector, the emphasis on accounting, and the type of accounting employed, has changed significantly. The desire to make public sector organizations more efficient, to save public funds, and yet still to provide quality services, has resulted in the public sector’s now using accounting measures previously associated with the corporate sector [Van Peurse and Pratt 1998: 123]. With the shift in focus from cash budgets, compliance and expenditure control to accrual accounting, performance indicators, and performance auditing, public service providers have been increasingly exposed to accounting technologies [Guthrie and Humphrey 1996: 294], and accounting professionals have become indispensable members of highly professionalized “corporate management” teams in public sector organizations [Shand 1990a: 89]. The spillover of corporate-style accounting practices from the corporate sector through to the public sector and now to the nonprofit sector, is affecting nonprofit organizations in at least three ways, both directly and indirectly.

First, employees of religious/charitable organizations who are members of either The Australian Society of Accountants or The Institute of Chartered Accountants in Australia have a responsibility to comply with accounting standards and the performance codes of

their professional bodies [*Accounting and Auditing Handbook* 2000: 1186]. This means working to the highest standard of professionalism, attaining the highest levels of performance, and generally, meeting the requirement of serving the public interest. As a result of these requirements, both the external reports and the management accounting of religious/charitable organizations that employ professional accountants are subject to professional accounting standards.

Secondly, some aspects of professional accounting standards apply directly to nonprofit organizations (of which religious/charitable organizations are a subset), which are defined as “all entities whose objectives do not include the generation of profit, including a surplus, for distribution to members” [*Accounting and Auditing Handbook* 2000. 485]. Statements of Accounting Concepts (SACs), while not mandatory themselves, form part of the conceptual framework for the development and amendment of Accounting Standards relating to financial reporting [*Accounting Handbook* 2000: xxv]. SAC1 “Definition of the Reporting Entity” specifically tackles the issue of the type of reporting entity to which it refers. It transcends the type of organization, applying equally to the public or private sectors, and to business or non-business, profit or nonprofit entities. What it means is that if an entity has financial report users who are “dependent on general purpose financial reports for information for making and evaluating resource allocation decisions” [*Accounting Handbook* 2000: 5], then that entity must prepare its financial statements in accordance with Accounting Standards. This requirement hinges not on legal structure, but on the existence of "dependent users". In the case of charitable organizations that rely heavily on government and the public for funding, the argument could be made that there are "dependent users" who rely on the financial information those organizations provide in their financial statements. Consistent with SAC1, SAC2 “Objective of General Purpose Financial Reporting”, states that “general purpose

financial reports shall provide information useful to users for making and evaluating decisions about the allocation of scarce resources” [*Accounting Handbook* 2000: 23]. It makes frequent reference to religious/charitable organizations, specifically referring to its applicability to “churches, foundations, professional associations and charities” [*Accounting Handbook* 2000: 15]. Once again, the rationale is that because of the economic benefits of the “efficient and effective” use of scarce resources, and the reliance by religious/charitable organizations on donors for resources [*Accounting Handbook* 2000: 16], it is desirable that managements and governing bodies are held accountable, by means of general purpose financial reporting. As the level of accountability required by such organizations is raised, it is likely that many large nonprofit organizations, particularly church charities, which have not previously regarded themselves as "reporting entities", will be caught by this wider concept.

Thirdly, some of the changes to public sector accounting required by accounting standards have filtered through to religious/charitable organizations which are dependent on government funding, in terms of the financial reporting required in order to achieve and maintain funding, and the adoption of accrual accounting. The result of public sector reforms has been that since 30 June 1999, as required by AAS31 (Australian Accounting Standard 31) full accrual accounting has been adopted by governments in order to provide report users with “a comprehensive summary of their financial performance, financial position, and financing and investing activities [*Accounting Handbook* 2000: 284].

In 1974, Moonitz [1974: 146] asserted that the accounting profession should stay out of the nonprofit field for a long time, as far as accounting principles were concerned. He drew a distinction between the nonprofit sector and the profit-seeking sector on the grounds of their interest in the concept of net income: it was of little importance to nonprofit organizations,

but was “crucial and critical” to profit-oriented organizations. Fifteen years later, Mautz [1989:66] claimed that the nature and importance of differences between the two sectors appeared to have been unacknowledged, with the result that inadequate attention had been given to accounting for nonprofit organizations. He argued that nonprofits were so significantly different from business entities that they required additional elements and “quite a different reporting system”, and that it was possible to carry accruals “too far”, resulting in confusion. In spite of these differences, the need for adequate financial reporting by nonprofits must be acknowledged, if only to counter negative publicity from nonprofit disasters [Herzlinger 1996].

The structure of standard setting arrangements in Australia<sup>10</sup> has seen the "splitting" of standard setting boards on a "private versus public sector-basis", rather than a "business versus non-business-basis" [Leo and Addison 2000: 56]. The result is that while many accounting standards refer to the not-for-profit<sup>11</sup> sector, there are no standards that deal specifically with the issues unique to that sector.<sup>12</sup> This may change with the recent issue of a Policy Paper by CPA Australia [2000], which deals with financial reporting by not-for-profit entities. It openly acknowledges the failure of Accounting Standards that are designed for "businesses or governments" to meet "the specific needs of the entity and users" in the nonprofit sector [CPA Australia 2000: vii], and urges exploration of issues relating to the delineation of boundaries of not-for-profit entities, the types of users of not-for-profit reports and their information needs, and methods of measuring performance that are applicable to not-for-profit entities [CPA Australia 2000].

This recent interest and acknowledgement by the Australian accounting profession of the significance of the nonprofit sector and their failure to address their specific needs, is



consistent with a growing body of research from other disciplines that has highlighted the unique set of parameters in which religious/charitable organizations operate [La Barbera 1991; Jeavons 1994]. Organizations within this sector in the past certainly have done things differently from those within the for-profit sector, although it could be demonstrated that in many cases, in terms of financial management, the gap is closing rapidly [Parker 1998:50]. Although senior managers of religious/charitable organizations are interested in different information from the managers of for-profit organizations, increasingly they are required to adopt the accounting practices of the corporate sector, and now the newly corporatized public sector. Because religious/charitable organizations cannot be “closed systems”, i.e. they depend on the flow of resources from their external environment, understanding the institutional environment in which they operate is crucial to an understanding of their operations [Earles 1999]. They will be concerned about “bolstering their reputations, good standing and desirability as fund recipients in order to enhance and stabilise their resource flows”, and this will involve modelling themselves after other successful nonprofit organizations [Bielefeld 1992: 52 – 53], and adopting the practices of the organizations on whom they depend for funding.

The increasing sophistication of fundraising strategies, and the increasing pressures and restrictions placed on government funding have huge implications for religious/charitable organizations in terms of financial reporting and accountability. These organizations are being forcibly shifted from the practices of the pure nonprofit sector into the world of corporate high finance, and are being required more and more to compete in that arena, and to conform with corporate and government expectations. Whether or not it is appropriate simply to copy strategic management and accounting practices from the commercial sector is problematic, and consideration needs to be given to the nature and unique characteristics of

these organizations, and the potential stress that the imposition of business practices will have. Certainly, they need funds if they are to continue, but increasingly their ability to generate those funds is tied to their image, not only of caring, but also of corporate-style financial management and accounting. The next section focuses on the impact of such changes on Hearts and Hands.

## **THE IMPACT OF ACCOUNTING ON THE ORGANIZATION**

Hearts and Hands, as an organization, is acutely aware of the image it presents to its public, especially in financial matters. Not only does it need to be seen to be using donated funds responsibly, but its accounting practices must be beyond reproach. Its accounting has traditionally stressed the accurate recording of funds received, the careful tracking and control of expenditure, and the presentation of financial reports within the guidelines of currently acceptable financial reporting. As accounting practices have changed over time, it has been essential for Hearts and Hands to present a financial image in keeping with that which is valued and esteemed by society.

Hearts and Hands has a history of being open to its environment, relying heavily on the public not only for financial support, but also for technical expertise in an advisory or consultancy capacity. Because of this organizational culture, changes to institutional funding arrangements, a heavy reliance on government funding and a desire to attract more corporate sponsorship, the introduction of accrual accounting by Hearts and Hands was inevitable. A reliance on several external consultants' reports<sup>13</sup> also helped to set the scene for changes to financial reporting, resulting in the production of consolidated, accrual-based financial reports, and the introduction of accrual budgeting. The study of these changes provided a

fascinating insight into the impact of a huge structural and technical change on a conservative, hierarchical, religious/charitable organization, as new accounting technologies were introduced. It also revealed a dramatic cultural shift, as professional accounting requirements were implemented in an organization whose accounting had previously been performed by ordained members, for the most part untrained in accounting.

### **Business operations and external consultants**

Hearts and Hands is a strongly hierarchical, autocratic organization with a culture of decisions being made at the top levels of the organization by ordained personnel. Generally, those ordained personnel do not possess professional financial qualifications, even though they are responsible for millions of dollars in investments and make decisions that have huge financial implications. Traditionally, Hearts and Hands has relied on external consultants, either paid or voluntary, and on advisory boards made up of people from large corporations who volunteer their professional expertise on financial, marketing and administrative matters. This reliance has meant that Hearts and Hands has been very much open to its external environment, and open to influences from the business world, while still maintaining its own ordained decision making structure.

However, as the institutional environment in which Hearts and Hands operates has taken a more business-oriented direction, financial expertise has become a much greater necessity at the top levels of the organization. This has placed considerable strain on the organization at board level, as accounting information has not traditionally been the major source of input for decision-making. Were board decisions mission-oriented or money-oriented? The temptation seemed to be that while Hearts and Hands possessed the vast property resources it did, and

while there was a constant stream of legacies and bequests flowing in, there would be funds available to mop up the consequences of unwise financial decisions. After all, mission needs were seen to be paramount. On occasions when board members asked for accounting information, it was usually unavailable. The financial expertise of board members varied so much that some had difficulty deciphering accounting information, but had great expertise in understanding the way the organization operated. In the new competitive environment, these traditional arrangements were under threat.

One consultant's report which had far-reaching effects in the organization was a study based on Hearts and Hands retail outlets which sold donated clothing, furniture and household goods. Although it generated a significant profit each year which funded its drug and alcohol rehabilitation programme, it commissioned the report with the aim of providing "a fresh and objective look at the industry's operations and to make recommendations which would improve the overall efficacy and effectiveness of the industry whilst simultaneously improving profitability and control". The findings of the report were based on the establishment of benchmarks and key performance indicators (KPIs) in the areas of retail, production, transportation, raw materials and administration. One aspect of the report was to highlight overstaffing at a significant number of outlets, possibly the result of Hearts and Hands' charitable view of employing people who needed jobs. The recommendation of new strategies was in order to lift Hearts and Hands' performance to the level of the "big business" which it had become, by managing and controlling it according to "sound business practices". At the time of this study, a similar consultancy report was being prepared on aged care services, driven by the need to operate that segment of the organization's interests in a businesslike manner within an increasingly competitive environment.

To what extent were the recommendations of such reports implemented? This was determined partly by the level of resistance such changes brought. While the necessity for some change, in terms of fundraising and meeting the requirements of external agencies such as government departments, was a driving force, changes which affected the fabric of the organization and its mission were more likely to be resisted. The organization was forced to bow to institutional pressures, but it did not necessarily have to adopt them wholeheartedly or unreservedly. Constraints on moving towards business-oriented practices were practical in terms of personnel and expertise, cultural in terms of organizational structures and routines, and philosophical in terms of mission-orientation. The implementation of new accounting techniques was problematic for all these reasons.

### **Financial reporting**

Hearts and Hands' first set of consolidated, accrual-based annual reports was presented in 1997, at the corporate launch of their major fundraising appeal. It was significant, because it was an event focused on raising funds from businesses, and it unambiguously linked the request for funding with the promotion of a corporate financial image. Where, in previous years, 500 copies of the reports had been published, in this year 5,000 copies were issued. They were prepared not just to fulfill the strict letter of the law (Hearts and Hands' trust deeds and government requirements), or to deflect any criticism of their financial practices, but pro-actively to create an image of an up-to-date, financially responsible organization conforming with generally accepted accounting principles. An employee acknowledged that they were prepared as an exercise designed to attract corporate sponsorship.

These glossy reports provided no hint of the upheaval their production had cost the

organization. Once the decision was made to change to accrual accounting, it remained for it to be put into practice. This proved to be difficult, which was hardly surprising, given the strength of Hearts and Hands' unique hierarchical structure, conservative culture, and the initial absence of any meaningful training. Employees and ordained members struggled with the implementation, and while it was acknowledged as inevitable, it was only those who had some form of accounting training, who described it in a positive way.

A report prepared by an external consultant commissioned to provide accounting training for staff highlighted the negative impact of the adoption of accrual accounting, stating that "most centre and (divisional) staff cannot cope with the accrual accounting system and the accounting issues surrounding the transactions being processed". Some of the reasons identified for this problem were a lack of understanding of accounting issues, a lack of developed accounting policies, procedures and instructions, and a lack of adequate training. The difficulties were exacerbated by the tendency of Hearts and Hands', being a religious/charitable organization, to employ people "at the bottom end of the market". At some centres, employees "panicked and left because they couldn't cope with accrual accounting". The result was that poor quality financial information was produced, to the frustration of accounting personnel at the head office who were responsible for preparing the financial reports.

At every level of the organization, the gap between accountants and non-accountants, professionals and ordained members, was startlingly obvious. The Chief Accountant, a trained professional accountant, had come to Hearts and Hands from a large international corporation where he was able to produce fully audited accounts three weeks after the end of the financial year. To his frustration, it was not happening at Hearts and Hands, where the

consolidation process dragged on for months. He described his feelings of frustration at dealing with personnel, including ordained members of Hearts and Hands, who simply could not perform basic accounting functions, at receiving inaccurate and late information, and at having to institute a system of training well into the process, to try and overcome some of the difficulties that were being encountered.

The Chief Accountant was then responsible for dealing with problems caused by poor quality accounting information, and the result was frustration and time pressure for accountants at the head office as they struggled to “clean up” information and reconcile it in time for the external auditors to do their work. The difficulty was to find a “politically acceptable solution” to the identified deficiencies, with the result that a systems review was put into place, with an acknowledgment that it was accounting solutions that were required. One strategy adopted was to divide an administrative position, traditionally held by an ordained member, into two parts, one to be performed by a trained accounting professional. While many organizational members recognized the inevitability of this, it caused pain for some, as they saw decisions being taken out of the hands of ordained members and being placed into the hands of “outsiders”.

### **Accrual budgeting**

The most time-consuming, all-embracing, wide-ranging accounting task undertaken within Hearts and Hands is the preparation of the annual budget, which has undergone revolutionary changes in recent years. These changes have been the result of organizational restructuring, the switch to a global budgeting system, the introduction of accrual accounting, an increasing emphasis on computerized accounting and the influence of accounting professionals. All

these facets reflect an increasing emphasis on professional accounting techniques, following the practices of both the corporate and public sectors.

The budgeting system reflected the same cultural realities which were highlighted with the introduction of accrual accounting: it was a sink or swim system with little or no training offered, even though the people relied on to perform accounting functions had little expertise in that area. The introduction of a more sophisticated system made deficiencies in these areas all the more apparent. Another interesting organizational phenomenon was the reluctance on the part of some ordained members at head office to allow those lower down the hierarchy to take control of money. While the new system required the devolution of responsibility, the authority to accomplish this was handed over reluctantly, or not at all.

Just as there were frustrations at all levels of the organization with the introduction of accrual accounting, there were frustrations in the area of budgeting as well: personnel were untrained, budget requests were not accompanied by sufficient information, the system was unwieldy, the divisions were slow in processing budgets from churches and social centres, and the head office was slow in granting budget approvals. There was a general distrust of the head office and the accounting professionals, and a feeling expressed by those lower down the hierarchy, that they were out of touch with the implications of budgets on the mission of the various centres. Some felt their mission was being hijacked. One ordained member questioned who was serving whom in the budget process. He did not think they should adjust to suit “the accountants and systems people”, but felt that budgets ought to be audited not just in an accounting sense, on expenditure, but on their “values and priorities”. Another ordained member described his budget as “a faith and mission goal statement”, with another criticizing his treasurer’s budget as “what we’d expect an accountant to do”, stressing the need to see



“a little more faith in income projections”. Some people were upset when their budgets, carefully constructed to reflect their mission, were slashed either at divisional or head office without consultation.

The imposition of a business-oriented budget system onto Hearts and Hands’ traditional culture was not just a technical matter, but a reflection of a different philosophical approach to budgeting, that of breaking even, and thinking about the mission in economic terms, in a more stringent way than had been done in the past. One ordained member observed that “our whole costing and budgeting process does not help goal setting and mission focus”. This was obvious at the higher levels of the organization as well, as non-accountant board members struggled to come to terms with the new global accrual budgeting system. The chief financial officer of Hearts and Hands described the new budget as “a strategic and management planning tool”, and tried to streamline the budget approval process, without much success in its first year of operation. Members of the board, drawn from non-finance areas, did not usually have the opportunity to study budget reports before meetings, and consequently when they were confronted with vast quantities of data, often incomprehensible to them, they were not in a position to make informed decisions about budget approvals.

In the budgeting process also, distinctions between accountants and non-accountants were apparent. The increasing number of professional accountants, business managers and bookkeepers employed at social centres and in administrative positions at the head office and at divisional offices, meant that many ordained members were in a position of not understanding the tasks performed by people who operated under their authority. Unskilled in corporate accounting and management techniques, they were catapulted into a new system without adequate preparation. As the new techniques became increasingly valued within

the organization, some ordained members found this a threat, and a cause for concern, that these techniques may become more important than the achievement of Hearts and Hands' mission.

## **WIDER IMPACTS**

While the introduction of the GST has raised the profile of accounting in the charitable sector, it has not occurred in a vacuum. It represents a growing trend, demonstrated vividly by what occurred in Hearts and Hands, to introduce more sophisticated accounting and accountability procedures into a sector unused to corporate accounting methods. A few years ago Hearts and Hands was a conservative, traditional religious/charitable organization with a conservative, traditional nonprofit cash based accounting system. As a result of the necessity of meeting society's changing expectations of the nonprofit sector and satisfying the funding requirements of government, it was catapulted into a period of intense change as it adopted a new corporate-style accounting system. This had a significant effect on the organization's structure, culture and systems as it struggled to satisfy expectations for a higher level of accounting practice. Increasingly, accounting professionals were employed to perform tasks once done by ordained members. As accountants joined Hearts and Hands from the corporate world, they brought with them expectations of what accounting ought to be and ought to achieve in an organization. They wanted to improve accounting techniques, increase the use of accounting for decision making and set agendas for organizational structure and the development of an effective accounting system. The challenge for Hearts and Hands will be to maintain its mission in the face of increasing pressure to adopt accounting and practices from the corporate world.

This scenario, in different forms, is being played out in other religious/charitable and nonprofit organizations. The current economic reality is that the increasing involvement of business and business methods in charitable organizations represents a “fundamental shift in our institutional arrangements” [Hall 1990: 161]. With government spending cutbacks and greater demands for financial accountability from organizations that receive government funding, corporations are being sought as donors of funds and expertise for the benefit of nonprofits, and thus for the alleviation of social problems. Religious/charitable organizations are often the means by which this is accomplished, and they therefore need to conform to the practices of the organizations on which they rely for funding. The adoption of financial techniques from the world of business can result in pressure to compromise their mission and religious orientation, as accounting in religious/charitable organizations is influenced by professional accountants whose agendas may be different from those traditionally held by the organizations in which they work. The part that accounting plays in individual religious/charitable organizations is, therefore, highly significant and undergoing fundamental changes at the present time. More studies of the way these institutionally determined practices are being embedded in individual organizations will provide further enlightenment about the effects of these changes, about the nature of accounting as a powerful social and institutional practice, and about what constitute relevant and useful accounting and financial reporting guidelines for nonprofit organizations.

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<sup>1</sup> Institutional isomorphism is the process by which “organizations are driven to incorporate the practices and procedures defined by prevailing rationalized concepts of organizational work and institutionalized in society” [Meyer and Rowan 1977: 340]. By conforming with those practices and procedures, organizations achieve legitimacy, which enables them to compete for funding with other organizations in their field.

<sup>2</sup> Since the subject of this study is a large religious/charitable organization, the major focus is on organizations which have a religious base and are involved in the provision of welfare services. Other nonprofit organizations will have similar challenges as they attempt to find an appropriate balance between their not-for-profit agenda and the realities of providing welfare services in an increasingly competitive and corporatised environment.

<sup>3</sup> A pseudonym for the organization.

<sup>4</sup> This was a qualitative research project whose primary concern was the impact of accounting technologies on organizational practices [Irvine 1999]. Data was analyzed using the NUD\*IST (Non-numerical Unstructured

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Data Indexing Sorting and Theorizing) computer database. The story of Hearts and Hands presented in this paper is the result of that analysis. Where quotation marks are used in this section of the paper, the remarks are those made by interviewees.

<sup>5</sup> Kiely et al [1994: 9] identified some of these as “family violence, family breakdown, issues of public safety, inequitable geographic and socio-economic distribution of long term unemployment, growing homelessness, a rise in mental illness, the emergency of a ‘new poor’ and generational poverty”.

<sup>6</sup> This is illustrated by the English example, where one of the roles of the Charity Commission is to investigate claims of fraud and mismanagement in charities. Many charity managers displayed a “lack of experience and suitable skills for running a charity” [Francis 1996: 18 – 19], or worse, were guilty of maladministration and malpractice. The workload involved in monitoring the performance and management of organizations that go to the public for funds is huge and growing. Increasingly, charities will be monitored to ensure that they conform to acceptable financial practices.

<sup>7</sup> Parker [1998: 52] identified three categories of nonprofit organizations as “has-been”, “celebrity” or “star”. This status referred to the organizations’ image and consequent attraction of funds from donors.

<sup>8</sup> Funding practices have moved from a philanthropist and submission model, through a planning model to a competitive tendering model and eventually a quasi-voucher model [Lyons 1997b: 9 – 11].

<sup>9</sup> The introduction of business and marketing plans for some service providers is an illustration of this.

<sup>10</sup> The Australian Accounting Standards Board (AASB) and the Public Sector Accounting Standards Board (PSASB) have been the major standard setting boards in Australia.

<sup>11</sup> The Accounting Standards use the term “not-for-profit” where in most of this paper the term used is “nonprofit”.

<sup>12</sup> Some issues of particular relevance to charitable organizations include how to record donations (e.g. donations in kind, government grants, pledges), how to treat depreciation, and the concept of reserves [Leo and Addison 2000: 57].

<sup>13</sup> One report that particularly related to the organization's accounting system was prepared by a consultant who provided accrual accounting for staff. Another was a report prepared by a consultant of the organization's recycling business. It urged the streamlining of procedures and the introduction of benchmarking. The external auditors also prepared a report on the computerized accounting system.