

**The Impact of Privatisation on Management Accounting Control
Systems: A Case Study of two Saudi Arabian Privatised Companies**

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A Thesis Submitted in Fulfilment of the Requirement for the Degree of
Doctor of Philosophy

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November 2010

Abstract

Most of the literature on management control systems (MCSs) shows that state-owned enterprises (SOEs) lack autonomy, do not have clearly defined objectives, and therefore have inadequate accounting systems, accountability, and control systems. Whilst some researchers claim that privatisation per se should improve this aspect of enterprise performance and accountability, others argue that change cannot be brought about without accompanying structural, cultural and external environment changes. As a result of its economic reform policy, governmental development plans, the need to join the WTO, and the need to overcome the poor performance and ineffectiveness of certain industries, the Saudi Arabian Government privatised some of its SOEs.

This study is an exploratory investigation into the effect of such policy on two selected organisations and their MCSs in Saudi Arabia. Its main objective is to describe the nature of control systems before privatisation and determine the impact it has subsequently had on the companies in question. In addition, it investigates whether privatisation was the only reason for change or whether there were other influencing factors. The case study was conducted within two Saudi companies that have been privatised recently, viz., the Saudi Telecom Company and the Saudi Electricity Company. For triangulation purposes, the case study employed three modes of data collection: semi-structured interviews, examination of classified official corporate documents, and semi-structured interviews with an external related party (the Saudi Investment Authority).

The main finding of the study is that privatisation alone cannot change MCSs: without changes in organisational structure, culture and the external environment, the privatisation process cannot effectively achieve its objectives. The study found out that although both companies were privatised, changes in their respective control systems were different for three main reasons. (1) The degree of competition: the telecommunication sector becomes more competitive and therefore the Telecom Company had to develop very efficient control systems so it could compete in the market. However the Saudi Electricity Company continued to dominate the market and as result there was no strong motive to apply stringent MCS. (2) Managerial power within the two organisations: Whereas in Saudi Electricity engineering managers were dominant and therefore highly influential on the kind of changes the company was seeking, in the Saudi Telecom Company accounting managers dominated and were very different in their attitude towards changing control systems. (3) Government involvement: Saudi Electricity had very limited autonomy since the Government was still the main decision maker on factors such as pricing and policy, whereas Saudi Telecom had a considerable level of autonomy in its policy making.

DEDICATION

This thesis is dedicated to my Parents for their patience, prayers and spiritual support over the years. It is also dedicated to my brothers, sisters, wife, and friends

Acknowledgment

Verily all the praises are due to Allah. By his grace, guidance and help, Allah has made easy the completion of this thesis. May Allah benefit with it readers; he is all hearer and all responsive. Thanks are due to many people for their helpful comments and contributions.

I would like to offer my sincere thanks to Mr. Simon Pallett for supervising my work during the past years. His valuable critical and insightful comments and suggestions on initial drafts of each chapter of this thesis together with his overwhelming encouragement and support at all stages of my study were invaluable and much appreciated. I would also like to thank Dr. Lana Liu for being very helpful and supportive.

I wish to record my appreciation to Umm Alqura University for granting me a scholarship to pursue my PhD study. I would also like to record my gratitude to the two organisations for allowing me access to conduct the empirical research and to all individual participants within these organisations for the generous time they spent with me and great enthusiasm shown during the conduct of the empirical work. Without their assistance and cooperation this research would never have been completed. Special thanks are extended to Mr. Abdulraheem Alanazi from STC and Mr. Naif Alnofaiee from SEC for their arrangements and cooperation.

I would like to express my sincere and heartfelt gratitude to my parents for their patience and prayers. Without them, not only would this work have been impossible, but also the inspiration underlying it would not have been allowed to flourish. I would like also to pay special tribute to the patience, understanding and support of my brothers, sisters, and wife.

There are also other friends who were not directly involved in the research but who gave me a lot of support and encouragement as well as providing me with much information and data. I appreciate all the help and support I received from them.

Last, but not least, I would like to thank Dr. Naif Binlebdah, Dr. Mohammad Alsumairi, Dr. Ibrahim Alshahrani, Mr. Saad Alqahtani, Mr. Faihan Binlebdah, and Dr. Mofareh Alqahtani. I hope I have not forgotten anybody; if I have, I thank them too and hope they will forgive me for that

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Chapter 1: Introduction

Introduction

State-owned enterprises' (SOEs') reform is a worldwide phenomenon. Since the 1970s, governments throughout the world have undertaken reforms that improve the market-orientation of their policies, e.g. trade liberalisation, deregulation of domestic markets, and privatisation of SOEs, in order to improve economic efficiency and maintain long-term growth (Campos and Esfahani, 2000).

State-owned enterprises, mainly in developing countries, are often inefficient and insufficiently accountable due to many factors, for example, lack of clearly defined objectives; overstaffing; lack of resources; time and cost overruns; inefficiency of huge inventories; poor quality products; lack of autonomy, control, qualifications, competition and incentives linked to performance; inadequate measures for judging performance; insufficient compensation and training; lack of necessary information due to inadequate accounting systems; weak management; wrong or controlled pricing policy; recruitment, promotion and training policy; lack of auditor general power; ineffective internal or external control; inadequate financial targets, and failure to expand services to meet rapidly growing demand (Harris, 2003; Ayub and Hegstad, 1986; Shirley and Nellis, 1991; Shirley 1983' Aharoni, 1986; Singh, 2000; Ramamurti, 1991; Pallot, 1998; McCrae and Aiken, 1988). Privatisation has made accounting research more significant. The policy of privatisation has become an important element in the development programme of developing countries. Accounting is considered as the driving force in these new policies (Sobhan, 1991; Wickramasinghe, 1996; World Bank, 1995).

During the past two decades the Kingdom of Saudi Arabia has been the subject of rapid economic development in all areas, including the business sector. Therefore, in Saudi Arabia, a privatisation programme has been initiated to overcome the inefficiency of the public sector and to achieve economic development. It is assumed that under the privatisation programme management control systems will become effective, of the

change to private ownership (Uddin, 2004). The main objectives of this research are to study the changes that privatisation has made in management accounting control systems (MACS) in privatised Saudi Arabian companies, and find out whether privatisation alone has an effect on MACS or there are other factors that have been taken into consideration.

This chapter aims to describe the research problem, starting with describing the background of the study, then declaring its aim and objectives, specifying the research methodology and outlining the structure of the thesis.

1.1 Background of the Research Problem

Saudi Arabia is a comparatively young country, established on 18 September 1932. The Saudi government took advantage of the oil boom years in the 1970s, and established a modern state and world-class infrastructure as an instrument to speed up development in the country, including railways, airlines, ports, water, electricity, postal and telecommunications activity. At that time, the government was the only body able to establish these huge projects to fulfil basic requirements and provide public services to the society. However, during the last three decades, the Saudi economy has witnessed growing budget deficits coupled with high population growth, low investment in infrastructure, and poor performance and ineffectiveness. As a consequence there has been increasing pressure to restructure and diversify the Saudi economy in order to engage in the global trend towards enhancing the efficiency and effectiveness of the public sector and developing the private sector. Therefore, privatisation has become a necessity for state-owned enterprises, which are considered major players in economic performance and social activities in the country.

Advocates of privatisation presume that ownership changes will induce superior management accounting controls, and hence greater productive and allocative efficiency (Adam et al., 1992; Vickers and Yarrow, 1988). It is assumed that under the privatisation programme, management accounting control systems will be effective as a result of private ownership. According to most accounting studies, the market mechanism indicates how business functions should be performed. Having received a

signal from the market mechanisms, a management accounting control system can formulate appropriate strategies and control mechanisms for the enterprise (Uddin, 1997). However, there are some studies which question the belief that privatisation can be the only cause of the change in the management accounting control systems in privatised organisations especially in developing countries (Uddin and Hopper, 2003; Wickramasinghe and Hopper, 2005). Flamholz, Das and Tsui (1985) state that the three elements of the context of management control (external environment, organisational structure, and organisational culture) can be effective as well as the change on the ownership status.

The interest in changes in management accounting control systems due to the changes on ownership signify a need for research on accounting in the context of recent changes in developing countries. Unfortunately, no attempt has been directed towards understanding the management accounting control systems and privatisation in Saudi Arabia. As far as the research shows, almost all authors have been concerned with financial accounting. This study is motivated by this deficiency. Therefore, this study aims to investigate the changes that occur in management accounting control systems after privatisation and explore whether privatisation was the only reason for the changes or whether there were other factors.

1.2 Aim and Objectives of the Study

It appears that there is lack of empirical literature and clear understanding of management accounting control systems in privatised Saudi Arabian companies. In principle, this study will attempt to investigate the changes that appear in management accounting control systems due to the privatisation in Saudi Arabia. It is hoped that such a study will make a highly significant contribution to knowledge in general and to the organisations and the government of Saudi Arabia, as the government is in the process of privatising other state-owned enterprises. Its importance to the organisation and the Saudi economy in general can be gauged from the fact that a large number of participants in the research enthusiastically asked to be shown the final report of its findings and recommendations. This may also be because of the general dearth of this kind of research work in the Saudi public and private sectors.

This research has the following objectives:

1. To investigate the nature of change in management accounting control systems in the two post-privatisation Saudi companies;
2. To determine the factors other than privatisation that led changes in the management accounting control systems in the selected companies;
3. To examine whether privatisation improve management accounting control systems or not;
4. To examine the impact of cultural, political and structural factors on the changes in the management control systems of Saudi privatised companies;
5. Propose recommendations drawn from findings relating to Saudi privatised companies that might assist the government of Saudi Arabia when it privatise other organisation.

To address these objectives, the following research questions were developed:

- I. What were the changes that appear in the aspects of management accounting control systems in privatised Saudi companies?
- II. What were the factors that affected the changes on the management accounting control systems other than privatisation?
- III. Does privatisation improve management accounting control systems?

This research is not intended to be a comparative study of the impact of privatisation on management accounting control systems in different countries, but a comprehensive analysis of changes on management accounting control systems due to privatisation in the Saudi Arabian context. It is not intended to generalise the findings to other companies on other countries, as it is well known that cultural, legal and political differences exist between countries and that findings from one context cannot be extrapolated to another.

1.3 Research Methodology

The design of research in management accounting can take several forms: it can be either normative or positive and it can be based on either theory or practice. The major methods used will be descriptive case study and semi-structured interview surveys.

In order to accomplish the research objectives, the researcher needs first to have a general understanding of the organisational practices and values that influence management control systems. Thus the first stage of this research is devoted to reviewing the literature on management accounting control systems in general and its relation to privatisation in particular. This investigation aims to provide a better understanding of the meaning, aspects and the boundaries of these phenomena.

This empirical study is based secondly on extensive in-depth interviews with respondents at various levels in two Saudi privatised companies and 3 governmental officials. The purpose of these interviews is to explore the investigated organisations' previous and current MACS and the role of privatisation in changing it. The examination of highly confidential organisations' documentations is used on the study. As a result, this case study employs a methodological triangulation approach, combining qualitative methods and documentation, through the complementary use of primary data (interviews) and the examination of highly confidential documents (secondary data) pertaining to the MACS of the organisations.

In terms of validity, as noted earlier, it is not intended to generalise the findings of this research to other companies or SOEs. Hence, external validity is not a concern here; instead, the focus is on internal validity. In other words, could the research be repeated to produce the same results? The research was designed to meet this criterion. More details concerning the utilisation of these methods and data analysis techniques are to be found in Chapter Four.

1.4 The Significance of the Study

As stated earlier, this study seeks to explore and understand the changes that occur on MACS as a result of privatization in Saudi Arabia. A number of arguments justify the

importance of this study. First of all, the importance's of the issue of management accounting control systems and changes in them to all companies in any country. Second, privatisation in Saudi Arabia is a new issue that needs more in-depth investigation, especially due to the lack of empirical literature and clear understanding of MACS in Saudi SOEs and private companies. Third, as far as the researcher is aware, this study is the first empirical exploration of management accounting control systems and the changes that appear in it as a result of privatization in any country that is a member of Gulf Co-operation Council (GCC)¹ including Saudi Arabia. Fourth, this study will provide policy makers in any developing country especially Saudi Arabia with information on the steps and the aspects that the country should take in any privatized sector in order to enable the privatization policy to be affected in regard to MACS. Fifth, because the study is conducted through interaction with the subjects, this will enable the individual organizational actors to come to a better understanding of themselves and the MACS in their respective organizations. Sixth, it is anticipated that the results of this study will be useful not only to Saudi Arabia but also internationally, to private investors because it will clarify many current and future obstacles regarding MACS, and it is hoped that other developing countries, especially the members of GCC which have a similar environment to that of Saudi Arabia, will benefit from the knowledge gained. This knowledge should allow future useful comparisons and extrapolations. At the national level, the study is hoped to be of particular interest to state-owned enterprises' managements, controllers, boards of directors and decision makers, the Ministry of Finance, the Ministry of Planning and Economy, the Consultative Council, General Investment Authority, Universities, Educational and Training Institutes, Accounting and Consulting firms, Banks, and Potential Investors. Internationally, this study will attempt to fill the wide gap in the international literature on management accounting reform that stressed by Enthoven (1998) and Lapsley (1993).

1.5 Structure of the Thesis

The thesis consists of six chapters including this introductory chapter (see Figure 1.1 The Structure of the Study).

¹ This is including Saudi Arabia, Kuwait, Qatar, Oman, United Arab Emirates, and Bahrain.

Chapter One provides a general overview of the research problem under investigation. It discusses various issues, including the background to the research problem, research objectives, research methodology, the significance and importance of the study, and the study structure.

Chapter Two gives an overview of the Saudi economy, a brief history of its political systems, a review of major economic developments, directions of development planning in Saudi Arabia, reasons for applying privatisation policy in Saudi Arabia and sectors that candidates for privatisation, other countries experiences with privatisation including developed and developing countries, and overview of the two organisations under study.

Chapter Three contains the literature review; it examines the subject of management accounting control systems and provides a broad overview of the relation between privatisation and changes on MACS. It provides a better understanding of the main themes and aspects of MACS in general and the changes on them due to the privatisation. Finally, it provides us with a clear expectation of the changes on MACS because of the changes on the ownership status (privatisation).

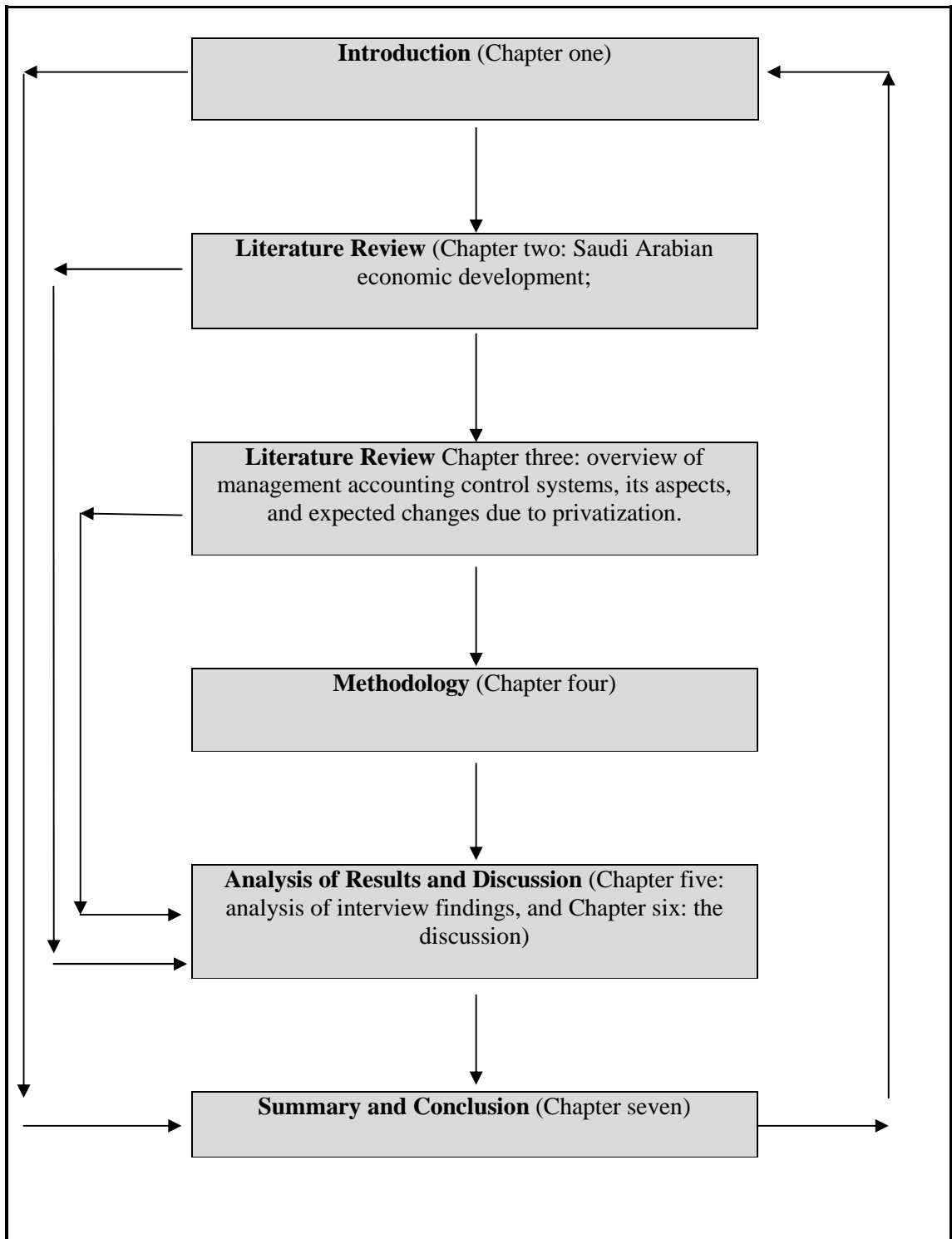
Chapter Four presents the research design and methodology chosen to address the aims and objectives of the study. It explains the reasons for selecting certain data collection methods and describes the design of the data collection instruments. It also describes the research hypotheses and questions that are investigated in the study.

Chapter Five presents and analyses the results of the qualitative aspects of the case study. It presents the changes that occur on MACS on the organisations under study.

Chapter Six provide a discussion of the changes that occur on MACS based on the analyses on chapter five and reveal the other factors that have implications on MACS beside privatisation.

Finally, **Chapter Seven** offers a summary and conclusion of the study. In addition, its major findings and limitations are discussed and suggestions are made concerning possible further research.

Figure 1.1 The Structure of the Study



Chapter 2. An Overview of Saudi Arabia and Its Economy

Introduction

The Kingdom of Saudi Arabia is not only the homeland of the Arab peoples but also the birthplace of Islam, the world's second-largest religion. The Kingdom of Saudi Arabia was founded in 1932 by Abd Al Aziz bin Abd Al Rahman Al Saud. The central institution of the Saudi Arabian government is the monarchy and Islamic law (Sharia) is the primary source of legitimacy. The Sharia has the same status as the constitution and the power of the Monarch is not unlimited, as it is constrained by the Sharia (McCurry, 1994). The Kingdom of Saudi Arabia remains a leading producer of oil and natural gas and holds approximately 25 percent of the world's proven oil reserves (Ministry of Economy and Planning, 2006).

The Saudi government is committed to pursuing economic reforms and diversification and promoting foreign investment in the country in the context of Saudi Arabia's accession to the WTO in December 2005. A rapidly growing population, aquifer reduction and an economy largely dependent on petroleum output and prices are all ongoing government concerns.

This chapter discusses the geography, demography and governance of Saudi Arabia and reviews its business environment by looking at the major economic developments affecting it. In the context of this project it specifically examines the reasons behind the recent privatisation programme and its implementation.

The chapter is divided into seven main sections, viz.,

- (1) Brief description of the location and population of Saudi Arabia;
- (2) Governmental system in the Kingdom and the process of decision-making in the country
- (3) Government policy towards business;
- (4) Major developments in the Saudi economy;
- (5) Development planning in Saudi Arabia';
- (6) Review of the Saudi public and private sectors;

- (7) Reasons for privatisation in Saudi Arabia and privatisation experiences of other countries.

2.1 Geography and Population

Saudi Arabia has a total area of 2.2 million square kilometres—about 10 times the size of the United Kingdom and a third the size of the continental United States (Saudi Ministry of Information 1997). The Kingdom covers roughly 80 percent of the Arabian Peninsula and is bordered by Iraq and Jordan to the North, Kuwait to the Northeast, the Arabian Gulf, Bahrain, Qatar and the United Arab Emirates to the East, the Sultanate of Oman and the Yemen Republic to the South and by the Red Sea to the West (Figure 2.1 Map of the Kingdom of Saudi Arabia).

Figure 2.1 Map of the Kingdom of Saudi Arabia



Source from Infoplease, (2005)

According to the latest estimates of the Central Department of Statistics, the total population was 24 million in 2006, comprising 17.3 million Saudis (73% of the total population) and 6.7 million non-Saudis. Saudi Arabia is one of the fastest growing nations in the world in terms of population growth, which is expected in the next few years to remain exceptionally high, at 3.2 percent per year, in comparison with the global growth rate of 1.5 percent (SAMA, 2006).

2.2 Government Systems

Saudi Arabia is an Arab and Muslim state, whose constitution is based on the Qur'an (the Book of Allah) and the Sunnah (Words and Practices of the Prophet Mohammed: peace be upon him). It is a monarchy, with a King whose official titles include President of the Council of Ministers and Custodian of the Two Holy Mosques and who occupies multiple positions as Head of State, Prime Minister and Supreme Commander of the Armed Forces, formulating and executing national policies. The Deputy Prime Minister, who is also the Crown Prince and the Minister of Defence and Inspector General, directly assists the King. Other ministers, who are well-known people of intellect and wide experience, appointed to the Council of Ministers, provide policy and legislative support to the King. The King also receives advisory support from the Consultative Council, the majority of whose members have received their higher education or earned postgraduate degrees from among the best universities in the world.

It should be pointed out that the political development of Saudi Arabia differs from that of most developing countries. Saudi Arabia has no history of exploitation and subjection by any Western colonial power. Al-amri (1982: 54) states:

Most of the developing nations, in their formative stages, were heavily influenced by one or the other of the European nations. Accordingly they patterned their independent system of government after those nations... Saudi Arabia, on the other hand, was never a colony. Its relations with other nations were always on a more remote, more equal basis. And when the political system of Saudi Arabia was being formed, it relied on the values of the nation, predominantly those of Islam, rather than on a foreign model.

In addition to being the most influential Arab country and leader of the Islamic world, the Kingdom has maintained a respected and influential position in the international community. Saudi Arabia is a founder member of the Congress of the Islamic World, the Arab League, and the United Nations, the Gulf Cooperation Council (GCC), the International Monetary Fund and the G20, and many other international organisations (SAMA, 2008).

2.2.1 The Council of Ministers

In the 1930s, the central administration was established for the first time in Saudi Arabia as a result of two independent developments. The first was the discovery in 1938 of oil, which gave the Kingdom a source of income through which all its needs could be met. This required a centralised government to manage its affairs. The second development was the increasing complexity of government².

Prior to the 1992 reforms, the Council of Ministers exercised three main functions of government: legislative, executive, and administrative. However, due to the establishment of the state Consultative Council in 1992, a new constitution for the Council of Ministers was issued in August 1993, which limited the Council of Ministers' responsibilities to mainly exercising executive authority, which it gets directly from the King who acts as Chairman of the Council and Prime Minister.

The council's executive jurisdiction includes the following functions:

1. Monitoring the implementation of statutes, rules, and decrees;
2. The creation and organization of public services;
3. Following up implementation of the overall development plan;
4. Establishing committees that will investigate the progress of the work of Ministries and other Governmental bodies or a specific issue³.

Although the establishment of the Consultative Council as part of the 1992 reforms reduced the Council of Ministers' monopoly over the creation of legislation, the Council

² Three ministries were established in 1950: Foreign Affairs, Finance and Defence. Other ministries, including Interior, Communications, Education, Agriculture, Commerce and Health were established in 1954. The Directorate General of Petroleum and Minerals with other agencies and departments followed in 1958.

³ Art.24 of the Basic Law of Council of Ministers.

of Ministers has the right to look into the decrees of the Consultative Council (Art.19, and see section 2.3.2) and may disagree with them.

The King, as President of the Council of Ministers, carries veto power over its decisions. In addition, the first and second Deputies report to the President of the Council, while Ministers are required to report to the Council and its President. Decisions are voted on by the majority of members present, but are not binding until approved by His Majesty. One of its main responsibilities is to study the state budget before its issuance in accordance with a Royal Decree and vote on it chapter by chapter⁴.

2.2.2 Consultative Council

In order for a Government to be legitimate in Islam, it must be based on Islamic Principles. Consultation is considered an Islamic Principle; therefore, Government must encourage consultation and enforce the rule of consultation at every level of Governmental operations. The Saudi government is obliged to consult the citizenry on public affairs and abide by agreements made in consultation. In March 1992, the King announced thirty articles governing the Consultative Council (CC) and it was apparent in his speech that this newly established Council was an extension of the existing system. The Council started with 60 members (Art.3), was later extended to 91members, including the Speaker of the Council, and now consists of 150 members. In August 1993, the King appointed members of the Council and the Speaker: members are selected and appointed from different sectors based on their experience, knowledge, and specialization to reflect all professional groups in the country and to reach a balance that mirrors Saudi society as a whole.

The CC discusses what is sent to it by the King and makes recommendations. It has the ability to initiate laws if ten of its members suggest an idea to the King, which may be pursued further on this request (Consultative Council Report, 2006).

According to Article 15 of the Basic Law of Government (BLG), the Consultative Council gives its opinion on the general policies of State presented before it by the President of the Council of Ministers (the King). In particular, the Council may:

⁴ Art.26. The Basic Law of Council of Ministers.

- a) Discuss the general plan of economic and social development and voice its opinion on it;
- b) Study laws, regulations, concessions and international treaties and agreements and offer suggestions on them;
- c) Interpret laws;
- d) Discuss annual reports submitted by Ministers and other Government agencies and offer suggestions on them.

In 2003, the King issued a decree giving the Consultative Council the authority similar to the Council of Ministers to propose new laws without first seeking his permission. The move was prompted partly by rare protests in favour of Government reform (Consultative Council Report, 2006).

2.3 Government Policy on Business

Until the emergence of the oil industry, Saudi society was basically engaged in primitive agriculture, fishing and the *Hajj* (pilgrimage) trade. Most of businesses at that time were family owned. The first time foreign companies started investing in Saudi Arabia was as a result of the discovery of oil. These companies made significant contributions to a successful Saudi economy, although their business aims and objectives constrained the time and money that they were able to dedicate to the planning of local business development, the major exception being Saudi Aramco, which gave much more help to the local businesses than any other Western company (Wright, 1996).

The Seventh Plan⁵ period (2000-2004) saw a number of initiatives aimed at creating a conducive business environment and attracting private investment, particularly foreign direct investment. The most important of these initiatives are:

⁵ Over the last three decades, Saudi Arabia has witnessed gradual rising accumulation of surpluses from oil sales with sharp price and production increases, which have continued for quite a time. To utilise these surpluses for the development of human and natural resources, the Saudi government started five-year development planning in 1970 as a framework for the process of overall development. Development plans have been formulated under the guidance of the Ministry of Planning and National Economy and with support from other public agencies. These plans have played a crucial role in developing the country. So far, Saudi Arabia has accomplished seven five-year development plans and the eighth development plan is being implemented during the current period (2005-2009). The five-year plans are prepared according to General Objectives and Strategic Bases and are approved by the Consultative Council and the Council of Ministers.

- (1) SAGIA (Saudi Arabia General Investment Agency), which was created to be responsible for national and foreign investment affairs. It issues investment licences, facilitates procedures for foreign investors via one-stop-shops (comprehensive service centres) in all major cities, proposes policies and measures for the improvement of the investment climate, promotes investment opportunities and provides relevant information.
- (2) The new Foreign Investment Law issued in April 2000 ensures equal treatment for national and foreign investors by allowing foreign companies to obtain full ownership of projects and pertinent assets, as well as offering equal investment incentives including soft loans provided by the Saudi Industrial Development Fund (SIDF). Foreign companies are also allowed to carry over their losses for an unlimited number of years for purposes of tax, which has also been reduced to 20 percent of the profits.
- (3) The Capital Market Law, issued in 2003. In view of the significance of the capital market in promoting economic growth, and with stock market and other mechanisms being considered as instruments for channelling national savings, stimulating national investment and attracting foreign investment, the Capital Market Law aims at restructuring and regulating the Saudi capital market by developing the institutional structure of the market and completing the related infrastructure in line with international best practice to ensure transparency and safety of dealings. The most significant features of this law are:
 1. The establishment of three new institutions with administrative and financial autonomy intended to replace the provisional measures that were adopted by the market. These are the Securities Exchange Commission (which is considered a supervisory and regulatory body), the Securities and Exchange Market and the Securities Depository Centre, as custodian of securities and related settlements.
 2. The separation of the supervisory and regulatory role from the executive role of the capital market. The former is fulfilled by the Securities and Exchange Commission and the latter by the Securities Market and the Securities Depository Centre under private sector management.
- (4) Establishment of the Human Resources Development Fund in 2000. The aim is to support the process of training and educating the national workforce.

- (5) The launch by SIDF, in collaboration with the commercial banks, of a programme of support for small and medium enterprises (SMEs), under which SIDF guarantees up to 75 percent of the loans provided by the commercial banks to SMEs (Ministry of Economy and Planning, 2006).

2.4 Review of Major Economic Developments

This section will provide a detailed description of the economic environment in Saudi Arabia. An examination of the Saudi economic environment, focussing particularly on the importance and contribution of oil to the whole economy of the Kingdom will be presented briefly. Other socioeconomic indicators such as employment, interest rates and inflation rates are also discussed.

2.4.1 *Economic Environment in Saudi Arabia*

According to the Energy Information Administration (2007), in the context of becoming successfully integrated into the global economy, Saudi Arabia, the largest economy in the Middle East, has emphasized the importance of regional unity among Gulf States economically, politically and militarily. Reflecting positive conditions in the world oil market, Saudi Arabia enjoys continued optimism and improvement in the domestic investment environment in all sectors of the economy. This is due to high oil prices, increasing oil production and export earnings, coupled with structural reforms, economic diversification and stable macroeconomic policymaking (Saudi American Bank, 2008).

As shown in Table 2.1 Selected Economic Indicators, the Saudi economy continued to record high growth in all sectors during fiscal year 2006, which remains heavily dependent on oil and petroleum-related industries, including petrochemicals and petroleum refining.

Table 2.1 Selected Economic Indicators

	2002	2003	2004	2005	2006
Estimated population (million)	21.5	22.0	22.7	23.1	23.7
GDP at constant price (billion riyals)	707.1	804.6	938.8	1,182.5	1,307.5

GDP at constant prices of 1999 (billion riyals)	637.2	686.0	722.2	766.0	798.9
Non-oil GDP deflator	99.0	102.1	105.9	110.3	110.2
Inflation rate (consumer prices)	0.2	0.6	0.4	0.7	2.2
Aggregate money supply M3 (billion riyals)	390.4	417.5	496.1	553.7	660.6
Average price of Arabian light oil (US\$)*	24.32	27.69	34.53	50.15	61.05
Riyal's real effective exchange rate (2000=100)	99.0	90.5	84.4	82.3	81.8
Ratio of currency in circulation to total money supply	13.4	13.3	12.1	11.6	10.5
Ratio of total deposits to total money supply	86.6	86.7	87.9	88.4	89.5
Net foreign assets of domestic bank (billion riyals)	52.5	41.0	47.1	26.4	70.6
Interest rates on domestic currency deposits (3 months)	2.23	1.63	1.73	3.75	5.02
Bank capital adequacy ratio (Basel standard)	21.3	19.4	17.8	17.8	21.9
Actual government revenue (billion riyals)	213.0	293.0	392.3	564.3	673.7
Actual government expenditure (billion riyals)	233.5	257.0	285.2	346.5	393.3
Ratio of budget deficit /surplus to GDP	-2.9	4.5	11.4	18.8	22.2**
Exports of goods (billion riyals)	271.7	349.7	472.5	677.1	786.6
Import of goods CIF (billion riyals)	121.0	138.4	167.8	223.0	248.4
Ratio of current account surplus to GDP	6.3	13.1	20.7	28.5	27.4
Current account (billion riyals)	44.5	105.2	194.7	337.0	357.7
Share price index (1985=1000)	2,518.1	4,437.6	8,206.2	16,712.6	7,993.3

Source: OPEC, 2007

The major indicators show that the oil price had a positive impact on economic conditions in 2006. According to OPEC sources, the average price of Arabian light oil rose by 42.2 percent to \$50.15 a barrel compared to \$61.05 a barrel in 2006, which increased the actual revenue of Saudi Arabia (SAMA, 2007).

The increase in oil prices had a positive impact on all Saudi economic sectors. As shown in Table 2.3, GDP (at current prices) rose by 10.6 percent to SR 1.3 trillion in 2006, while the real growth was 4.3 percent, amounting to SR 798.9 billion.

Therefore, the budget of Saudi Arabia was in substantial surplus in 2006, amounting to SR 289.7 billion or 22.2 percent of GDP. The balance of payments current account recorded a surplus for the eighth consecutive year, increasing by 6.0 percent over the preceding year. This growth in the state budget can be seen as resulting from the increased oil price in 2007 (ibid).

According to the Saudi Arabia Monetary Agency (SAMA 2007), actual oil revenue increased to SR 604,407 million in 2006 (see Table 2.2), when oil revenues stood at

89.7% of total revenues, compared to 89.4% in 2005, while non-oil revenue was about 10.3%, against 10.6% in 2005.

Table 2.2 Actual Oil and non-oil Revenues (million riyal)

Year	Oil Revenue		Non-oil Revenue		Total Revenue
	SR	%	SR	%	
2002	166,100	78.0	46,900	22.0	213,000
2003	231,000	78.8	62,000	21.2	293,000
2004	330,000	84.1	62,291	15.9	392,291
2005	504,540	89.4	59,795	10.6	564,335
2006	604,470	89.7	69,212	10.3	673,682

Source: Ministry of Finance Report, 2007

Table 2.3 Distribution of the State Budget 2006 and 2007 (by major sectors)

	2006		2007	
	Million SR	% of total	Million SR	% of total
Human resources development	87,164	26.0	96,483	25.4
Transport and communication	9,804	2.9	11,329	3.0
Economic resources development	12,454	3.7	13,902	3.6
Health services and social development	26,798	8.0	31,902	3.6
Infrastructure development	4,555	1.4	5,188	1.3
Municipal services	11,588	3.5	13,576	3.6
Defence and national security	110,779	33.1	132,922	35.0
Public administration, utilities & general items	62,814	18.7	61,756	16.2
Government specialized credit institutions	575	0.2	1,026	0.3
Subsidies	8,469	2.5	12,808	3.4
Total	335,000	100	380,000	100

Source: Ministry of Finance (2008)

The allocation of finance for each of the major sectors increased at varying rates in 2007 compared to 2006 as it shown from Table 2.3.

2.4.2 Major Socioeconomic Objectives

In addition to the enhancement of economic growth, employment, exports and the diversification of economic activities, the objectives of the Saudi Eighth Development Plan (2005-2009) includes greater attention to the provision of care to poor social groups and basic health and education services, and balanced distribution of the benefits of development among all regions of the Kingdom. In response to regional and international economic developments, the Plan adopts the objectives of strengthening economic integration among GCC states, enhancing Arab economic cooperation and

accelerating the process of merging into the global economy (Ministry of Economy and Planning, 2006).

Table 2.4 shows the main macroeconomic indicators and targets during the Eighth Development Plan as compared with the recorded achievements of the Seventh Development Plan. The macroeconomic projections were developed after taking into consideration the internal and external variables that had a direct or indirect impact on the Eighth Development Plan.

Table 2.4 Macroeconomic Indicators of the Eight-Development Plan Compared with the Seventh Development Plan (%)

Indicators	7 th Development Plan (actual) 2000-2004	8 th Development Plan (targeted) 2005-2009
A) <u>Growth rates (annual average)</u>		
* Real GDP (1)	3.44	4.6
- Oil sector (2)	2.59	2.73
- Non-oil sector	3.93	5.21
e) Private sector	4.28	5.68
f) Government sector	2.95	3.82
* Gross fixed capital formation	4.4	10.72
- Oil sector	16.92	20.12
- Non-oil private sector	2.32	10.45
- Government sector	10.33	3.18
* Goods and services exports	3.72	3.03
* Goods and services imports	7.32	4.57
B) <u>As share of GDP at current prices (3)</u>		
* Gross savings	39.8	40.8
* State budget balance	9.4	1.4
* Current account balance	21.8	18.02
C) <u>Unemployment and inflation rates</u>		
* Inflation rate (4)	- 0.60	0.60
* Unemployment rate (5)	7.04	2.84
- Males	5.63	2.42
- Females	15.86	4.35

Source: Macroeconomic Projections, Ministry of Economy and Planning (2006).

Notes:

- At constant 1419/20 (1999) prices.
- Crude oil, natural gas and petroleum refining products.
- By the end of the Plan.
- Average annual growth of consumer prices.
- Exclusive to Saudi labour force as a percentage of labour force by the end of the Seventh and Eighth Plans.

2.4.2.1 Cost of Living

As Table 2.1 Selected Economic Indicators shows, the general cost of cost of living index (1999=100) registered an increase of 2.2 percent in 2006. The wholesale price index recorded an increase of 1.1 percent in the same year, while the non-oil GDP deflator declined by 0.1 percent (SAMA, 2007).

The average inflation rate as measured by annual changes in the cost of living indices during the twelve months to March 2008 rose by 5.4% (Saudi American Bank, 2008). During the period April 2007-March 2008, the rate of inflation for goods and services surpassed the rates of the previous five years (2002-2006).

The group of renovation, rent, fuel and water rose by 10.7 %, food and beverages by 8.0%, goods and other services by 6.8 %, medical care by 5.6 %, education and entertainment by 0.7 % and transport and telecommunications by 0.3 % (SAMA, 2007).

2.4.2.2 Interest Rates

The body responsible for fixing the interest rate in the Kingdom is the Saudi Arabia Monetary Agency (SAMA), which, like any other central bank, employs interest rates as one of the tools to control the money supply in the economy. In comparison to a rise of 1.64 percentage points to 5.13 % in the Eurodollar rate in 2006, the average interest rate for three month riyal deposits rose by 1.26 percentage points to 5.02 percent. The smaller increase in the riyal deposit rate than in the Eurodollar deposit rate resulted in the differential between the two average rates turning in favour of the dollar rate to the extent of 11 basis points. The trend from 2002 to 2006 is shown in Table 2.5.

Table 2.5 Interest Rates on Riyal and Euro \$ Deposits
(Average rate on 3-month deposits)

Year	Saudi Riyal Deposit	Euro \$ Deposit	Differential between Riyal and Euro \$ rate
2002	2.23	1.71	0.52
2003	1.63	1.11	0.52
2004	1.73	1.53	0.20
2005	3.76	3.49	0.27
2006	5.02	2.13	-0.11

Source: SAMA, 2007

2.4.2.3 Exchange Rate

The riyal is pegged to the dollar and this remains a central principle of policy⁶. SAMA maintained the riyal exchange rate with the US dollar at 3.75 per dollar during 2006. This rate was made official on January 1, 2003. The declining trend in both the nominal and real effective exchange rates of the riyal continued during 2006. The index of nominal effective exchange rate (NEER)⁷ (year 2000=100) declined steadily from 103.5 in 2002 to 90.3 in 2006. Likewise, the index of real effective exchange rate (REER)⁸ fell from 99.0 in 2002 to 81.8 in 2006, as shown in Table 2.6 (IME, 2007).

Table 2.6 Indices of Nominal and Real Effective Exchange Rates (2000=100)

	2002	2003	2004	2005	2006
NEER	103.5	95.9	91.2	90.6	90.3
REER	99.0	90.5	84.4	82.3	81.8

Source: IME's International Financial Statistics, 2007.

The riyal briefly rose to a 20-year high after the US Federal Reserve cut its interest rates in September 2007 and SAMA decided not to follow this cut, partly due to concerns about the inflationary effects of low interest rates and a lower value for the riyal, which returned to its peg against the US dollar in early December of 2007 (SAMA, 2007).

2.4.2.4 Unemployment

During the mid to late 1980s, in the wake of high oil prices, the oil-producing countries of the Middle East experienced rapid development, which contributed to economic growth, infrastructure development and the expansion of public goods provision, and finally created excess labour demand that could not be met by domestic resources. Foreign workers were therefore imported to fill the gaps (Ruppert, 1998).

The economies of GCC countries became highly centralized and dominated by the public sector, partially due to the presence of large publicly owned oil-related industries. In order to implement national development plans, the demand for qualified workers increased in both public and private sectors during the period of economic

⁶ All GCC member countries have the US dollar as official anchor for their currencies.

⁷ NEER represents the trade-weighted average of the Riyal's bilateral exchange rates with currencies of selected countries and the Euro area.

⁸ REER represents adjusted for relative movements in price level indicators of Saudi Arabia, selected countries and the Euro area.

boom. However, at the same time, the Ministry of Economy and Planning reported an annual growth in unemployment of 9.8 percent, bringing the unemployment rate to 12.02 percent of the total labour force in the Kingdom of Saudi Arabia, with unemployment among Saudi males at 9.07 percent and among females at 26.27 percent, as Table 2.7 shows.

Table 2.7 Unemployment Rate by Sex and Nationality

Year	Saudi			Non-Saudi			Total		
	Male		Female	Male		Female	Male		Female
	Total			Total			Total		
2000	6.54	17.64	8.15	1.13	0.96	1.11	3.78	9.34	4.57
2001	6.82	17.32	8.34	.98	0.60	0.93	3.87	9.14	4.46
2002	7.57	21.70	9.66	.82	0.62	0.79	4.21	11.51	5.27
2003	8.00	23.18	10.35	.80	0.79	0.79	4.36	12.51	5.56
2004	8.39	24.40	10.97	.77	0.93	0.80	4.49	13.36	5.82
2005	8.74	25.41	11.52	.75	1.06	0.80	4.60	14.07	6.05
2006	9.07	26.27	12.02	.74	1.17	0.80	4.71	14.69	6.25

Source: Ministry of Economy and planning, 2007

Apart from historical reasons, other factors can be identified as being influential in determining the supply of and demand for skilled workers in the Saudi labour market. These include a wide range of determinants such as social, economic, political, educational, and managerial and externally influenced factors. In general, it is agreed “education will be the main inspiration for altering and solving the major problems of human resources development in Saudi Arabia” (Al-Abdulwahed, 1981: 186).

The researcher believes that the increasing levels of unemployment among Saudi nationals can be attributed primarily to the poor quality of the Saudi educational system. There is also a tendency for young Saudis to be reluctant to take basic low-level positions and work their way up into positions of responsibility, as happens in Western countries. Instead, there is an expectation among them that they will be able to enter employment in high-level positions where they would supervise other employees who might be more experienced than them.

2.4.2.5 Public Debt.

Until 1988, Saudi Arabia financed its deficits through a drawdown of government deposits. The practice of financing the deficit through domestic borrowing started in 1988 when SR 42 billion (15% of GDP) worth of Government bonds were issued to commercial banks and autonomous Government organisations. The 1990s witnessed a

rapid build-up in the Saudi internal debt, from SR 237 billion in 1992, or 51% of GDP, to SR 650 billion in 2002 equal to 94% of 2002 GDP of SR 659 billion. The public debt has continued to rise, reaching nearly 100% of GDP (NCB, 2003). Most of the debt is owed to Governmental organizations, which reduces the risks associated with high levels of debts. Nevertheless, the Government must still make interest payments on all of its debt, and this debt servicing has become a significant part of the budget: SAMA-estimated SR 32 billion, or 15% of actual expenditures in 2002 at a 5% rate of interest (MECG, 2000, and SAMBA, 2002).

Allocation of the debt between organizations is as follows:

- a) Special Government Bond” holders hold SR 235.7 billion. Special bonds have been as hoc issuances ad bonds primarily to contractors to honor, late payment obligations of the government.
- b) Farmers and contractors hold SR 37 billion. The government has issued special bonds or “Farmers Certificates” to farmers over the past several years for late payment for government purchase of crops.
- c) SR 137.9 billion is held by the Retirement Pensions Agency. This pension fund manages the retirement pension programmes for government employees.
- d) SR 120 billion is held by the commercial banks in Saudi Arabia.
- e) The General Organization holds SR 68.4 billion for Social Insurance (GOSI). This organization manages the retirement pension of Saudis employed in private sector.
- f) Other establishments and funds hold SR 54.8 billion. (SAMBA, 2002).

Because of the increase of the Saudi budget and huge surplus on its budget due to the increase of the oil prices the Saudi government managed to reduce the amount of public debt from SR 660billion in 2002 to be SR237 billion in 2008 equal to %13.5 of GDP (Arab News, 2009).

2.5 Directions of Development Planning in Saudi Arabia⁹

According to the Ministry of Economy and Planning (2006b), planning for development is a process that is intended to bring about phased and orderly socio-economic transformation from an existing state to a new more desirable state. In the context of setting targets, the planning process and the plan document give due consideration to domestic and external conditions and challenges, which are prioritized in terms of their nature and the extent of their impact on the development process. The efficiency of the planning process depends on its capacity for continuous renewal and adaptation, in order to keep up with the changes and specific conditions of the individual phases of development. Thus, where planning is a means of meaningful socioeconomic development, the methodology of planning is the structure of that process. The Saudi government started five-year development planning in 1970 as a framework for the process of overall development to utilise the surpluses from oil sales arising from sharp price increases and its ability to increase oil production. These development plans, which have been formulated under the guidance of the Ministry of Economy and Planning with the support of other public agencies, have played a crucial role in the economic development of Saudi Arabia. To date, Saudi Arabia has accomplished seven five-year plans and the eighth development plan is being implemented during the current period (2005-2009).

2.5.1 Integrated Strategic Planning

The strategic dimension has been an essential element of the development planning process employed in the Kingdom of Saudi Arabia. In fact, any development plan has to be guided by a vision and a strategic perspective. Over the first five development plans, a set of ‘General Objectives and Strategic Principles’ served as the strategic dimension and provided the general framework for the objectives, policies and programmes of individual plans. Taking a step forward, over and above its general objectives and strategic principles, overseen by the Supreme Economic Council and approved by the Consultative Council and the Council of Ministers, the Seventh Development Plan adopted a long-term perspective vis-à-vis the national economy.

⁹ Most of the information and economic statistics in this section are based on the reports issued by the Ministry of Economy and Planning, Saudi Arabia.

2.5.1.1 The Plan's Indicative Role

Starting with the Fifth Development Plan (1990-1994), the process of planning for development adopted a methodology of indicative planning for the private sector, as a complementary approach to the directive planning methodology adopted vis-à-vis the public sector. However, certain aspects of the Eighth Plan methodology have been further developed to enhance the Plan's indicative role. This development comes in response to the growing role of the private sector over recent years and the expected further expansion of that role over the coming years, prompted by the progress of privatisation and the process of stimulation of private investments. Among the aspects that have been developed are:

- Increased emphasis on effective policies and improved transparency in their implementation.
- Ensuring that policies are accompanied by relevant implementation mechanisms, and setting of specific quantitative and time-bound targets for these mechanisms. This will allow for effective monitoring and evaluation of performance and efficiency of policies by responsible agencies.
- Listing of strategic projects into a separate chapter of the Plan document. The list provides data on project volumes and investment requirements and, as such, provides an indicator to the business sector of the size and nature of the Plan's investment priorities. (Ministry of Economy and Planning, 2006b).

2.5.1.2 The Plan's Directive Role

The emphasis on policies and objectives, particularly those relating to activities and outputs, aims at strengthening the role of the implementing agencies at all levels of government, in achieving the Plan's objectives through the selection of the best possible programmes, projects and other activities. The process of setting policy objectives coupled with relevant implementation mechanisms allows the agencies responsible for follow-up and monitoring to improve their performance in carrying out these tasks.

On the other hand, the emphasis on activities and their outputs, the establishment of indicators for measurement of the output and the setting of targets for these indicators

will contribute to the improved efficiency of the agencies involved, because performance criteria are tied directly to activity objectives. For example, the objective of health activity is to improve health standards. While health sector inputs, including hospitals, physicians and health centres are essential to improve health standards, they are not sufficient by themselves. Thus, activity output indicators provide a direct reflection of service standards and other activity objectives.

Table 2.8 makes it evident how closely Government expenditure follows the fortunes of the Kingdom's oil revenue, with the Seventh plan (2000-2004) not reaching the peak of the 'boom years' of the Third plan (1980-1984). The researcher expects in this current development plan (2005-2009) that government expenditure will be the more than in any previous development plan, due to the huge oil price increase during 2008.

Table 2.8 Expenditure (billion riyal) by Saudi Development Plan (1970-2004)

Expenditure	First plan		Second Plan		Third Plan		Fourth Plan		Fifth Plan		Sixth Plan		Seventh Plan	
	SR	%	SR	%	SR	%	SR	%	SR	%	SR	%	SR	%
Economic resources development	9.5	27.7	97.3	28.0	192.2	30.0	71.2	20.4	34.0	10.0	48.2	11.5	41.7	8.5
Human resources development	7.0	20.6	51.0	14.7	115.0	18.5	115.1	33.0	164.6	48.0	216.6	51.5	276.9	56.7
Social and health development	3.5	10.3	27.6	8.0	61.2	9.9	61.9	17.7	68.0	20.1	87.5	20.8	95.8	19.6
Infrastructure development	14.1	41.4	171.3	49.3	256.8	40.8	100.7	28.9	74.2	21.9	68.1	16.2	73.8	15.2
Total	34.1	100	347.2	100	653.2	100	348.9	100	340.9	100	420.4	100	488.2	100

Source: Ministry of Economy and Planning, 2006

The growth targets of the Eighth Development Plan (2005-2009) were set up in a manner that reflects the strategic directions of the Kingdom's long-term economic development. These include improvement of the standard of living of Saudi citizens, development of human resources, diversification of the economic base and a rise in the productivity level of the Saudi economy. The most important objectives and policies of the Eighth Development Plan (Ministry of Economy and Planning, 2006) are summarised as follows:

- Increasing economic growth rates.

- Increasing the private sector's contribution to economic growth and national income.
- Diversifying the economic base.
- Improving the balance of payments position in favour of the Kingdom.
- Realizing a high degree of economic balance and price stability.
- Realizing balanced development in all regions of the Kingdom.

2.5.2 Implications of the Saudi's Accession to the WTO

Saudi Arabia has concluded bilateral market access negotiations with all interested WTO Members. The WTO General Council formally concluded negotiations with Saudi Arabia on 11 November 2005 on the terms of the country's accession and Saudi Arabia became a full WTO Member on 11 December 2005.

There were many advantages of accession to the WTO, the most important of which was encouraging private sector investors to establish export-oriented industries, as a result improving the competitiveness of national products in local and global markets. It also enabled the Kingdom to make use of the trade laws and rules in protecting its foreign trade sector against unfair practices, such as dumping, imposing arbitrary duties, commercial counterfeiting of products and other practices which might have adversely affected the stability and development of trade.

The Kingdom was also able to avoid the unilateral measures and differential trade policies practiced by some countries since its exports were no longer subject to dumping or counter-tariffs unless within the provisions of WTO legislation. Similarly, the Kingdom had the right, according to WTO laws, to resort to various measures to protect its trade interests.

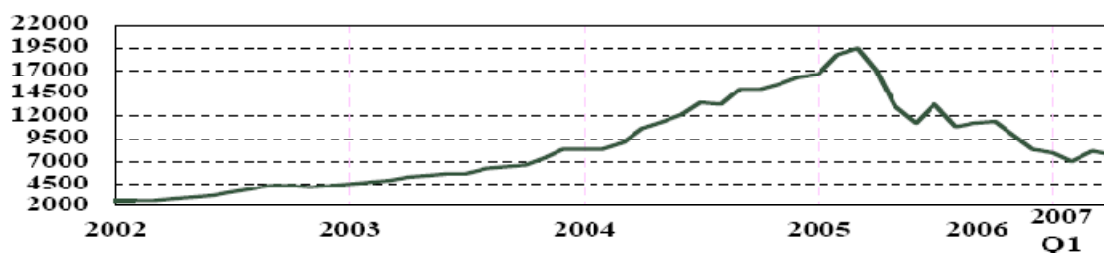
The Kingdom's petrochemical exports were the major beneficiary of the positive impacts stated above due to the reduction of custom duties in the WTO member countries as well as the removal of constraints, which were hindering penetration into the markets of these countries. These factors improved the competitiveness of petrochemicals exports.

The most serious negative implication of the Kingdom's accession to WTO lay in the increased foreign competition in Saudi domestic markets, particularly in banking, telecommunications and consulting services, as well as consumer products.

2.5.3 Activation of the Saudi Stock Market

The endorsement of the Capital Market Law by the Council of Ministers in 2003 represented a major step towards restructuring the Saudi stock market. It was able to operate more efficiently and expand and create effective instruments for investment of savings, while promoting the requirements of transparency, equity and protection of dealers. The Saudi stock market is the largest and most active in the Gulf region in terms of market capitalization, which reached SR 891 billion in the first quarter of 2007 (Figure 2.2).

Figure 2.2 General Share Price Index (1985=1000)



Source: SAMA, 2007

In 2006, the number of shares traded rose by 11.6 percent to 68.5 billion, compared to 61.4 billion in 2005, due to the effect of the split in April 2006 of the nominal value of the shares of all listed companies into SR 10 per share instead of SR 50 per share. Therefore, the number of transactions increased by 106.2 percent to 96.1 million, compared to 46.6 million in the preceding year, with 86 companies trading on the Saudi share market at the end of 2006 having an average market capitalization of \$3,800.6 million per company (SAMA, 2007).

Comparative studies also indicate the possibility of making the stock market more developed and comprehensive. However, this will depend to a great extent on the effectiveness of the rules to be set by the Securities and Exchange Commission regarding the regulation of transactions and conditions for listing of companies in the

market, as well as the removal of the constraints, which impede the development of the market. In this context, the following mechanisms may contribute to the creation of an appropriate investment climate to facilitate the development of the Saudi stock market:

- 1) Putting more effort into implementation of the Capital Market Law with regard to restructuring and regulating investment in securities and providing more transparency and financial disclosure to companies which issue shares, to assure the safety of dealing in the traded securities.
- 2) Ensuring measures for the activation of the primary market for shares. The existence of an active primary market is a precondition for an active stock market, since it allows the listing of new shares, thereby enhancing the scope and activities of the market. It is noteworthy that the level of activity of the Saudi primary stock market remains weak. Only 13 companies have been added to the companies listed on the market over the last decade, contributing to an increase of market capitalization of only 3 percent. To address this weakness and to activate the primary market, it may be necessary to:
 - a. Accelerate the implementation of the privatization programme.
 - b. Encourage the transformation of family-owned companies into joint-stock companies, which could be listed on the stock market.
- 3) Establishing investment banks that will set up and manage investment funds and portfolios, as well as providing investment trust services including advice to investors, marketing of securities covering public subscriptions and delivering other services related to the activation of security markets.
- 4) Allowing foreigners to invest in shares of some companies listed in the Saudi stock market. This will contribute to channelling the savings of foreigners residing in the Kingdom towards productive activities in the Saudi domestic economy.
- 5) Evaluating the influence of banks' financing of investment in securities. It is noteworthy that bank finance of private sector investments in securities increased in 2004 by 49 percent as compared to 2003. This may be one of the reasons behind the sharp rise in the general stock price index during 2004.

2.6 Public and Private Sectors in Saudi Arabia

Public and private sectors play a crucial role on the Saudi Arabian economy. This section will describe the background and development of both sectors.

2.6.1 Public Sector in Saudi Arabia

The public sector in Saudi Arabia has grown in parallel with the development of the Kingdom itself. At the beginning of the 1970s, the start of economic development in the country, Saudi Arabia lacked infrastructure projects and its private sector was unable to provide the financial resources and administrative potentialities necessary to execute large-scale economic projects to meet the requirements of growth.

At the same time the intention was to redistribute the increasing income from oil in the form of services and public utilities to all community categories at low prices (AL-Shakawi, 2002).

Trivedi (2002) divided the growth of the public sector into three stages as follows:

a) Foundation of Public Administration (1902-1953):

The focus of this stage was on management of individuals without any attempt to create a centralized administrative structure. Governors ruled regions with other officials, judges and treasurers undertaking principal administrative duties;

b) Centralisation of Public Administration (1953-1969):

All Government bodies were brought together under the supervision of a single agency when the Council of Ministers was established as a central administration in the Kingdom. After World War II, there was a tremendous demand for oil, which increased Governmental revenue from SR 172 million in 1945 to SR 1,355 million in 1954, and led to an increase in the size and responsibilities of Government bodies. This in turn put great pressure on public agencies because they were unable to cope with the new practices due to lack of qualification. As a result an administrative gap started to emerge and became this became even more evident when the Government was faced with a serious financial crisis in 1956. This crisis was mainly due to excessive spending and weak financial control policies within Government departments and drew attention to the need to develop modern administrative and public management systems. A serious attempt was subsequently made to start a process of administrative reform to create a solid central administration within the country;

c) Foundation of the Development Administration (1970-Present):

The launch of the First Development Plan saw the introduction of the Development Administration. A number of public enterprises were created to accelerate the development process. This was preceded by the creation of centralized Government machinery and public agencies capable of planning and executing development projects.

2.6.2 Private Sector in Saudi Arabia

The nature and the scope of economic activity by the Saudi private sector and the development of its institutions have been closely linked to the Kingdom's overall development path since the adoption of the First Development Plan. Unlike the situation in some countries, the Saudi private sector's progress has never faced ideological constraints, as the Government has consistently shown, both by its stated policies in the Development Plan documents and by its actions.

Its commitment to principles are based first, on the Islamic Sharia and traditions that foster freedom for individuals to engage in economic activity of their own choice, and second, the philosophy of the market economy, with free access for all individuals and groups, as stated in Development Plans and guaranteed by the state.

During the Second and Third Development Plans, the increase in government expenditure, which was of historic proportions, began to shape the modern emerging private sector more forcefully. It successfully implemented a wide range of industrial, agricultural, healthcare, transport and operations and maintenance projects, establishing complementary links between the public and private sectors and avoiding any contradictions. (Alsughayer, 2001).

The tremendous expenditure, as a result of the booming economy and huge revenues from 1975 until early 1990s, led to private and public sector complacency about expenditure. Unfortunately, this attitude had negative consequences for the Saudi economy and society. It had created a growing private sector and a population dependent on state expenditure, with the result that both private sector and individuals had become interested in the state's policies and performance (Aldamer, 1995).

However, in the late 1990s encouraging signs of a more mature and autonomous private sector began to appear where reliance on Government expenditure had been reduced. At

the beginning of the Sixth Plan, several factors indicating the beginning of the private sector's growth were evident, providing grounds for optimism that the private sector would undertake an increasingly important role and become a major driving force for growth in the Saudi economy in the future (Alsughayer, 2001).

The Seventh Plan (2000-2005) was anticipated to continue reforms of privatisation and economic diversification of the economy and to add even greater emphasis on new additional sectors such as training and employment of Saudi population.

The early stages of the policy's adoption gave the private sector opportunities to engage in a wide range of economic activities and enabled it to make an effective contribution to the overall development of the Kingdom.

It was able to enhance its role in the national economy, improve its managerial, technical and financial capacity and therefore become more economically efficient in terms of both investment and production.

Thus the sector became capable of mobilizing capital for financing projects and using advanced management techniques and technologies in its operations. The Government further enhanced its developmental role by creating an investment climate leading to the privatisation of telecommunications, power generation, desalination and many other fields. By creating these investment opportunities the Government encouraged the sector's role in socioeconomic development. (Ministry of Economy and planning, 2008)

Despite the progress achieved by the private sector, it still faces challenges, which should be addressed during the coming period. Foremost among these are: continuing to improve the level of competitiveness of the sector to enable it to face the challenges of globalization; increasing its contribution to production and investment; providing sufficient job opportunities for the growing number of Saudi entrants into the labour market and increasing its investments in high value-added projects and activities which can be integrated with the basic industrial platforms, particularly the highly competitive export-oriented industries (Alsughayer, 2001).

2.7 Privatisation in Saudi Arabia

Privatization represents one of the strategic themes relating to the diversification and transformation of the Saudi economy. It also represents an important mechanism for increasing private sector participation in economic development. However, the oil and gas sector is not part of this programme and remains under state control. Following the announcement by the Supreme Economic Council of the privatization strategy and identification of the public facilities to be privatized, the next important stage was to be the preparation of an implementation programme for privatization.

This entailed:

- a) Preparation of a regulatory framework to support the privatization programme, particularly with respect to privatization of infrastructural facilities, including development of pricing controls for infrastructure services;
- b) Gradual implementation of the privatization programme, which entailed restructuring some Government organizations and transforming them into state-owned joint-stock companies. This was the first step towards full privatization;
- c) Assessing the value of assets of the facilities to be privatized using techniques appropriate to the individual facilities. This helped determine the total value of the facility and was used as a guide in the privatization process;
- d) Ensuring transparency in decision-making and implementation of measures related to privatization;
- e) Making use of specialized advisors in preparing detailed studies and managing the privatization implementation programme.

(Ministry of Economy and Planning, 2006b)

The implementation programme involved the preparation of a specific schedule to accelerate the process of privatizing the various economic sectors.

However, despite the initiatives, the more rapid development of Saudi exports required even more incentives to exporters that did not conflict with the commitments resulting from the Kingdom's accession to the WTO.

These incentives included:

- 1) Increasing technical assistance for exporters to reduce the average cost of production, improve the quality of exported products and enhance their competitiveness;
- 2) Intensifying efforts to accelerate implementation of export-related measures and provide trade information about overseas importers of Saudi products;
- 3) Expanding and activating the Saudi Non-Oil Exports Credit Programme adopted by the Saudi Fund for Development to protect the Saudi exporters against default of payment;
- 4) Studying the possibility of transforming the Saudi Exports Development Centre into a public organization with the aim of promoting and diversifying the Saudi exports base. This meant addressing the issues facing exporters and developing an appropriate strategy for export promotion. (Ministry of Economy and Planning, 2006b)

2.7.1 Privatisation Needs in Saudi Arabia. .

Unlike many developing countries and those of Central and Eastern Europe, Saudi Arabia and other Gulf countries did not need to transfer their economic system (which was considered a prerequisite for the privatisation process to take-off).

Furthermore, none of the Gulf countries were forced by the World Bank or the International Monetary Fund (IMF) to pursue privatisation as part of an economic reform programme, as was the case in many developing countries (Azzam, 1994).

However, the IMF did call for acceleration of economic reforms in the Kingdom in order to reduce the already large public debt, pressure on public finances, and encourage investment. It required that measures were put in place to cut expenditure and strengthen controls over spending to eliminate extra-budgetary outlays, and also recommended that the authorities made a clearer statement to the market of the timetable and steps that would be taken to execute an announced privatisation policy (Arab News, 26, 10, 2002).

In response, the Saudi Finance Minister stressed that the first step to overcome debts was getting rid of the annual deficit in the budget, which could be achieved by minimizing unnecessary expenditure and increasing revenues through seeking new sources of finance.

He stated that privatisation “will reduce pressure on the government. The private sector will provide services previously offered by the state. This will (positively) affect public spending”.

The minister further indicated that revenues generated from the sell-off would be used to pay for the entire domestic debt (Al-Jarallah, 2002).

AlKadiri (1999) pointed out that incomes from privatisation would make no material change in non-oil revenues for budgetary support, although they might reduce slightly the debt service portion of the budget.

He also contended that actual privatisation proceeds over the next 5 years would be modest compared to magnitude of the debt. For instance, the sale of 30 per cent of the Saudi Telecom Company would yield about SR 650 billion.

AlKadiri (1999) described privatisation as a short-term remedy: although it gave quick cash and cut spending commitments, it was not a long-term solution if there was not some form of revenue-generating process to go with it that would be sustainable over the long term.

However, other writers have pointed out that in many countries privatisation has led to dramatic improvements in customer service, particularly when competition is introduced or the private sector is made accountable for service standards (Speakman, 2002).

Speakman also referred to both empirical and anecdotal evidence indicating the need for Saudi state enterprises to use capital more efficiently, making reference to the costs of line installation in Saudi telecommunications as approximately double international norms. He indicated that in most infrastructure sectors there were cases of excess capital expenditure, whether over-specified container cranes, additional airport terminals, or empty hospitals.

The common perception of both informed observers and ordinary citizens in the Kingdom was that the public sector was not as efficient and effective as it could and should be (Trivedi, 2002).

The Saudi Arabian Secretary General of the Supreme Economic Council referred to privatisation as an important element of the Saudi reform programme and a strategic choice, pointing to the need to identify economic activities and Government services to be privatized, and to put in place a well-designed privatisation strategy.

In 2002 he stated:

Privatisation represents the government commitment to economic reform and conveys a positive picture to attract foreign investments. The nature of privatisation in Saudi Arabia slightly differs from that in some other countries. The creation of the country was based on private initiatives and Government intervention in economic activities happened during the oil boom years when the economy was growing at a fast pace but the private sector did not have the resources or technical ability to provide the goods and services that were needed. It simply could not create the industries, the housing projects, and the cities, airports, railways, roads, and hospitals, universities that were needed to bring Saudi Arabia into the modern world. However, the situation today is different since the very sophisticated private sector is endowed with resources to manage and finance many economic activities (Al-Tuwaijri, 2002).

Al-Homeadan (2001) argued that King Fahd's announcement of the privatisation policy on May 9th 1994 was due to the failure of some SOEs to maintain an acceptable level of service in terms of quantity and quality and as a result the Government had decided to allow the private sector to engage in all of the activities that such a sector was capable of performing.

In a survey study, Al-Homeadan (1996:286) found that department heads in Saudi SOEs preferred privatisation because of

Dissatisfaction with public bureaucracy, the difficulty of maintaining a large public sector, the need for the development of markets, for a more productive economy, to attract more international investment and ... the superiority of private sector managerial practices to create new economic opportunities, to reduce public expenditures, to reduce the budget deficit, to limit government intervention in the market place, to increase the private sector's capabilities, and to strengthen the local economy.

Speakman (2002) described the Government's role in Saudi Arabia as a change from an active participant in the economy to an economic policy setter and regulator. The private sector would be responsible for the delivery of many infrastructure services, which the public sector currently provided. It should play an increasingly important role in providing future social sector services, i.e. health, education and housing. Moreover, the natural resources sector would operate at full levels of private sector efficiency with full accountability to the people of Saudi Arabia.

2.7.2 Saudi Arabian privatisation programmes.

The Saudi government has a history of being very innovative in its approach to private sector participation. In May 1933 the Saudi government contracted out its oil operations to the Standard Oil Company via the formation of Aramco. The policy of acquiring technology and foreign expertise by using foreign companies has been pursued since 1973 through the encouragement of joint-ventures in a wide spectrum of sectors, including construction, manufacturing, banking, shipping and petrochemical processes.

By May 1995 there were, for example, 287 joint venture manufacturing projects in the Kingdom involving the public and private sector with foreign capital and expertise and 72% of the capital was in the chemicals and plastics sector (Al-Sarhan and Presley, 2001; and US-Saudi Arabia Business Council, 1995: 52).

The Saudi Government had already sold 30% of its shares in SABIC (the Saudi Arabian Basic Industries Corporation) to the public in the early 1980s. It also sold 30% of its shares in the Saudi Telecom Company in 2002 after five years of preparation and restructuring and also assigned the maintenance and operation of many of its agencies to the private sector. These included the Port Authority, the dry port under the supervision of the Railway Organization, as well as the operation and maintenance of some hospitals, and the maintenance and construction of roads.

Moreover, the Government used other methods of privatisation, including liberalization from legal monopolistic control and permitting the private sector to work and compete in a sector run by the Government, e.g. by permitting SNAS, DHL and other companies working in fast mail delivery and parcels to compete with the state-owned post enterprise.

The Government was also primarily concerned with setting up appropriate legal and regulatory structures for the privatisation process in the Saudi economy to ensure competition and avoid monopolistic tendencies.

The Council of Ministers Decree No. 60 (August 6, 1997) was the starting point to establish the eight objectives of privatisation in Saudi Arabia and the principles to be taken into account in order to achieve these objectives. The Council of Ministers Decree No. 257 of (February 5, 2001) stated that the Supreme Economic Council would be responsible for supervising the privatisation programme and monitoring its

implementation, in coordination with competent Government organizations, and for determining which activities were to be privatized.

Decree No. 6/22 issued by the Supreme Economic Council on 2 August 2001 provided for the reorganization of the Privatisation Committee within the Supreme Economic Council under the chairmanship of the Council's secretary-general. Members represented the Ministry of Finance, the Ministry of Industry and Electricity, the Ministry of Commerce, and the Ministry of Planning and National Economy; in addition two members were from the Advisory Board for Economic Affairs.

The Supreme Economic Council Decision No.1/23 dated 4th June 2002 approved a new privatisation strategy comprising eight basic objectives, each of which required the adoption of a number of policies.

The new privatisation strategy was prepared in accordance with the provisions of the Council of Ministers Decision No. 60 dated 6^t August 1990) which stated:

Expanding the private sector's participation in the national economy and enabling it to undertake its role in investment and financing should be in line with the national development plans, and positive for both the government and private sector.

The privatisation process constituted an important part of the Government's long-term strategy to enhance opportunities for the private sector and improve the efficiency and competitiveness of the national economy. This was achieved by encouraging participation by the private sector in economic development and employing the most appropriate ways of ensuring this would happen. This included transferring certain types of economic activity to the private sector and enabling it to accomplish its investments and financing role in accordance with the national development plan.

The privatisation strategy defines a number of administrative and implementation procedures related to privatisation, whereby the Economic Council will be responsible for supervising privatisation programmes and monitoring their implementation.

To carry out the required activities and functions necessary for the discharge by the Supreme Economic Council of its duties and responsibilities with respect to privatisation, the Privatisation Committee is involved in designing the privatisation strategy, determining and recommending the public enterprises, projects, and services to be privatized, determining the regulatory and implementation procedures for the

privatisation process, and monitoring and supervising the implementation of privatisation activities.

Although the strategy clarifies the steps that are to be taken, a specific timetable for the process has yet to be established.

The definition of privatisation as stated in the privatisation strategy is

“The process of transferring the ownership or management of public enterprises, projects and services to the private sector, relying on market mechanisms and competition, through a number of methods, including contracts for managing, operating, leasing, financing, or selling all or part of the governments’ assets to the private sector”.

2.7.3 Sectors that are Candidates for Privatisation

On 11th November 2002, the Saudi Council of Ministers approved a list of 20 vital economic state enterprises and sectors recommended by the Supreme Economic Council (SEC) for privatisation as shown in Table 2.9 below. The announcement of this list of sectors presented tremendous opportunities for the private sector and had major implications for the economy as a whole.

Table 2.9 The Full List of the 20 Enterprises and Sectors to be privatised

Activities to be Privatised	
1) Sale of State-Owned Shares in Limited Companies: Including the Saudi Electricity Company (SEC), Banks, the Saudi Arabian Basic Industries Corporation (SABIC), the Saudi Arabian Mining Company (Ma’aden), the Saudi Telecom Company (STC), and local oil refineries.	11) Municipality Services: Establishment of slaughter houses and their operations; establishment of general markets, selling centres and their operation; transportation and collection of municipality revenues; cleaning and waste removal
2) Sale of State-Owned Shares in the Capital of Joint Arab and Islamic Companies.	12) Social Services: Management and operation of social care institutions; employment recruitment of Saudis in the private sector.
3) Education Services: Establishment and maintenance of educational buildings; printing of textbooks; school transportation; student housing.	13) Roads: Management, operation, and maintenance of existing highways, and construction and operation of new highways.
4) Health Services: Establishment and operation of health facilities; patient transportation.	14) Agricultural Services: Quarantine and operation of diagnostic laboratories and veterinary clinics.
5) Desalination	15) Communications.

6) Air Transportation and its Services.	16) Airport Services.
7) Post Services	17) Railways
8) Mail Services	18) Sports Clubs.
9) Grain Silos and Flour Mills.	19) Government-Owned Hotels
10) Water and Sewage.	20) Services of the Industrial Cities.

Source: Arab News 13th November 2002.

2.7.4 Overview of Other Countries' Experience of Privatisation.

During the 1970s and 1980s a wave of privatisation programmes took place in many industrialised countries. The issue of privatisation in the West was aided by several factors. There was the election of Conservative Governments in many Western countries such as the UK and the United States. Conservatives believe strongly in allowing market forces to operate in order to promote economic growth. There were also structural obstacles to full employment and economic growth during the 1970s due to the oil crises. Subsidisation was seen as a serious obstacle to industrial restructuring and privatisation became the best candidate to bring about economic adjustment (Cook and Kirkpatrick, 1988).

This section will provide a brief overview of other countries experiences of privatisation. The section will provide the experiences of two Western 'developed countries', two Western 'developing' countries and one Arab 'developing' country. The aim is to find out if it is feasible to compare the Saudi experience with that of any other country.

2.7.4.1 Privatisation in United States.

The interest in privatisation in the United States goes back to the presidency of Carter; for example, the airline industry was privatised under the Carter administration. However, the greatest developments took place during the Reagan administration (Pack, 1987).

Municipalities, who had been contracting out various services, including garbage collection, police and fire brigade services since the 1960s, carried out the earliest form of privatisation; since then an increasing number of public agencies have contracted out various services to private enterprises. Between 1980 and 1982 the Pentagon offered 235 contracts to private contractors. However, privatisation in the sense of divestment

and as an ideological tendency came only as a result of close consideration of the Thatcher Government's model of privatisation (Donahue, 1989).

Privatisation efforts also came about as a result of the need to reduce the size of the Federal Government, including its growing budget deficit. Indeed, public expenditure increased excessively, from 9.9 percent of GNP in 1929 to 34.3 percent in 1985 (Pack, 1987).

In general, privatisation did not happen on as large a scale as in countries like Britain. This was due to the relatively small size of the public sector. While the average public sector in developed economies represented by 6.7 percent of the total workforce, the USA public sector employed only 1.5 percent.(Donahue, 1989).

2.7.4.2 Privatisation in the United Kingdom

Privatisation has been extensively used in the United Kingdom. Britain is often regarded as the principal model for privatisation in the Western world. However, the process of privatisation in its "legal arrangements to the terms of sale, was ad hoc". (Veljanovski, 1989: vii).

The Thatcher Government executed most of the actions, but the process still continued under later Governments. There is one obvious result of privatisation in Britain namely, the raising of revenue for the Government. Indeed, between 1977 and 1987, the it raised £25 billion. In the process, the proportion of GDP attributable to public sector industry fell from 9 percent to about 5 percent, while almost one million jobs were transferred from the public to the private sector (Hyman, 1989).

Privatisation, under the form of denationalization, started long ago in Britain. It was only in the second half of the 1970s that the current trend started. Before that, privatisation was a rather indecisive process as described by Burk (1988: 2):

Looking over the period from 1945 to 1988, a curious theme about the steel industry emerges. It was nationalized in 1949 by a Government, which did not wholly believe in its nationalization; it was then denationalized in 1953 by a Government, which did not wholly believe in its denationalization; it was then renationalized in 1967 by a Government, which did not wholly believe in its renationalization. Only time will tell if it was redenationalised in 1988 by a Government, which wholly believed in its redenationalisation.

The first privatisation in Britain took place in 1953 with the sale of the United Steel Companies. It was not easy for the Conservative Government to implement this denationalization as Burk's account of this first privatisation indicates (Burk, 1988). Starting from the second half of the 1970s, privatisation started slowly with the sale of shares of British Petroleum to the public in 1977 and 1979¹⁰ (Hyman, 1989).

According to Yarrow (1989: 56), this was a "revenue-raising exercise". This was soon followed by the sale of the aerospace industry (1981 and 1985), the shipbuilding industry (1985-1986), Amersham (1982), and Cable and Wireless (1981 and 1983).

Other major sales include British Gas (1986), British Airports Authority (BAA) (1987), British Airways (1987), and Rolls Royce (1987). British Steel and the Water Regional Authorities were privatized in 1988 and 1989 respectively (Hyman, 1989).

The privatisation of British Telecom in 1984 was the most popular privatisation programme because of its successful implementation in terms of raising revenue as well as public participation. The concern over BT's monopoly power led to the creation of a new regulatory watchdog, the Office of Telecommunications (OFTEL) (ibid).

Public opinion was very favourable because the programme encouraged individuals to participate in the ownership of these companies (Aharoni, 1988). However, many members of the public saw these purchases of shares as a means for quick and easy profit as they were sold to the public at a below market price. This view was endorsed when the value of BT shares immediately increased by 85% of their value.

While many previous privatizations were under-subscribed (such as Britoil with only 27 percent of shares bought by the public, and Cable and Wireless with 22 percent), the public applied for four times the available number of BT shares (Hyman, 1989). This created 2.3 million shareholders and at the same time raised £3.9 billion, the largest sale of a public enterprise at the time¹¹ (Hyman, 1989).

The strong commitment of the Government to privatisation was an important boost to the programme. However, the more important factor was the performance of the newly privatized enterprises themselves. Hyman gives a detailed account of the performance of privatized companies in terms of profit growth. For example, Amersham and Cable and Wireless increased their profit by a factor of almost five in the first seven years of their privatisation; British Aerospace's profits doubled in six years; and Rolls-Royce's

¹⁰ The Government sold 17 percent of its shares in BP in 1977, 5 percent in 1979, 7 percent in 1983 and 36.8 percent in 1987.

¹¹ This was later exceeded by the sale of British Gas that raised nearly £8 billion.

almost trebled. Jaguar turned its loss of £44 million in 1980 to profit of £107 million in 1986. Similar records are found in British Airways, BAA, British Gas, and British Telecom (ibid).

However, performance in other areas appears to be less encouraging. In a study carried out by the London Business School and United Research on executives from private and public enterprises (two thirds private), only 8 percent saw improved quality as the most important factor of success of their enterprise whilst only 27 percent saw product quality, and 18 percent saw customer service as a real concern of their organization (Waznah, 1996).

Deregulation has had mixed results. The Express Coach Services deregulation first led to intense competition, but National Express was eventually able to dominate the market by introducing its rapid service with toilet and refreshment facilities. Nevertheless, deregulation did have some positive effects such as increasing competition between coach and rail services, and in some fields of telecommunications (Yarrow, 1989).

Privatisation, and the clear determination of the Government to support it, helped the British economy to attract foreign investment. Foreign investors saw Britain as stable place to invest and this increased British foreign reserves. For example, when BT was privatized in 1984, 14 percent of the shares were bought by foreign investors (Hyman, 1989).

As described above, in many cases the British Government created regulatory bodies to protect consumers. The sale of British Telecom and British Gas, for instance, was accompanied by the creation of two regulatory agencies, the Office of Telecommunications and the Office of Gas Supply. Moreover, the Government kept a golden share in most of the privatized enterprises. This was basically meant to prevent any undesirable takeover or excessive foreign influence. Under the 'golden share', a privatized enterprise may have a combination of the following seven restrictions:

- 1 Prohibition on one person having an interest in 15 percent or more of the voting shares of the company;
- 2 Prohibition of total foreign ownership exceeding 15 percent;
- 3 Restriction on the issue of shares with voting rights different from those of ordinary shares;
- 4 Requirement that the Chief Executive be a British citizen;
- 5 Prohibition of the removal of Government-appointed Directors;

- 6 Restriction on the disposal of the whole or a material part of the assets of the group (material deemed to be 25 percent);
- 7 Restriction on the voluntary winding up or dissolution of the company.

This means that the Government did not give up indirect control over most of the privatized enterprises (ibid).

However Veljanovski (1989), while agreeing with the privatisation programmes, criticizes the lack of structural reform before privatisation. This, he maintains, has limited the scope of greater competition, which is the surest and most effective means of generating greater efficiency and consumer benefits. Indeed, many public sector industries and services kept their monopolistic privileges intact. There was, therefore, always the danger that regulation might not be enough to achieve the desired results which competition would easily achieve. As Littlechild states:

‘Regulation is essentially a means of preventing the worst excesses of monopoly; it is not a substitute for competition’ (Veljanovski, 1989: 26).

An example of this is the privatisation of British Gas in 1986 as one entity. This created a private monopoly in which the Office of Gas Supply (the regulatory agency) had little power of control (ibid). British Telecom was also under public criticism for its poor service (Yarrow, 1989).

2.7.4.3 Privatisation in Singapore

Interest in privatisation in Singapore started during the 1960s, but the actual divestment of public enterprises started in the 1970s (Low, 1988). In 1985 the Divestment Committee was formed and the Government has since sold off many enterprises including a food processing plant and an aviation company. The Government also reduced its interest in Singapore Airlines from 100 percent to 63 percent.

The goals of privatisation in Singapore are rather distinct in their nature. In Singapore privatisation took place not as a result of the need for funds to pay off public debt or as a result of political pressure, but came as a natural process. The Government clearly maintained that the proceeds from the sales were not needed. What happened is that privatisation of public enterprises occurred when Government thought that enterprises had grown sufficiently and could sustain its own activity without the help of the

Government. The money raised from the sale of such enterprises was then reinvested in other strategic sectors (ibid).

A number of major public enterprises have been privatized, such as the Rapid Transit Corporation and the Singapore Broadcasting Services. Other Government corporations are also currently under consideration, such as Telecoms, and the National University Hospital (Waznah, 1996).

Low (1988: 275) observes :

the Singapore public enterprises system is also a unique case among Third World countries insofar as its privatisation is the result of its success rather than failure. Along with buoyant growth, public enterprises have experienced tremendous success.

What is unique about privatisation in Singapore, therefore, is that it is used to raise funds to create new public enterprises. Public enterprises are not regarded as a problem, which the government seeks to get rid of, nor are they used to raise funds to pay for the public debt. In Singapore public enterprises are an integral part of the development programme. They take part in a continuous process of creation, development, sale, and creation.

2.7.4.4 Privatisation in Malaysia

There were many goals for privatisation in Malaysia. First the public sector represented a heavy financial and administrative burden on the Government, which aimed to reduce its involvement in economic activity. There were also economic objectives, such as promoting competition, improving efficiency and productivity. As a direct result of these, accelerated growth of the economy was hoped to be achieved. Most of these objectives were set up in the New Economic Policy (NEP) (Craig, 1988).

A large proportion of public assets were sold to the private sector. Among these were the Department of Telecommunications, the Malaysia Airline System, and Port Kelang Container Terminal. Other larger corporations, such as the Malaysian Airlines, Malaysian International Shipping Company, Port Klang, and the telecommunication system are being considered (Waznah, 1996).

Another form of privatisation is also used in Malaysia. Subcontracting has been used for a number of years. An example is the maintenance of the National Air Force, which was contracted out to the private sector.

2.7.4.5 Privatisation in Egypt

In 1961 Egypt undertook a massive nationalization programme, which reduced the number of large private companies from 240 to 60. Starting from 1974, however, Egypt has been following a more liberal economic policy (called *infitah*), allowing for the establishment of joint ventures and private companies (Ayubi, 1990).

Between 1970 and 1980, 560 new companies were created of which 113 were joint stock companies (Waterbury, 1985). This was aimed at increasing competition between private and public enterprises. This apparently had been unsuccessful as public enterprises were still suffering from inefficiency.

One of the most important problems with the internal functioning of Egyptian public enterprises was the constraint applied to the enterprises' management. Indeed, recruitment, and promotion were extremely restricted, while production decisions, pricing, and investment decision were mostly carried out by the government (Rivlin, 1985). Despite some proposal for divestment of parts of the public sector during the 1980s, it seems that contracting-out and joint ventures have been the most favoured tools (Ayubi, 1990).

Abd-al-Fadhil maintains that both the private and the public sectors are equally inefficient in Egypt and in many Arab countries. According to him, Egypt still suffers from a weak financial market, which cannot provide the necessary funds for privatisation (Abd-al-Fadhil, 1993). As Ayubi indicates, the public sector in Egypt is still dominant, and the state does not seem to be willing to undergo a large-scale privatisation programme. Only in the area of commerce and finance has the state let the private sector take the lead (Ayubi, 1990).

Between 1980 and 1987 several proposals for privatizing public enterprises were suggested. Unfortunately, none was carried out. The main reasons for this indecision was the "disinclination of Egyptian private capital to invest" as well as to the "resistance from public-sector personnel". (Ayubi, 1990: 97). A third reason is given by Ayubi, namely that "the state and bureaucracy were not prepared to relinquish the

control of functions and the special privileges provided to them by the public sector”. (1990: 97).

2.7.5 Overview of the Saudi Organisations Under Study

This section presents a brief profile of the organisations under study and describes the Government efforts that have taken place to prepare these enterprises for privatisation.

2.7.5.1 The Saudi Telecom Company (STC)

The Telecommunication sector of Saudi Arabia was part of the Communications Ministry established in 1952 to run all communication operations in Saudi Arabia such as post, telecommunication services, roads and railways. In 1975, the Ministry of Post, Telecom and Telegraph (PTT) was established to oversee the Saudi telecommunications sector (Al-Ansari, 1999).

In accordance with decree No. 135, the Council of Ministers decided in 1997 to transfer telecommunication services (telegraph and telephone) with all their various components, technical and administrative equipment to a Saudi Joint Stock Company, and decree No. 213 approved the establishment of a Saudi stock company named the Saudi Telecom Company (STC). Its initial capital was more than SR 12 billion, divided into 240 million shares of equal value of SR 50.

On 9 September 2002, the Council of Ministers approved an increase in STC’s capital from SR 12 to SR 15 billion. The company was established as result of the importance of the telecommunications sector and its role in accelerating development. (A privatisation team working with the World Bank had recommended privatisation of this sector and the Ministerial Committee on privatisation supported it). The STC was created as a business-oriented stock company providing all telecommunications services previously provided by PTT.

In December 2002, the Government of Saudi Arabia, represented by and acting through the Public Investment Fund (PIF or the Selling Shareholder), offered a minimum of 60,000,000 Shares, representing 20% of the Company, to individuals having Saudi

nationality, along with a maximum of 30,000,000 Shares, representing 10% of the Company, to the General Organisation for Social Insurance and the Public Pension Fund. The offer price was SR 170 per share, with a nominal value of SR 50. The Government continued to have effective control over the STC after the offering since the PIF retained 70% of the issued Shares. The company did not receive any of the proceeds from the sale of the Shares in the Offering.

In 1970, the total exchange line capacity in Saudi Arabia was only 76.6 thousand lines, but had increased to about 4.3 million by 2000, representing an average annual growth rate of 13.5 percent. The total number of telephones actually operating in the Kingdom also increased from 29,400 telephones in 1970 to around 2.9 million telephones in 2000, an average annual rate of 14.8 per cent (Ministry of Planning, 2001). Between 1998 to the end of 2001, the company's number of mobile subscribers increased 706%, reaching 2.5 million at the end of 2001, and the number of fixed line subscribers increased 74%, reaching 3.2 million at the end of 2001.

Similarly, the company developed an Internet backbone within its network, as Internet subscribers have increased significantly from 1998 to the present. Moreover, charges have been reduced to the lowest possible prices. The STC had almost 21,316 employees as of June 2002, 87% of whom were Saudi nationals. Its total assets were equal to SR 40.9 billion in 2002. The company's operating revenue for 2002 was SR 23.5 billion and net income was SR 3.5 billion. Annual revenue growth has averaged 17.1% over the last three years and average annual net income has achieved margins of 38.9% (excluding Government charges) (GIB, 2002). The STC deals with the Government as a related party where balances receivable from and payable to Government agencies at the end of year 2002 were SR 2.5 and 3.8 billion, respectively.

2.7.5.2 The Saudi Electricity Company (SEC)

In 1972, the Department of Electricity Services was established. It was separated from the Ministry of Commerce and given the additional responsibility of planning electrical services for the Kingdom as a whole. In 1974, the Ministry of Commerce was divided in two. One part became the Commerce Agency, the other the Industry and Electricity Agency.

In the same year the electricity tariff was set for all companies at a level below actual cost. In 1975, the Government adopted ambitious plans for economic development requiring very large investment in the development of industry and electrification. The Ministry of Industry and Electricity was formed, with an Industrial Affairs Agency and an Electricity Affairs Agency. The Electricity Corporation was established in 1976 to undertake responsibility for coordinating and achieving the ambitious electricity plans contained in the Kingdom's Development Plan.

From 1976 to 1981 all community electricity generation was gradually subsumed under the four regional Saudi Consolidated Electricity Companies (SCECOs), located in the Central, Eastern, Southern, and Western regions of the Kingdom. With the formulation of a coherent development plan and the establishment of the SCECOs, the Government was able to implement an electrification programme that brought electricity to the towns and, from the towns, to the villages and settlements throughout the Kingdom. The first SCECO (SCECO-East) was created in 1976. This was followed in 1976 by SCECO-South. Another consolidated company provided electricity for the south west of the Kingdom, and the central region was served by SCECO-Central.

The General Electricity Corporation (GEC) was a Governmental entity operating under the jurisdiction of the Ministry of Industry and Electricity. It had overall responsibility for the Kingdom's electricity system and had direct responsibility for the provision of electrical supplies to rural areas not then covered by SCECOs.

Under its Decree No. 169 dated 19.11.1998, the Council of Ministers approved the restructuring of the electricity sector with its main components (generation, transmission and distribution) and regulating its administrative and financial status, aimed at consolidating the ten electricity companies in the Kingdom into one company under the Saudi Electricity Company (SEC). Restructuring the electricity sector was the precursor to full privatisation to rationalise electricity consumption and to allow private sector independent power producers to participate in this vital sector.

In November 2001 an independent authority, the Electricity Services Regulatory Agency (ESRA), was established to review the cost of electric energy and its tariff. From the time the SEC was formed in December 1999 until the establishment of ESRA, electricity tariffs were issued by the Council of Ministers. The tariffs used by SEC were higher than the ones used by former SCECOs since the new maximum tariff was set at

38 Halalas¹² compared to 20 Halalas for the old tariff. In October 2000, before establishing the ESRA, the Council of Ministers reduced the Tariff significantly and maximum tariff went from 38 to 26, which caused a reduction in operational revenues by approximately SR 2 billion for the 12 month period ended 31 December 2001, compared to the 9 month period ended 31 December 2000.

In 2001, the company's capital was set at SR 38.3 billion, divided into 765,755,418 shares (74.15% for the government, 6.89% for Saudi Aramco, and 18.96% for the private sector). The share value was set at SR 50. The company's total assets stood at SR 90.6 billion, its total operational revenue was SR 28.3 billion, and its total operational expenses were SR 25.5 billion. It ended 2001 with posted profits of \$332 million (SEC, 2001). In 2002, after registering a loss of \$182.9 million in the first half of the year, the SEC ended the year with a net profit of \$270.4 million, mainly owing to high power consumption during the hot summer months (Arab News, 20th April 2003). The Company served approximately 3.8 million customers in 2001 compared to 216,000 in 1970 and customers are expected to reach 8.5 million in 2020. Therefore, the Saudi Government plans to invest as much as SR 438 billion by 2020 to meet growth in demand from a soaring population (up to 38 million) (Arab News, 20 April 2003). It also plans to grant concessions to the private sector to construct new power plants (generation sector) on a BOT (build-operate-transfer) basis.

2.8 Summary

During the past three decades, Saudi Arabia has paid great attention to the implementation of long-term economic reform. The Saudi Government has also put great effort into financing Government spending (operation and investment), providing public services, building infrastructure projects and financing the growing volume of its activities. The effort of economic reform by the Saudi Government has been associated with a growing role for the private sector that is reflected in its growing contribution to production, investment, employment and exports.

The Saudi Government's need for providing public services efficiently, raising enough funds, cutting spending that the private sector can handle and completing the

¹² SR 1 = 100 Halalas

requirements for the accession to the WTO, such as an open market, led it towards a policy of privatisation. The Saudi privatisation experience is different from other countries. It is different from any other developing countries as the motivation for privatisation is different. The main motivation for privatisation in developing countries is the outside pressure from the World Bank and developed countries that force developing countries to change and adopt systems based on their successes.

However this is not the case of Saudi Arabia as the country has entered privatisation with total freedom. Saudi Arabia, based on the World Bank classification, is considered as developing country but it is a very wealthy country, so it has a unique situation since whilst it cannot be considered a developed country, it is a very rich and sophisticated developing country. Therefore the Saudi privatisation experience cannot be compared to any other country's experience.

Chapter Three will provide a review of the concept of Management Accounting Control Systems, the aspects of Management Accounting Control Systems, and the changes in the aspects that are likely to follow changes in ownership.

Chapter Three: Literature Review

Introduction

For businesses the need for organisation, in the sense of determining objectives and subsequently developing systems to successfully achieve these objectives, is implicit. At the same time, systems that have been put in place need to be controlled and monitored against original objectives in order for them to be deemed 'successful'.

Indeed 'Organisation' of any kind, without some form of control, would be impossible (Tannenbaum 1968), a fact further endorsed by McMahon and Ivancevich (1976:349) who claim 'there is practically universal agreement that organisation implies control' and Otley & Berry (1980:232): 'control is a central and inescapable feature of all human organisations'. Flamholz, Das and Tsui (1985) cite three additional elements to be considered in the context of control: the external environment, organisational structure and organisational culture, all having a significant effect on the nature and change of the management control systems.

The chapter will explore the concept and framework of management control systems and investigate the relationship between privatisation and control systems. The components of management accounting control systems will be explained in this chapter. The three elements of the context of control will be discussed as well as the relationship between accounting and accountability and control. The final part of the chapter will discuss the changes anticipated as a result of changes in ownership namely privatisation. Thus the chapter is organised as follows:

- (1) Concepts of management control;
- (2) The framework for management accounting control systems;
- (3) The relationship between privatisation and control systems;
- (4) A description of the ten aspects of management accounting control systems used as a basis for the investigation in this study;
- (5) Description of current Saudi management accounting control systems;

- (6) Summary including a description of the subsequent hypotheses to be tested in the remainder of the project.

3.1 Concepts of Management Control

Although there is some ambiguity in defining the meaning of the terms ‘organisation’ and ‘control’, there nevertheless remains common consensus that the latter is a fundamental part of organisational activity. In fact, organisation can itself be viewed as a control process, occurring when groups of people feel the need to co-operate in order to achieve purposes, which require their joint action (Otley and Berry, 1980).

In order to understand the nature and meaning of control in organisations, it is first necessary to understand what is meant by control in general. Conceptually a control system can be considered as a ‘black-box’, converting a stream of inputs into a stream of outputs, with the internal details of the process being ignored for the present.

The term ‘control’ is probably one of the most inadequately defined in the English language, having a wide range of suggestions. Rathe (1960) listed ‘57 varieties’ or interpretations, ranging from ‘prohibit’ to ‘manipulating’. However, within this variety there are two major themes: (i) the idea of control as domination where the person ‘in control’ is the one who has the power to enforce his will on others; (ii) the idea of control as regulation where the controller detects a difference between ‘what is’ and ‘what ought to be’ (Vickers, 1967) and here this difference acts as a motivation for action.

Application in a business context includes both of these strands of meaning, implied in Webster’s Dictionary definition (1961):

Application of policies and procedures for directing, regulating and coordinating production, administration and other business activities in a way to achieve the objectives of the enterprise.

In a more general sense, control is concerned with the processes by which a system adapts itself to its environment. That is, in a self-regulating system, such as a business enterprise, both the specification of objectives and the means of their achievement are internally generated and form part of the control process. This point of view is reflected

in a definition of management control put forward by Lowe (1970: 765) where he defines a management control system as:

A system of organisational information seeking and gathering, accountability and feedback designed to ensure that the enterprise adapts to changes in its substantive environment and that the work behaviour of its employees is measured by reference to a set of operational sub-goals (which conform with overall objectives) so that the discrepancy between the two can be reconciled and corrected for.

There are multiple dimensions to control in organisations (Merchant, 1985): it is shaped by or 'through' processes of education, socialization and coercion and due to these implied interactive processes control it is often seen as a procedure which cannot be directly observed.

To state that somebody is controlled by, or controls somebody can only be inferred by indicators, such as certain patterns of behaviour, or certain meaning individuals attribute to a situation or action (Scheyt et al., 2003).

According to Antony et al. (1989), management control is

A tool for managers who use it in their interaction with subordinates. It is a people-oriented process. Line managers are the focal points in management control. They make the plans for implementing strategies and attaining goals, and they are the people who must influence others and whose performance is evaluated.

There are four necessary conditions that must be satisfied before any process can be said it's controlled (Otley and Berry, 1980). First, objectives for the process being controlled must exist: without an aim or purpose control is meaningless. Secondly, the output of the process must be measurable in terms of the dimensions defined by the objectives, i.e., the degree to which the process is attaining its objectives must be assessable. Thirdly, a predictive model of the process being controlled is required so that cause of the non-attainment of objectives can be determined and proposed corrective actions evaluated. Finally, the ability to take subsequent action must exist in order that deviations from successfully attaining the objectives can be reduced. If any of these conditions fail to be met, the process can no longer be said to be 'in control'.

3.2 The Framework for Management Accounting Control Systems

The choice of an appropriate management accounting control system is contingent upon the organisation itself, its specific circumstances and the nature of its objectives.

Not only will these objectives heavily influence the choice of performance measures to be used, they will also act as the criteria against which the choices that have been made can be evaluated (Otley, 1999). Any control system requires objectives and goals against which its performance can be assessed, but, as Otley and Berry (1980) maintain, no specific contingent formulation is necessary to appreciate that the existence of different goals need the selection of different performance measures and control.

Therefore it is acknowledged that the development of strategies and long-term plans for an organisation is part of the planning and control process of management. In a widely adopted definition of management control, Anthony (1965) suggested a hierarchy for planning and control:

Level 1: Strategic planning:

Any organisation should have one or more goals and senior management will decide or participate in deciding the general nature of the activities that the organisation should undertake in order to achieve these goals;

Level 2: Operational control:

Processes devised to carry out the day-to-day activities of the organisation, comprising rules, procedures, forms, and other devices that govern the performance of specific tasks.

Level 3: Task Control:

Determining the specific tasks needed to achieve the day-to-day activities.

Management control functions as the link between the first two types of planning and control stages in order to implement strategic policy. It does not focus on detailed operating decisions, nor on the activities that are the focus of task control; rather, it is the means by which management ensures that the organisation carries out its strategies effectively and efficiently. Thus the two main functions of the process of management control according to Anthony (ibid.) are:

- a) The planning and coordination function which ensures that the day-to-day tasks are performed by all participants to the achieve organisation's goals; and
- b) Providing a monitoring and feedback function, which is used to ensure that, planned actions are achieving desired results.

However, Lowe and Puxty (1989) have subsequently argued that Anthony's approach is too restrictive in that it has 'assumed away' many important problems. In their opinion, the first was concerned with defining strategies, goals and objectives: as such these procedures were complex and ill defined, with strategies being produced as much by accident as by design. The second problem concerned the methods used to control the production processes, which were dependent upon the specific technologies, which in themselves were widely divergent. The final criticism was that Anthony's reasoning concentrated upon planning and control through accounting rationales and contains little or no discussion of socio-psychological or behavioural issues.

Anthony's classification suggested that control was the last stage in the management process, but other authors have suggested that management control includes all parts of Anthony's hierarchy, for example, that control must be considered from a holistic and organisational perspective, which also relates to the environment (Lowe and Puxty, 1989).

In the context of continual change, particularly when organisations are reducing the workforce, Anthony's hierarchy becomes invalid and the holistic view of integrated management control succeeds (Otley, 1994). Anthony (1988) later suggested that the boundaries between categories are ambiguous, implying that management control can be broadly defined. Although Anthony (1965) specifically suggested that the study of control should be broadly based in the behavioural sciences, his work showed little evidence of borrowing from behavioural science and control has popularly taken on the suggestion of accounting control (Otley, 1994).

Management control systems are based on the idea that a system is an assembly of interconnected elements that functions as a collective whole (Wilson and Chua, 1993). They can be discussed in terms of process (what they do) and structure (what they are) (Anthony and Herzlinger, 1980). In terms of structure, management control systems are collections of control mechanisms, each designed to achieve some part of control. The structure or mechanisms used by any particular control system should be matched with the type of control found in the organisation (Wilson and Chua, 1993).

Scott (1981) distinguished closed and open system models, and then within each of these categories he further distinguished between rational and natural models.

In his opinion, closed system theories concentrated exclusively on the internal environment of the organisation, with closed rational models, as characterized by the scientific management movement. Thus they endeavoured to find the most efficient means of organising operations within organisations.

Closed natural systems approaches emphasise the behavioural aspects of control systems.

The beginning of cybernetics and systems theories indicated the emergence of an open systems perspective, where the most important development was an emphasis on the need to consider the external environment faced by an organisation when designing management control systems (Lowe, 1971; Beer, 1972; Emmanuel et al., 1990).

Contingency theories emphasised the importance of contingent variables such as technology, organisational size and structure for management control. These were rational approaches, however, which tended uncritically to accept the existence of the external environment and the need to adapt to it.

On the other hand, natural models within the open systems perspective were much more critical in their approach, emphasising the ability of factors to influence their environment. The studies included in 'Critical Perspectives in Management Control' (Chua, Lowe and Puxty, 1989) which emphasised such issues as the political nature of organisational activity, and the ways in which power was exercised.

These open natural models emphasised the changing environment and the ways in which management control has developed to deal with and sometimes resist that change. Radical changes in the political environment were crucial drivers of the need for organisational change including changes in management control in the public sector. Controls are considered and can operate at different levels: some are considered externally, on a societal level, sometimes by governments, but are operated within the organisation.

Other control systems are designed and operated within the organisation, for example management accounting and other performance reporting systems. Organisational structure provides a formal framework, which represents particular roles, rules and

procedures, and positions and prescriptions of authority. On a more abstract level are the values and ethics of a society, which influence the laws and controls, which are possible, as well as separating abnormality from acceptable behaviour.

Flamholz, Daz and Tsui (1985) capture all three aspects of control just discussed, and thus provide a useful model, given its concern with external, internal and cultural issues in control. They portray the control context as consisting of three elements: external environment, organisational structure, and culture.

The control context may either facilitate or reduce the effectiveness of the control systems in co-ordinating human efforts toward the achievement of organisational goals. It may facilitate control effectiveness by the additional control that is applied by several dimensions in the various contextual factors; for example, organisational formalisation, centralisation or standards of professionalism found in the organisation's external environment. The control context may reduce the effectiveness of the control systems if the control systems are incompatible with the norms, values, management philosophy or practices in the larger context (Flamholz, Daz and Tsui, 1985).

Kaplan (1983) states that the objective of a management control system is to provide information that is useful in decision-making, planning, control and evaluation.

According to Drury (2002), management accounting control systems are a form of result controls. These systems are largely defined in monetary terms, such as revenues, profits and ratios, and may also include non-accounting measures such as the number of customer deliveries. For him, the following steps are involved in result controls:

- Defining the performance dimensions such that they are congruent with the organisation's objectives;
- Setting performance targets to cover all aspects of performance dimensions;
- Measuring financial and non-financial performance; and
- Providing reward or punishment.

Anderson (1988) states that apart from being responsible for the setting of goals and decision-making on how these goals are to be reached, managers also play a key role in motivating employees to focus their attention on achieving them. According to Black and Porter (2000), managers use control as a process to assess whether the current operation is congruent with the organisation's objectives. From one point of view, control helps to ensure that the current operating systems meet what the organisation

has set out to achieve (Lorange & Scott-Morton 1974; Wheelen & Hunger, 2000). It therefore acts as an element in the feedback loop that alerts the manager to adjust activities to meet the objectives (Schermerhorn, 1999). From another point of view, the managerial control process is seen as deciding what activities the organisation should be doing and comparing actual accomplishments with these plans.

The managerial control process thus plays a very significant role in strategic management, which involves a long-range planning and strategy development affecting current operations, which in turn determines the future success of an organisation. Thus, the management control process involves both planning and controlling (Anderson, 1988; Anthony & Govindarajan, 1995; Black & Porter, 2000; Lorange & Scott-Morton, 1974). For example, if the organisation's goal is profitability, managers need to take appropriate measures or control those measures that could possibly influence future profitability. In so doing, they are able to make adjustments to their plans before problems get out of control (Wheelen & Hunger, 2000).

3.3 The Relationship between Privatisation and Control Systems

It is believed by many that privatisation and market mechanisms will lead to more efficient use of resources and their management (Vickers and Yarrow, 1988). Privatisation programmes have been widely imposed on less developed countries (LDCs) by the World Bank, the IMF and other western donors as a condition for bailing out the ailing economies of these countries (Cook and Kirkpatrick, 1995; Kikeri et al., 1994; Uddin and Hopper, 1999, 2001, 2003). It argued that privatisation would lead to better productive and allocative efficiencies (Boycko et al., 1996). Private enterprises are able to organise their factors of production to reduce production costs more efficiently than public enterprises. Private enterprises also have better reward and incentive systems, which are linked to economic performance and have a much clearer principal-agent relationship than public enterprises. Furthermore, the competition in the private sector enables private enterprises to be able to allocate resources more efficiently than public enterprises. As such privatised SOEs are subject to the discipline of the price mechanism through which inefficient activities may be eliminated (Rutherford, 1983). It is therefore assumed that productive and allocative efficiencies of

SOEs would improve upon privatisation (Adam et al., 1992, Hemming and Mansoor, 1988).

World Bank Reports (1995, 1996) justifying privatisation emphasise the lack of accountability and transparency in SOEs, and their immunity from market disciplines and the scrutiny of legal institutions. Kirkpatrick (1988) argues that if the principal objective of privatisation is to increase economic performance, the priority should be to increase competition rather than to transfer ownership.

Since the 1980s, privatisation has been the most significant policy in the wave of market reforms, which have swept over the global economy (Cook, and Kirkpatrick, 1995).

After more than a decade, researchers have moved on to address the outcomes and effects of privatisation (Uddin, 1997) and understand the performance of privatised enterprises (e.g. Weiss, 1995; Karatas, 1995,) together with their impact on societies (Cook and Kirkpatrick, 1995).

Some of these studies have addressed the internal issues of organisations (Potts, 1995), whilst other researchers have looked at the positive impact it has had on the economy as a whole (Nestor and Nigon, 1996; Sergio, 1996; Hartneck and McMahon, 1996).

However, other researchers found the opposite or mixed results (Jomo, 1995; Kararas, 1995). The World Bank (1992) concluded that privatisation has had a positive impact on economic performance, measured in terms of increased investment, improvements in productivity, and output growth and diversification.

Most research on internal accounting controls and privatisation has focussed on developed countries (for example, USA, and UK) (Espeland and Hirsch, 1990; Wright et al., 1993; Ogden, 1993). Espeland and Hirsch (1990) claimed that accounting controls played an important role in justifying ownership changes whilst Wright et al. (1993) investigated some important issues relating to “Finance and Control in Privatisation by Management Buy-Out”. They reported a positive impact made by management buy-outs, such as that it enables the introduction of more appropriate financial control systems, employment contracts and negotiating machinery, and frequently released former subsidiaries from the constraints on investments resulting from cash constraints on loss-making parents. They found that privatisation through management buy-out produced better financial control systems, employment contracts and negotiating machinery, and the release of investment constraints on subsidiaries .

The reasons for that are the stronger incentives that managers have and that privatisation moves the organisation from a bureaucratic to free market position.

Ogden (1994) demonstrated how accounting controls created customers and markets for privatised UK Water companies and transformed political objectives into apparently organisational performance matters.

Kirkpatrick (1988) has advocated privatisation on the ground that it will have a significant impact on economic performance at the enterprise level. He argued that the change in ownership will impose the discipline of private capital markets on the enterprise, thereby improving productive efficiency.

Potts' 1995 study concentrated on the privatisation of estate agriculture in Tanzania and found that production performance, after the ownership change, had been mixed. Two estates, out of many, had remarkably good production, but most of the other estates seem to have experienced further decline for two or three years before recovery. He implicates management problems in the declining performance. Potts concludes that there is no conclusive evidence to suggest that the economic performance of public sector estates in Tanzania has been worse than that of the private sector in general. He suggests, however, that substantial managerial autonomy and resources are important factors in improved performance.

The study of Karatas (1995), about the performance of pre-privatisation and post-privatisation firms in Turkey, admits the limitations of available performance indicators for the evaluation of post-privatisation performance.

Accounting researchers have examined the transformation of control systems in conjunction with ownership issues. The results of their research have highlighted the various effects of organisational control in the context of ownership changes (see Espeland and Hirsch, 1990; Wright et al., 1993; Ogden, 1993). Some of these studies are related to the changes of ownership and its relations to management accounting in general. This is due to the shortage of studies on the relationship between privatisation and management control systems.

Ogden's study (1994) is comprehensive and relates to privatisation and control issues. He attempts to theorise management decisions and the internal performance in newly privatised UK Water companies. Ogden analyses how water companies solicited customers, instead of being actively pursued by customers themselves, through the medium of a competitive market. Privatisation provided this opportunity for management and, in turn, management accounting played a central role in translating a political objective into an organisational performance matter.

Another study, undertaken by Wickramasinghe (1996), gives a comprehensive assessment of privatisation issues and the transformation of control issues in the context of a developing country. Wickramasinghe looked at two case studies from Sri Lanka, and made a series of comparative interpretations. He found that political influences over management control, and ineffective bureaucratic relations were common in the public mode of accounting control, while these characteristics were always connected to the traditional 'King Concept' (non-capitalist behaviour). On the other hand, after ownership changes, a private mode of accounting emerged, under which political influences and ineffective bureaucratic controls were reduced. He argued that although this institutional change was predominant in this mode of accounting, the articulation of cultural beliefs, and the dominance of production controls over accounting controls, was common to both modes of accounting, in both firms.

It can be argued that management control systems could be designed to consider some variables such as market and price, which is not common in the public sector. Nevertheless, accounting researchers have recognised the problematic nature of private sector MCS values. Values such as 'efficiency' and 'effectiveness' are too subjective and value-laden (Humphrey, 1991). Humphrey (1991) also commented that the common definition of effectiveness is the goal-model that developed from theories viewing the organisation as a machine. Organisations are assumed to be goal-seeking entities and their effectiveness is judged by their degree of goal attainment. A related assumption is that an organisation's chances of attaining its goals are maximised by increasing the goal-related activities. Yet the identification of goals is not as simple a task as assumed by government policy-makers.

Based on the above literature, it can be said that changes in ownership in general, especially privatisation, have a great effect on organisation in general and management

control systems in particular. The discussion now will turn to identify the aspects of management control systems that may be changed because of privatisation and identify the importance of each of them on the control systems within organisation.

3.4 Management Accounting Control Systems Aspects

As mentioned earlier, management control requires both planning and controlling activities. Planning is the process of setting goals and performance standards, then taking action to implement them. Control activities measure performance against these goals and standards; then remedial actions are taken to correct any deviations if required. Management control involves several activities, including:

- 1) Planning what the organisation should do;
- 2) Coordinating the activities of several parts of the organisation;
- 3) Communicating information;
- 4) Evaluating information;
- 5) Deciding on what action should be taken; and
- 6) Motivating employees to change their behaviour

(Anthony & Govindarajan, 1995).

The role of management accounting at a strategic level is to support the 'business model' of the organisation. This denotes how the company chooses to compete. Among the most important purposes of management accounting are to cover a wide range of financial activities such as financial planning and financial transactions, and to provide management with an evaluation of expenditure on property and people.

Medori (1998) identifies the following functional areas of management accounting:

- Pricing decisions, which require information about the cost of products;
- Integration of financial accounts and management accounts: this field of integration is concerned with the valuation of stocks;
- Investment analysis, which is concerned with making investment decisions by using a number of techniques (e.g. NPV and IRR);
- Budgeting, which provides a plan for achieving organisational strategy and a mechanism for performance measurement;

- The Performance Measurement System (PMS), which is used to improve process control and evaluation, and to compare the performance of different organisations, plants, departments, teams and individuals.

Management accounting control systems (MACS) are seen in this research as a package of management accounting control techniques and aspects that have been assembled in the MACS used by companies. Ferreira (2002) argued that while designing MACS, companies adopt certain MACS techniques and aspects. He stated (p.24):

These techniques will produce information with particular characteristics, which become characterising features of the MACS. The characteristics of information produced by MACS depend heavily on the features of the individual techniques included in it.

Based on other literature (Kaplan, 1984; Johnson and Kaplan, 1987; Stewart, 1991; Kaplan and Norton, 1996; Chong and Chong, 1997, Ferreira, 2002) there was a distinction between traditional and contemporary techniques. Uddin (1997) in his research to provide idealised management control systems in the private sector based on the problems that occur in management control systems in the public sector, identified five traditional aspects of management control systems which are: organisational objectives, budgetary system, intensive systems, accounting system, and effectiveness (Table 3.1 Idealised MCS's in Private Sector). Uddin (1997) did his study on Bangladesh and he generalized his findings and the aspects of MACS that he came out with to all developing countries. Ferreira (2002) added two other aspects to the MACS, which are the Balanced Scorecard (BSC) and Costing Systems especially the usage of Activity-Based-Costing (ABC), although he considered them as contemporary aspects of MACS.

Some other accounting researchers have been aware of the limitations of traditional approaches to control (Burchell et al., 1980; Tinker, 1980). These researchers criticised these approaches arguing that they were not adequate to explain the broader context of an accounting control system. Recently, some contemporary accounting researchers have been giving attention to understanding the organisational context of management control, systems such as the external environment, organisational structure, culture, and strategy, which will enrich our understanding of practices (Tinker et al., 1982; Gordon and

Narayanan, 1984; Merchant, 1984; Flamholz, Das and Tsui, 1985; Uddin and Hopper, 2003; Simons, 1995; Kennedy and Widener, 2008; Berry et al., 2009; Tsameny et al., 2010).

Table 3.1 Idealised MCS's in Private Sector

<i>MCS Issues</i>	<i>Problems with MCS in Public Sector</i>	<i>Idealized MCS in Private Sector</i>
Organizational Goal Setting	Multiple and conflicting objectives are to be set. Objectives are formulated with more consideration for social and political issues	Single organizational goals can be achieved. They are based on commercial criteria
Budgetary Processes	The central authority, using bureaucratic mechanisms, prepares the budget. It does not reflect the reality of the enterprise. It is not used for control purposes.	Budget is seen as an objective and rational control tool.
Role of Incentive Systems	Incentive systems are characterized by the permanent wage structure of government. Performance evaluation is bureaucratically built.	Reward structures provide motivation to measure the performance of employees
Role of Accounting Systems	Accounting systems are constrained by governmental regulations for control and auditing purposes. It ignores organizational settings	Accounting systems rationally provide financial and non-financial information for control
Effectiveness	Effectiveness is not viewed in terms of organizational profitability. It is viewed in terms of the achievement of governmental objectives.	Efficient performance of organizational activities

Source: Uddin, 1997

This study will use the five aspects of management control systems that are presented by Uddin (1997, two aspects from Ferreira (2002) and the three elements of organisational contexts suggested by Flamholz, Das and Tsui (1985) in relation to management control to investigate and understand the changes that have been effected by Saudi privatised companies after privatisation (Table 3.2).

Table 3.2 The aspects of MCS and the three elements of organisational context that will be investigated in the study:

<i>Aspect of MCS and Elements of Organizational Context</i>	<i>Author</i>
Objectives Setting and Strategy	Uddin (1997)
The Budgetary Process	Uddin (1997)
Incentive Systems	Uddin (1997)
Accounting System	Uddin (1997)
Effectiveness (PMS)	Uddin (1997)
Balanced Scorecards	Ferreira (2002)

Costing System	Ferreira (2002)
Organizational Structure	Flamholz, Das and Tsui (1985)
Organizational Culture	Flamholz, Das and Tsui (1985)
External Environment	Flamholz, Das and Tsui (1985)

3.4.1 Objective Setting and Strategy

Public enterprises have been created for objectives influenced by statutory requirements, central government interventions and national and local, political and domestic processes (Jones and Pendlebury, 1988). Being consistent with a country's development goals, the public sector has to face conflicting objectives such as profit earning vs. providing services to the population. The idealised MCS of the public sector does not consider these contradictory factors when setting goals and more often than not objectives are set by bureaucrats who are totally unaware of the organisational context (Uddin, 1997).

On the other hand, it can be argued that public sector objectives can be achieved through recognising the dynamic nature of the organisation and society. Thus, the problems of the public sector may not lie in multiple objectives or ownership; rather they lie in the recognition of the reflexive relationship between the organisation and society and politics (Hopper et al, 1986).

The view of the idealised MCS of the private sector argues that rational goals can be set as they represent a congruence of interests (such as customers, shareholders, and managers). In addition, goals and objectives in the private sector are clear, specified, measurable and are set based on commercial criteria (Uddin, 2003). He also stated that setting objectives is a result of the collective work of managers at all levels, as each division can set its objectives based on the general objectives of the company.

The importance of the relationship between business strategy and MCS is now widely recognised in the management accounting literature (Simons, 1995; Gosselin, 1997; Otley, 1999). Miles and Snow (1978) made the distinction between four types of strategies that they named defender, analyser, prospector, and reactor. They maintained that the defender focus is primarily focused on internal operations, prospectors on

environmental scanning, whilst analysts divide their attention between internal operations and scanning the environment for new opportunities.

Further, they established a relationship between the strategies pursued and control system characteristics. According to them, defenders concentrate on efficiency levels, cost control and monitoring trends. By contrast, prospectors keep on monitoring their environment in search for new opportunities, leading them to give priority to planning activities and using more 'soft' measures. In turn, analysts try to combine the better of these two worlds keeping their attention not only on internal operations, but also in scanning their environment. It is the lower intensity in doing this that makes the difference between analysts and both defenders and prospectors. Finally, reactor companies do not follow a coherent pattern of behaviour; this implies that no prediction can be rationally made regarding their activities.

Simons (1987), in his study about the relationship between strategy and accounting control systems, showed that the accounting control system does respond to the different strategies and objectives followed by companies. The evidence suggested high performing companies following a prospector-type strategy attached greater importance to forecast data, to setting of tight budget targets, and to close monitoring of output.

From the above arguments, it would be expected that due to privatisation an organisation would change its objectives so that they are set on a commercial basis, taking account of other social and political factors, whilst when state-owned it took account of social and political s rather than commercial factors. These new objectives would enhance the focus on the company's profitability and achieving organizational targets rather than meeting targets set by the government. Each management level in each department would share the process of setting objectives, as they would set their departments' objectives and would be held accountable for them.

3.4.2 The Budgetary Process

The budgetary tool is the principal control mechanism of financial MCSs. Previous research findings in developing countries have revealed that the budget plays a traditional role only, not only in control mechanisms of the public sector, as it is only concerned with presenting how the organisation spends government money (Hoque and

Hopper, 1994, 1997; Wickramasinghe, 1996). However the public sector budget is subject to governmental authorisation whilst in the private sector budget is conventionally seen as a tool for objective and rational control over sub-units (Uddin, 1997).

Wildavsky (1979, 1975) argued that budgeting systems accomplish many purposes beyond achieving control since they are forms and sources of power, and serve both as guardians of scarce resources (Budgeters) and as advocates of sub-units (Budgetees).

In general, the budget is seen as a means of decision-making, and a process of planning and control (Anthony et al., 1992). However in many public enterprises the budget is not properly prepared. It appears as a mere adaptation of the previous year's budget due to untrained managers and the absence of management dialogue between accounting and other departments (Uddin, 1997).

Previous studies on public management control have revealed that participation in the budget is totally absent in the public sector. Rather, the budget comes from top management, which is usually unaware of the circumstances of particular departments (Hoque, 1993; Uddin and Siddique, 1995).

Budgetary control is an important part of a firm's management control systems (Merchant, 1998). The way in which corporate managers seek out performance information, the type and detail of the information they ask for and the arrangements they have for discussing the results with business-unit managers are all part of the budgetary control process (Anthony and Govindarajan, 1998). This process comprises the following three components:

- i. Emphasis on meeting the budget – i.e., the extent to which the evaluation of managerial performance is primarily based upon the business unit managers' ability to continually meet the budget on a short term basis (Anthony and Govindarajan, 1998; Hopwood, 1972).
- ii. The amount of information detail required for budget reviews – i.e., the extent to which subordinates are required to submit reports that discuss performance to date, identify variances and propose detailed corrective actions if it appears that the budget targets are not being met (Anthony and Govindarajan, 1998; Merchant, 1981).

- iii. The intensity of budget-related communications- i.e., the extent to which budgets are used to facilitate information exchange throughout the organization, to force analysis and debate, and to assist corporate managers to personally involve themselves in the decision-making activities of their business-unit managers (Simons, 1995).

Al-Sughayer (2001) in his study of the budgetary process in Saudi Arabia found that budgetary control in Saudi Arabia is concerned primarily with regularity and compliance and does not direct any attention towards an evaluation of the efficient use of resources or the effectiveness of plans and objectives. He gave as a reason for the absence of an appropriate mechanism for enforcing budget reforms the fact that in the country's political system power was mainly centred in the hands of the government, which led to strong intervention by the government in the budgetary process and control within the organisation. Finally he concluded that effective change in accounting and budgeting practices would most probably occur if it is preceded first by a change in the organisation's operating strategy and then a reorganisation of its administration and structure.

Form the above discussion, it would be expected that due to privatisation, an organisation would gain full autonomy in setting its budget and would use it as a tool to evaluate and control its activities

3.4.3 The Role of Incentive Systems

Incentives are an essential element for a perfect control system, yet the idealised MCS of the public sector does not place any emphasis on them. The wage structure of the public sector in LDCs is largely fixed and extra rewards are rarely used. Wage structure and bonus systems are devised by bureaucrats who do not consider organisational needs, participant values or production relations, while employing wage structure and reward systems on the shop floor (Murshed, 1989).

On the other hand, the reward structure of the private sector is seen to be more effective, since it considers the performance of the individual (Uddin, 2003). Reward systems are

concerned with two major issues: performance and rewards. Performance includes defining and evaluating performance and providing employees with feedback. Rewards include bonuses, salary increases, promotion, stock awards, and perquisites (Kerr and Slocum, 2005).

Performance measurement and incentive systems may assist in developing and achieving strategies by providing clear signals about the intended strategic direction and supplying the necessary motivation by rewarding behaviour that is goal directed (Lawler and Rhode 1976). Reward systems encourage employees to work toward planned strategic outcomes (Carey 1992). Reward systems require performance measurement systems to evaluate performance and determine bonuses (Carey 1992).

Reward systems can motivate employees to pursue strategic priorities by setting performance measures targeted on priorities and sharing rewards between employees and the organization, based on achieving these performance targets (Carey 1992; Welbourne et al. 1995). These systems emphasize employee involvement in co-operating to improve performance as well as formulating rules governing performance measures and the distribution of rewards (Bowen and Lawler 1992).

Tsamenyi et al., (2010) in their study of privatised companies in Ghana argued that before privatisation, organisations lacked proper supervision of employees. They argued that “employees were not disciplined and there was no effective means by which workers could channel their grievance” (p: 437). They argued that labour cost efficiency was low before privatisation. They mentioned that the governmental organisation has to obtain the related ministry’s approval before it can take any action like disciplining employees. They stated that before privatisation employees’ wages were not competitive enough, resulting in low employee morale and job satisfaction. He also stated that due to the lack of creativities and motivations, employees were hardly given training and refresher courses by the organisation to keep them up-to-date in their knowledge. Finally they mentioned that these entire problems lesser after privatisation.

From the above arguments, it would be expected that as a result of privatisation, an organisation would develop a competitive reward system for its employees based on accurate evaluation of employees’ performance. In addition the organisation would provide its employees with adequate training and development activities to keep them up-to-date and improve employees’ performance.

3.4.4 *The Role of Accounting Systems*

An appropriate accounting system is an important tool that gives visibility to the activities of an organisation, and can help enforce accountability (Uddin, 2004).

Roberts and Scapens (1985) argue that the use of accounting information in organisations should be understood in terms of the role it plays in the production and reproduction of systems of accountability

The 'New Public Management' literature is a valuable source of studies concerning the importance of accounting in changing organisational contexts, and of relevance to this study, given its consideration of an industry which moved from a public sector nationalised industry to a new privatised status (Uddin, 2004).

With regard to the earlier discussion of accountability, there are important implications for accounting in the move from the emphasis on stewardship in the old public sector to the new emphasis on measures of economy, efficiency and effectiveness. Attempts to quantify performance mean that accounting has a central role as a control mechanism in public sector reform and several authors have considered the effect of this in a variety of organisational contexts. These studies are helpful in considering not only the external environment of control within which change was taking place, but also the relevance of accounting for internal and cultural issues (ibid).

An important issue in relation to external accountability is the use made of accounting information in regulatory decision-making, and the reporting requirements for management in this regard. Given that accounting information is presumably an important factor in the regulator's decisions, to what extent is he/she required to disclose the accounting basis of decisions? With regard to the internal operations of the organisation, the new emphasis on profitability and efficiency would also impact on the priorities within the organisation (Ferreira, 2002).

With regard to the external environment, authors such as Miller and Rose (1990) recognise the importance of accounting in enabling change at the macro level of society as a whole. They discuss the importance of how regulatory mechanisms enable

‘government at a distance’, in particular the use by government of a range of ‘technologies’ and the complex mechanisms through which it becomes possible to link calculations at one place with action at another.

Humphrey, Miller and Scapens (1993) discuss the rise of ‘accountable management’ in the public sector and emphasise the usefulness of accounting-based technologies in such initiatives, with their potential for extending discretion and choice for individuals, while still ensuring that actions are taken in accordance with broader economic, financial and social objectives of government. However, they emphasise that:

The continuing mobilising power of the accounting potential, in the face of unmet expectations, unintended consequences and criticisms, suggests that ‘accounting should be accounted for’ (Hopwood, 1985:cited in Humphrey, Miller and Scapens, 1993 p: 18, 19).

Considering now the importance of accounting to the internal environment of organisations, Humphrey (1994) examines the role of private sector management consultants in the implementation of FMI (Financial Management Initiative) in the probation service. His study illustrates the difficulties of applying traditional management accounting principles in complex public sector organisations, and questions the claims to expertise of the consultants with their ‘quite restricted notions of management and control’. This theme of doubting the efficacy of private sector accounting practices for the public sector is recurrent in much of the NPM literature. Several authors (Carter, 1989, 1990; Humphrey and Pease, 1991; Pollitt, 1986, 1990; Hood, 1991) focus their research on the variety of performance measures that have been introduced to different areas of the public sector, in the name of promoting ‘economy, efficiency and effectiveness’. They suggest that the dominance of financial and economic measures may render other discourse less visible, and suggest that wider issues such as quality of service and equity in its provision are likely to suffer as a result. Keat (1991) in discussing issues of the restructuring of organisations suggests that the model of the commercial enterprise has taken on ‘paradigmatic status’, manifest in various corporate organisations undertaken by public sector managements to provide a sharper focus on financial performance.

Turning now to studies that emphasise organisational culture, it has been argued that accounting can play an important role in transforming organisational cultures (see section 3.4.9). Laughlin (1991) points out that accounting systems are an important part

of an organisation's design and crucially linked to its interpretive schemes. Dent (1991) and Capps et al (1989) both examine accounting's capacity to provide new frames of meaning within which organisational actors may operate. Dent's study documents the eventual rise of the new business culture in European Rail over the traditional engineering/railway culture, and the resistance to change along the way. Other important studies in this vein include a series of articles written about the National Coal Board (Berry et al, 1985; Hopper et al, 1986; Capps et al, 1989), which emphasise the importance of tradition and organisational culture for understanding management control in the NCB, within a changing social and political environment. Ogden (1994, 1995, and 1997) has examined issues of accounting and accountability in the context of the water industry. In the case of utilities, privatisation has meant a new focus on profitability and shareholder value. Ogden (1995) discusses these changes in relation to the water industry in the UK in terms of the emergence first of 'a vocabulary of costs' and subsequently of a 'vocabulary of profits'. Ogden emphasises how the professional judgments of engineers have become less important as more attention has been devoted to financial measures and argues that resistance to the change is illustrated by senior management's continuing efforts to transform the corporate culture from one based on engineering and operating demands to one based on business priorities and customer needs.

Miller (1992: 80) provides an interesting view of accounting information's role in decision-making, which is relevant to the regulatory process, and which encapsulates the findings of many of the studies just discussed:

Along with other practices of government, the technologies of accountancy often intersect poorly with the specifics of the 'real'. The conditions that would make them work 'perfectly' are frequently absent, unplanned outcomes emerge, and new situations make existing technologies obsolete. Paradoxically, this is not an obstacle for calculative technologies but a source of their strength, for the alleged shortcomings of one calculative technology allow consultants and others to demonstrate the advantages of a new one. As with government, we find a conviction that there exists a calculable answer to the problems of the enterprise and even of social life. This conviction, often devoid of empirical evaluation, underlies much of contemporary accounting.

It can be argued that Management control systems in the public sector view an accounting system as a system, which only prepares annual reports for auditing and

stewardship purposes. These reports are not considered in problematical decision-making or controlling purposes. Decisions in most cases depend on bureaucratic procedures. Accounting information is rarely used for this purpose. On the other hand, the idealised MCS of the private sector views accounting systems as instruments for providing qualitative and quantitative information (Uddin, 1997). The usefulness of accounting information in decision-making does not depend on the way it is presented, rather on the way it is interpreted. It is thus apparent that the idealised role of accounting in private and public sectors disregards its social construction. Critical accounting studies have argued that accounting information cannot be useful until and unless it is interpreted in the socio-political context of the organisation (Tinker et al., 1982; Berry et al., 1985; Hopper et al., 1986; Cooper and Sherer, 1984).

From the above arguments, it would be expected that accounting information in privatised organisations would serve more purposes than in the public sector. The accounting systems that would be used in the privatised company would provide qualitative and quantitative information and reports for internal control purposes and to aid decision-making. In addition, it would be expected that accounting information would provide fair presentation of the organisation's financial situation for investors.

3.4.5 Effectiveness

It is argued by accounting researchers that proper control systems play a significant role in effective organisations. Nevertheless, the term 'effectiveness' is itself a questionable word, depending on how it is viewed (Humphrey, 1991). Organisational effectiveness refers to the extent to which organisational goals are achieved. Conventionally, organisational effectiveness has been seen as the degree of efficiency achieved through organisational functions. Idealised MCS accept this concept of organisational effectiveness (Uddin, 1997). Idealised control systems have problems in addressing complex organisational issues. It is also recognised that control systems are subject to various limitations driven by social, political and cultural factors (Hopper et al, 1986). In idealised management control systems, effectiveness can be recognised by sufficient performance measurement tools (Uddin, 1997).

One of the main roles of management accounting systems is applying performance measurement systems, which become a central focus of much management accounting research. Otley (2001) suggests,

Much of the thrust of the 'new' management accounting has been centrally concerned with the issues of measuring organisational performance (P:248).

Olson and Slater (2002) state that performance measurement is at the heart of the management control process in any organisation. As new strategic objectives are identified, the organisation may realize the need for new performance measures that encourage and monitor new actions (Dixon et al, 1990). Thus, organisations may use a broad range of performance measures to reflect the diverse nature of management decisions and efforts (Holmstrom, 1979; Banker and Datar, 1989; Feltham and Xie, 1994; Ittner and Larcker, 1998a).

Traditionally, PMSs have provided a means of monitoring and maintaining organisational control (Nanni et al., 1992), which is the process of ensuring that those strategies are implemented by an organisation that would result in the achievement of overall goals and objectives (Brignall and Ballantine, 1996). Various writers have defined performance measurement differently. For instance, Marshall et al. (1999) define PM as the development of indicators and collection of data to describe report on and analyze performance. Taking a more comprehensive angle, PM is a function of the efficiency and effectiveness of actions, according to Neely et al. (1995), who propose three definitions of a PMS as follows:

1. The process of quantifying the efficiency and effectiveness of actions;
2. A metric used to quantify the efficiency and/or effectiveness of actions;
3. The set of metrics used to quantify both the efficiency and effectiveness of actions.

Kaplan and Norton (1996b) maintain that measurement is a key factor, as management is impossible without both internal and external measures, and these have a huge influence on all personnel and stakeholders. Thus,

if companies are to survive and prosper in information age competition, they must use measurement and management systems derived from their strategies and capabilities (p.75).

Behn (2003) holds that managers can use performance measures (PMs) to “evaluate, control, budget, motivate, promote, celebrate, learn and improve” (p.586). He emphasises that there is no single performance measure, which is capable of fulfilling all of these eight purposes. Managers must recognise those purposes that any given PM might serve and how these measurements could be effectively employed. Hacker and Brotherton (1998) argue that an effective measurement system is one that helps managers to determine whether the activities which are being carried out within a facility do indeed support the achievement of objectives, thus helping the organisation to achieve its stated vision.

The information age environment has made it imperative for both manufacturing and service organisations to acquire new capabilities for competitive success. How well a company manages its intangible assets will have more bearing on its success than its physical, tangible assets (Kaplan and Norton, 1996c; Evans, 2005). Neely et al. (2004) emphasise that PMSs are an essential part of company strategy. Furthermore, executives may introduce new strategies and innovative operating processes rather than using the same short-term financial indicators they have been using for decades, such as return on investment (ROI), sales growth and operating income. Effective measurement, in their opinion, must be an integral part of the management process (Vokurka, 2004; Brewer et al., 2005).

PMSs can be classified into three main categories, two of which are quantitative measures of performance. The first comprises market measures, that is, those that reflect changes in stock prices or shareholder returns, and the second comprises summary accounting-based measures, which can be defined in either residual terms (e.g. net income after taxes, operating profit, residual income, economic value-added [EVA]) or ratio terms (e.g. ROI, return on equity [ROE], return on net assets [RONA]). The third category is qualitative measures, assessing subjective areas of performance such as ethical behaviour and the satisfaction of stakeholders, customers and managers (Parnell et al., 2000). They may also include employee satisfaction, delivery performance, process improvement, measures of material and parts delivery time, throughput time,

due-date performance, quality, machine flexibility, and inventory levels (Hendricks et al., 1996).

It is often argued that a drawback of accounting measures is that they induce a short-term focus (Jacobs, 1991). They are by nature backward looking and thus do not accurately reflect the effects of employees' efforts or decisions on future corporate performance. This problem is particularly acute in situations where investments in intangible assets are important (Lev, 2001). Managers whose performance is evaluated in terms of accounting income are discouraged from making investments in intangible assets by their conservative accounting treatment.

The shift to non-financial measures was not a criticism of financial measures as such, but a reaction to a change of question. Whereas to answer the original question, 'How am I doing against my objective?', it was reasonable to measure financial progress, when the question changed to 'What should I be doing for the future?' this was no longer appropriate, since financial PMs were essentially backward looking (Al-Sumairi, 2009).

Ghalayini and Noble (1996) review the differences between traditional (financial) and non-traditional performance measures (Table 3.3).

Table 3.3 Comparison between traditional and non-traditional PMs

<i>Traditional Performance Measurements</i>	<i>Non-traditional Performance Measurements</i>
<ul style="list-style-type: none"> ▪ Based on outdated accounting systems ▪ Mainly financial measurements ▪ Intended for middle and top managers ▪ Lagging metrics (weekly or monthly) ▪ Difficult, confusing and misleading ▪ Lead to employee frustration ▪ Neglected at shop floor ▪ Fixed format ▪ Do not vary between locations ▪ Do not change over time ▪ Intended mainly for monitoring performance ▪ Not applicable to JIT, TQM, etc. ▪ Hinder continuous improvement 	<ul style="list-style-type: none"> ▪ Based on company strategy ▪ Mainly non-financial measurements ▪ Intended for all employees ▪ On-time metrics (hourly or daily) ▪ Simple, accurate and easy to use ▪ Lead to employee satisfaction ▪ Frequently used on shop floor ▪ No fixed format (depend on needs) ▪ Vary between locations ▪ Change over time as needs change ▪ Intended to improve performance ▪ Applicable to JIT, TQM, etc. ▪ Help to achieve continuous improvement

Source: Ghalayini and Noble (1996)

According to Kaplan (1983), many academics, professionals and consultants encouraged the need for manufacturing companies to adopt non-financial performance

measurements, which then became a principal feature of PMSs and were used more extensively within companies (Frigo and Krumwide, 1999).

Ittner, Larcker and Randall (2003) conclude that the importance of all non-financial performance categories to long-term organisational success is less than the anticipated use of these categories in performance measurement and decision-making. They also indicate that extensive use of PMs for one managerial purpose does not necessarily imply that they are used for another. The overall evidence of the effect of non-financial measurement on accounting-based performance was mixed. The results also proved that non-financial measurement usage was significantly associated with innovation strategy, quality strategy, the length of the product development cycle, industry regulation and the level of financial stress. Finally, the association between non-financial measurements and company performance was dependent on whether the use of these measurements matched the company's characteristics. According to Kaplan and Norton (2001), there is a view that non-financial measures are better indicators of long-term performance and that they sustain the monitoring by managers of progress towards strategic objectives.

There is empirical evidence to suggest that financial and non-financial measurements are not substitutes. Rather, the latter are used as additions to the former (Govindarajan and Gupta, 1985). However, it is only recently that effective frameworks of performance measurement have emerged that integrates both types. These frameworks work on the principle that management accounting information systems cannot rely on financial measurement alone. Professional accounting associations have also encouraged the use of integrated performance measurements (Neely, 1999).

Based on the above arguments there was lack of the use of proper performance evaluation system on SOEs. It would be expected that privatised organisations would use more sophisticated performance evaluation systems including both financial and non-financial indicators.

3.4.6 *Balanced Scorecards*

Kaplan and Norton (1992, 1996, and 2001) define the Balanced Scorecard as a framework to facilitate the translation of the business strategy into controllable performance measures. In particular, the BSC is considered a comprehensive system of strategically aligned performance measures. Niven (2002: 16) defines the BSC as

A carefully selected set of quantifiable measurements derived from an organisation's strategy. The measurements selected for the Scorecard represent a tool for leaders to use in communicating to employees and external stakeholders the outcomes and performance drivers by which the organisation will achieve its mission and strategic objectives.

The BSC is beneficial to organisations in many ways. For instance, it focuses on accountability with respect to goals and objectives, and relates strategy to performance. It provides a means to assess whether progress is being made and enables the organisation to adjust accordingly. It gives employees a better understanding of the cause-and-effect relationships in regular activity (Misiaszek and Oriot, 2002; Vaivio and Jarvenpaa, 2002; Sandkuhl et al., 2003; Neely et al., 2004; Ahn, 2005; Anand et al., 2005; Crawford and Scaletta, 2005; Dilla and Steinbart, 2005; Lawson et al., 2005; Phillips and Louvieris, 2005). Many other benefits of the BSC have been recognized in previous studies and mostly they are related to control over the organisation overall activities.

Kaplan and Norton (2001a) argue that the BSC has evolved as a framework for measuring organisation performance. Recognising that measurement has consequences beyond reporting the past, they elaborated the BSC concept from a mere performance measurement system to an organising framework for a strategic management system.

Many researchers concur with the notion that the BSC is a strategic management tool, enabling senior management to communicate their vision for change, at the same time empowering business divisions and employees to find new ways of accomplishing day-to-day activities while working towards the company's strategic objectives (Epstein and Manzoni, 1998; Ritter, 2003). According to a recent Institute of Management Accounting survey of performance, the scorecard has proved to be an effective tool of strategy communication and clarification (Salterio and Webb, 2003). The benefits of using the BSC as a strategic management tool (Bailey et al., 1999) are:

- Enhancing communication within the organisation.
- Promoting the active formulation and implementation of organisational strategies.
- Improving the alignment of divisional or individual goals with the organisation's objectives and strategies.
- Updating organisational strategies and making them visible.
- Aligning annual or short-term operating plans with long-term strategies.
- Aligning performance evaluation measurement and long-term strategies.

Norreklit (2000) contends that apart from financial and non-financial measurements, the BSC also contains outcome measures and the performance drivers of outcomes, which are linked together in cause-and-effect relationships, making the PM system an integrated control system. Also, Kaplan and Norton (2001b: 94) recommended that

Every measure selected for a BSC should be an element of a chain of cause and effect relationships that communicates the meaning of the business unit's strategy to the organisation.

Thus, controlling the essential factors in a cause-effect relationship between measures may lead to a much better perspective on the requirements the business has in order to achieve its intended outcome performance (Lawson et al., 2005).

Interview data reported from a case study of a Fortune 500 company suggests that managers believe that the cause-and-effect relations included in their scorecard have resulted in increased efficiency and profitability (Salterio and Webb, 2003). Chang et al., (2002, cited by Kasperskaya and Oliveras, 2003) offer some preliminary evidence of the existence of cause-and-effect relationships within the Performance Assessment Framework (PAF) of the National Health Service in the UK.

BSC is a system that help organisation to transfer its strategies into controllable performance measures for the organisation and its employees. As a result the use of BSC can provide more efficiency to the organisation. It can be argued that an organisation can be efficient without using BSC if it uses the right performance measures and has a clear method for translating its business strategies into performance measures In the case of most of SOEs, they lack tools for translating their strategies and

goals into controllable performance measures; therefore it would be better for the organisation after privatisation to apply BSC, as the benefit would outweigh the cost.

3.4.7 Costing Systems

According to Drury (2000), a cost and management accounting system should generate information for meeting the following requirements:

1. Allocating costs between costs of goods sold and inventories for internal and external profit reporting;
2. Providing relevant information to help managers make better decisions;
3. Providing relevant information for planning, control and performance measurement.

The first item above is required primarily for meeting external financial accounting requirements. Most organisations produce internal profit statements for their business units at monthly intervals (Drury and Tayles, 1995) for management purposes. Thus, the first requirement is necessary for both financial and management accounting purposes. Many service organisations, however, do not hold inventories, so they do not need to allocate costs between goods sold and inventories. Routine and non-routine financial reporting is required for meeting the second requirement. Routine information is required at periodic intervals relating to the analysis of the profitability of products/services to ensure that only profitable products/services are marketed.

Nonroutine- financial information is also required for those strategic decisions that are made at infrequent intervals such as the introduction of new products or services and the negotiation of long-term contracts with customers. Accurate cost information is required for decision-making since inaccurate costs can lead to incorrect decisions such as the discontinuation of profitable products and the continuation of marketing unprofitable products. Less accurate information relating to product costs may suffice for meeting the first requirement above (profit measurement for a company or business unit) since the aim is to allocate costs between inventories and cost of goods sold at the aggregate level rather than the individual product level.

Drury (2000) explained the major differences between traditional and ABC systems. Both systems rely on what has become known as the two-stage allocation process. In

the first stage traditional costing systems assign indirect costs to cost centres (normally departments), whereas ABC systems assign costs to each major activity centre rather than departments. Therefore, the first distinguishing feature between the two systems is that ABC systems assign costs to a greater number of first stage cost centres (i. e. cost pools).

The second stage allocates costs from the cost centres to cost objects (e. g. products/services). Traditional costing systems allocate indirect costs to cost objects using a small number of allocation bases/cost drivers that tend to vary directly with volume produced. Direct labour hours/cost and machine hours are the allocation bases that are mostly used by traditional costing systems.

In contrast, ABC systems use many second-stage cost drivers including drivers that do not vary directly with volume produced. Examples include the number of production runs and the number of purchasing orders for allocating the costs of production scheduling and purchasing to cost objects respectively. Therefore, the major distinguishing feature of ABC systems is that they rely on a greater number of cost centres and different types of second stage cost drivers. By using a greater number of cost centres and cost drivers that are based on cause-and-effect allocations, ABC systems should report more accurate product/service costs. Traditional cost systems are likely to report less accurate costs because, in the first stage, they often allocate costs to only a very small number of cost centres (sometimes a single cost centre for the whole business unit) and make extensive use of arbitrary allocations in the second stage of allocating indirect costs to cost objects.

The criticisms of traditional product costing systems relate mainly to the reporting of inaccurate costs for decision-making. Traditional product costing systems are considered to be sufficiently accurate for financial accounting and profit measurement purposes. This is because it may not be necessary to measure accurately the resources consumed by individual products. The objective of the costing system here is to provide a reasonably accurate analysis of the total costs incurred during a period between cost of sales and inventories. Cooper and Kaplan (1988, p. 22) argue that most organisations use traditional costing systems, designed primarily for meeting financial inventory valuation requirements, to generate cost information for decision-making requirements. They claim that such costs are accurate enough for financial accounting, but are mostly totally inadequate in terms of accuracy for decision-making.

In recent years many researchers have drawn attention to the fact that traditional costing systems are unable to cope with the developments, which have occurred in business environments. By the mid-1980s, the prominent critics of traditional costing systems (Kaplan, 1985; Cooper and Kaplan, 1987) were highlighting their deficiencies in terms of the methods used to allocate indirect costs to products/services. They assert that direct labour or other volume-based costs drivers fail to measure the consumption of non-volume based activities accurately and, hence, result in distorted product or service costs. Using purely volume-based cost drivers tends to lead to over-cost high volume products and services and under-cost low volume products or services.

As the business environment in Saudi Arabia changed by implementing the privatisation policy, it would be expected that privatised companies would improve their decision-making process by applying an accurate and efficient costing systems, such as ABC.

3.4.8 Organisational Structure and Control

Organisational structure is an important element of control in organisations and this section will consider some of the views in the literature on why different structures exist, why they change and how they contribute to the control of organisations with different characteristics. An important feature of organisational change in the public sector in recent years has been the reform of organisational structures to facilitate the introduction of a new focus on market rather than public service modes of organisation.

The institutional economics theory of markets and hierarchies suggests that organisational structure will depend on the cost of obtaining information about organisational processes and outputs. Williamson (1975) suggests that the governance structures of organisations will take the form of markets or hierarchies depending on which one allows economic transactions to be conducted at lowest cost. The main distinction between the two is that in hierarchical organisations transactions are mediated by rules and procedures rather than by prices and the laws of supply and demand, as in market structures. From an institutional economics point of view, hierarchy is an inferior form of organisation, likely to result in inefficient operations.

Ouchi (1980) suggests that where outputs are easy to measure, but transformation processes are not well understood, the market structure is satisfactory, while hierarchical organisations are better suited where transformation processes are well-understood but outputs are difficult to measure.

He adds a third structure, which is the clan, where neither outputs nor transformation processes are well understood. A significant feature of organisations in which clan structures are important is the pre-eminence of professional expertise and judgement, and a sense of common purpose, based on shared values and beliefs, which binds individuals together without the need for more formal mechanisms of control, with traditional examples including the health and education sectors. Hierarchies and clans have been the prevailing structures in the service-delivery state, with the former based on bureaucratic mechanisms, strongly supported in many cases by common recognition of the importance of public service ethic.

Ezzamel and Willmott (1993) are critical of the markets and hierarchies framework that, as they argue, ignores the importance of power relations and the fact that market relations are usually based on a hierarchical structure of domination. Emphasising the importance of both political and cultural discourses in determining and defining appropriate structures, they contend that:

...The discourses and practices of economic rationalism are not 'given' or 'natural' but arise within and serve to secure and legitimise particular (historical) power/knowledge relations (1993, p.111).

In discussing the changes in the public sector, which have occurred in an attempt to introduce more market-based practices, they emphasise the importance of new structures of domination that serve the rise and reproduction of new groups in power. They also stress that such changes have strengthened hierarchical forms of control at the expense of clan modes of regulation, using examples from the health and education sectors to illustrate their case. While accountability in a hierarchical organisation is from subordinate to superior, based on legitimate authority, under a clan structure accountability is based on peer review. The authors emphasise that the increasing importance attached to new calculative and rationalistic technologies of accounting that promote competition and financial accountability may be incompatible with the 'sense of purpose and service' which is a tradition in the public sector. They suggest that new modes of governance violate basic tenets of faith in the public sector, with the result

that professionals have employed their developed clan control as weapon to attempt to resist changes, or at least to maximise their control over new arrangements.

They suggest five possibilities for organisational change deriving from the above. Firstly, actors may adopt new interpretive schemes, e.g. a move from a professional to a managerial approach to running an organisation is likely to lead to new structures evolving. Secondly, new values and interests may emerge, which require new structures, e.g. a new emphasis on profitability rather than service provision in the public sector. Thirdly, since the structuring of organisations is a political process, power relations are important, and the ascendancy of new factions of power may lead to the emergence of new provinces of meaning that subsequently shape the production and recreation of organisational structures. Finally, the last two possibilities for structural change relate to contextual constraints. Changes in technology, for example, may impact on organisational structure. More interestingly, turbulent change in the external environment may force changes in organisational structure.

The term 'horizontal organisation' has been used to highlight a perspective which views organisations as structured around a small number of business processes, or work flows, which link the activities of an organisation to the needs and capabilities of suppliers and customers (Ostroff and Smith, 1992). It is a perspective that has led to calls for management control researchers to pay more attention to lateral relationships, which involve co-operation and coordination amongst managers at similar levels of the hierarchy (Otley, 1994; Hopwood, 1996; Van der Meer-Kooistra and Scapens, 2004). Whilst modern organisations tend to be flatter, they are still hierarchies. So the challenge for management control is to develop concepts and systems that orchestrate both horizontal and vertical relationships (Berry et al., 2009). Techniques such as activity-based cost management and the Balanced Scorecard can provide ways of thinking about cost, value and performance that connect parts of the value chain between suppliers and customers. But they are not without their critics, given that major expectations of horizontal organisation are to encourage flexibility and learning, both of which often require effective co-ordination across the internal (functional) boundaries of organisations (ibid).

Perhaps more promising research into the relationship between management control and horizontal organisation has focused on the concept of responsibility accounting, which for several decades has linked organisation theory and management control theory. As originally conceived, it presented a model of organisations divided into responsibility centres, such as departments or divisions, where managers were individually accountable for sub-unit performance. Central responsibility accounting has been the controllability principle: the notion that a manager should be evaluated only on that which he or she controls (Berry et al., 2009).

As a result of privatisation, it would be expected that an organisation would change its structure to be clearer in terms of responsibility centres, as each department or centre will have a clear description of its accountability and responsibilities. In addition, the main concern of the organisation would change from only providing products and services, regardless of the economic benefit and customer needs, to be more concerned about customers' needs. Moreover, the restructuring of organisation due to privatisation would make managers co-operate more in setting sub-units goals and objectives.

3.4.9 Organisational Cultural and Control

Organizational culture is often defined as a net, which is woven around deep basic assumptions, beliefs, understanding, sense making and values shared by the organizational collectives. As a concept, it has developed through historical processes and it has potential for further changes. It can be said, however, that, to some extent at least, members of organizations tend to behave according to the patterns of an organizational culture (Alvesson and Berg, 1992; Martin, 1992). Geertz (1973:145) defines culture as the following way:

Culture is the fabric of meaning in terms of which human beings interpret their experience and guide their action; social structure is the form that action takes, the actually existing network of social relations. Culture and social structure are then but different abstraction from the same phenomena.

In looking further at the wider concept of organizational culture, it can be observed that there are often different subcultures within organizations. For example different professional groups have different views of the world and the nature of their business. Accountants might subscribe to one kind of philosophy and marketing people to another. Indeed, each group may have developed its own specialized language and set of favoured concepts. In this process of definition and delineation, functional barriers can be very real, resulting in a set of professional subcultures that could lead to great difficulty in communication (Jarvenpaa, 2007).

Culture is typically presented hierarchically, based on the stability and tangibility of the cultural elements. Artefacts, such as physical products of the culture, collective mental frameworks (such as symbols and heroes) and collective action patterns (such as rituals), form the outer part and values form the inner part and basic assumptions at the core of the culture. These basic assumptions are the hidden, mostly unconsciously, and taken-for-granted structure of meaning that guide human behaviour.

Organizations have their own symbols, which represent special messages for their members. In addition, heroes represent the valued characteristic of the organization and provide role models.

Rituals are ceremonial events, which support the values and beliefs of organizations and can strengthen a sense of identity and mutual connections. Symbols, rituals and heroes, as well as the physical artefacts such as system or products – the most visual forms of cultural – are human artefacts and they are, thus, the easiest cultural elements to replace (Hofstede et al., 1990; Alvesson and Berg, 1992). Many aspects of an organization's culture are thus embedded in the routine of everyday life.

Smircich (1983), in discussing the significance of the concept of culture for organisational analysis, argues that it is possible to view culture either as a variable or as a root metaphor. Culture as a variable can be understood in two ways. When viewed as an external independent variable, it is:

...considered to be a background factor, an explanatory variable or a broad framework influencing the development and reinforcement of beliefs...it is imported into the organisation through the membership. Its presence is believed to be revealed in the patterns of attitude and actions of individual organisation members (p.343).

When viewed as an independent internal variable, culture is defined as:

...social or normative glue that holds an organisation together. It expresses the values or social ideals and the beliefs that organisation members come to share. These values or patterns of belief are manifested by symbolic devices such as myths, rituals, stories, legends and specialised language (p.344).

Many discussions of recent changes in the public sector address aspects of cultural change from the 'culture as variable' perspective. Metcalfe and Richards (1990) say that Rayner considered change in the 'culture of Whitehall' to be an essential prerequisite for lasting reform of civil service management, since 'an impoverished concept of management' was believed to restrict public managers to programmed implementation of predetermined policies, without addressing issues of adapting policies and organisations to environmental change. Management was concerned only with internal routines and procedures, and management control was exercised through well-defined hierarchies of responsibility and authority.

Wilson and Hinton (1993) discuss attempts to address these shortcomings as being part of a move from an administrative to a managerial culture. They suggest that the emergence of 'new managerialism' is characterised by the importation of private sector concepts and techniques into the public sector, moving public services to a market or profit-oriented culture. Dawson (1991) defines this particular development as 'client culture', which may be differentiated from a market culture by the absence of financial goals, and the existence of unwilling customers with no choice of service (e.g. social services clients).

Culture was held to affect organizational members' perceptions of technical controls, which meant the different national or organizational cultures might "require" different controls. Culture has two important effects on the MCS (management control system) process. It can affect the choice of stimuli to which the individual attends, or it can affect any value judgment about the stimuli. Studies of this kind proceeded from definitions of generic organizational control subsystems (e.g. planning, monitoring, evaluating and rewarding, Birnberg & Snodgrass, 1988, p.447) whose functioning could

then be confirmed as more or less effective depending on the psychological dispositions (cultures) of their users (organisational members).

Alnamari (1993) argued that in a management accounting context differences arise in both the planning and control dimensions and the choice of organisational design. Planning for the future is one area of difference. In developing countries, including Saudi Arabia, there is a widespread belief that no one can influence to any degree events in the future. Events occur simply as a matter of nature. This type of belief or an attitude toward the future differs from that of Western societies. In Western societies most of the people see themselves as having choices, which can influence outcomes in the future.

Lane et al (1988) argue that in a situation like this, goal setting would tend to be hesitant and vague and that budget systems would be futile. The feeling of being unable to influence events in the future would in effect complicate the problems of getting managers to work for the objectives of the company, to meet budget objectives or even to take a serious part in planning and control efforts.

Similar problems arise on the control side where Saudis do not like mistakes being pointed out or admit that they have no explanation for variances. This attitude seems to be found in many developing countries as part of the culture. Therefore, personal evaluation of a manager's performance in such circumstances must be handled carefully. All criticism in front of others should be avoided. Discussion of a manager's performance should be a very private matter and should be oriented to company objectives and how the managers can help achieve these objectives, rather than to his own shortcomings. Also, with regards to performance evaluation, the relationship between superior and subordinate in developing countries is often a personal one and Saudi society's culture is no exception. The predominance of this type of relationship then places participants at a disadvantage in the performance management process that demands a relatively objective and rational focus on job tasks and goals and on action plans to meet them. It can be seen in Saudi Arabia that there are some companies that do not hire relatives, friends or people from the same tribe (Alnamari, 1993). In addition, Saudi people in general, in terms of preferences for qualifications used to favour engineers, believing any ideas they produce and trusting them more than any other people. However, this was the situation 15 years ago, and now the society has

changed and is more ready to accept and trust different qualifications (Al-Dehailan, 2004).

Another phenomenon in developing countries is the tendency to extreme centralisation. Savage (1978) argues that managers in developing countries like most people of these countries, are the products of highly-structured, traditional societies, where all authority is derived from family (or tribe) position and submission to authority is seen as the way to avoid the anxieties of living. Since authority in the traditional society derives from position (as family or tribal leader or as business owner), only the elite are seen to have authority. Authority is a symbol of eliteness and for an official or an owner to give up or delegate authority is to give up a part of his eliteness. This may help explain why people from traditional societies often find it impossible to delegate authority even though they may agree with the concept of delegation as being necessary. Furthermore, individuals with tribal authority find it difficult to act in a business subordinate role.

It would be expected that privatised companies in Saudi Arabia would experience changes in the culture of the organisation and in their employees' attitudes towards the organisation. It would be interesting to investigate whether the changes in culture are a result of organisational efforts to change culture or whether they are a result of changes in other aspects of the companies such as changes on human resource systems or changes in reward systems or changes in accountability centres.

3.4.10 External Environment and Control

For this study, the external environment comprises the economic and political environment, the regulatory bodies and their official pronouncements, as well as public opinion, reflecting the prevailing values and ethics of society. This section will concentrate in depth on the UK, as there is a lack of resources on other countries' experiences. Dissatisfaction with the way in which many public sector organisations were operating led the Conservative government, elected under the leadership of Margaret Thatcher in 1979, to effect significant changes in the sector.

For the nationalised utilities, privatisation was seen to be the answer, since these industries were in the unusual position for a public sector organisation of being self-financing and charging individual consumers for products, at least partly on the basis of usage levels. Thatcher's determination to improve the efficiency of operations and break the power of the trade unions, together with her vision of a share-owning democracy, were important reasons for her decision to privatise the previously nationalised industries (Heald and Steel, 1984; Veljanovski, 1987; Graham and Prosser, 1991). The lack of a profit motive in public utilities, their protection from fear of bankruptcy and the lack of performance evaluation and incentives for management were all seen as factors, which contributed to their problems, which could be successfully addressed by privatisation. Freeing industry from the 'dead hand of the state' legitimated the changes.

All of the above initiatives are characteristic of attempts by government to render more visible the economy, efficiency and effectiveness of public service operations, and consequently to increase accountability for performance by service providers (Hood, 1991; Pollitt, 1990). The rationale has been to introduce the market-based practices of private companies, by means of surrogates for competition such as the purchaser/provider split, the growth of contractual arrangements and flexibility in pay and conditions for staff to enable high performance to be rewarded. Many performance indicators have been devised to enhance visibility (Wilson and Hinton, 1993; Carter, 1991; Pollitt, 1990). The appropriateness of private sector practices for public sector organisations has been contested by a number of authors. Stewart and Ranson's (1988) comparison of private sector and public sector models (Table 3.4) provides a useful summary of the different principles applicable to the two ideal types:

Table 3.4 Public Sector Model vs. Private Sector Model

Private Sector Model	Public Sector Model
Individual choice in the market	Collective choice in the polity
Demand and price	Need for resources
Closure for private action	Openness for public action
The equity of the market	The equity of need
The search for market satisfaction	The search for justice
Customer sovereignty	Citizenship
Competition as instrument of the market	Collective action as instrument of the polity

Exit as the stimulus	Voice as the condition
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Source: Stewart and Ranson (1988)

They emphasise the distinctive nature of the public sector, highlighting the importance of collective decisions for the provision of public services, and considerations of equity and justice, which are absent from the private sector model. They also distinguish between customers and citizens, saying:

The public domain has its own conditions, which are ignored at their peril. The public are not merely clients or customers of the public service organisation. They are themselves a part of that organisation as citizens. Citizenship can be a basic value in the public domain. In building citizenship management has to encompass a set of relationships for which the private sector model allows no place. (p. 15)

The 'notion of enterprise' and the development of an 'enterprise culture' have been discussed at length by several authors (Keat, 1991; Morris, 1991; Rose, 1992). Keat (1991) says that the reforms undertaken to encourage an enterprise culture involve an extension of the domain of the free market and competitive forces, requiring the reconstruction of institutions along the lines of the 'commercial enterprise'. Also important is the adoption of new marketing techniques and 'previously alien vocabularies and discourses', in particular the emphasis on the consumer, a term which has supplanted specific references to recipients of public services, such as student or patient.

The UK Conservative government saw the main benefit of privatisation as the introduction of competition, which would both reduce costs and improve the quality of service (Casson, 2004). Aharoni (1991) claimed that the improvement of efficiency in an organisation is more likely to be the result of a strengthening of the influence of market forces than of changes in ownership. Competition can be introduced without privatisation, and in many cases privatisation does not result in increased competition. He claimed that privatisation alone, without the introduction of competition, may simply transform a public monopoly into a private monopoly. Therefore he argued that regulation is often the result of creating private sector monopolies. With strong competition the need for regulation is less

In her study about gas industry in UK, Conrad (1999) argued that once privatisation is introduced in a country, competition might be introduced as well. This will make the business environment more open and it will encourage the government to bring pressure on the regulatory bodies to be more flexible and clearer in their relationships with organisations. The information required from privatised organisations by the regulatory bodies would be different, as the purpose of asking for this information has changed. She stated that with privatisation there would be a change in the nature of the stakeholder group, so the relationship with them would be changed. Before the privatisation it was only the government, which owned the organisation, but after privatisation there are other investors and shareholders beside the government, who need more transparency and more detailed and different kinds of information. Before privatisation the government set the prices of the services, but after privatisation, and because of competition, the organisation needed to set its services prices by itself. Sometimes these prices needed to be approved by the regulatory body, acting to counter the risks of monopoly power. The organisation would need to convince the regulatory body that the set of the prices that it selected was legitimate by providing them with accurate and clear cost information.

In the case of Saudi Arabia, SOEs were considered to be governmental bodies that spend money as requested, so the regulatory bodies would ask for information that showed how the company spent the money received from government. The main two regulatory bodies in Saudi Arabia before privatisation were the Ministry of Finance and the related Ministry to the organisation (Alharthi, 2001). The government set all the prices of the services and products that were provided by SOEs and sometimes these did not cover the cost (Al-Dehailan, 2004).

From the above, it would be expected that as a result of privatisation, the role of ministries would be reduced and new regulatory bodies would be established. These regulatory bodies would be concerned more with developing a fair market and their requirements would be different from government requirements. In addition, it would be expected that the organisation would have more autonomy in its pricing and would experience less involvement of regulatory bodies. Moreover, as a result of privatisation, there would be different stakeholders, such as suppliers, customers, shareholders, and banks, so their needs would be different in terms of their required information.

3.5 Management Accounting Control Systems in Saudi Arabia

Because State-Owned organisations in Saudi Arabia mainly emphasised non-commercial rather than commercial objectives and physical production planning rather than financial planning and control, management and cost accounting were ineffectively carried out and deficient in achieving a sufficient level of planning, control and accountability (Al-Dehailan, 2004).

Organisations' prime concern was to comply with statutory obligations and internal rules and regulations. However, statutory obligations were viewed as interventions and obstacles to achieving the organisations' objectives as well as generally conflicting with internal rules and regulations (Ibid).

The levels of control and accountability were weak; nevertheless they were slightly better in partly state owned than wholly owned enterprises because wholly owned enterprises faced more intervention. This not only demotivated organisations' management and reduced operational efficiency, but also encouraged corruption¹³ within management. These were mainly the result of the absence of adequate controls. Therefore, the lack of performance accountability in wholly-owned enterprises was not only due to the lack of good quality information or inadequate financial and managerial accounting systems and reports, but also due to the substantial impact of outside intervention, for example by the Ministry of Finance or high ranking royal family members, on many internal decisions. (Ibid; Ramamurti, 1991; Ayub and Hegstad, 1986).

The level of control in state owned enterprises was weak in terms of value for money. This was due to the lack of control over efficiency in the level of expenditure, level of revenue, and the inadequate use by managers of organisations' assets and economic resources. SOEs suffered from a great lack of cost awareness (Al-Dehailan, 2004).

The value for money concept was difficult for Saudi SOEs to achieve due to their lack of autonomy, which resulted in inadequate finance and budget to achieve the

¹³ Corruption in this context means that misuse of the public money intentionally, and in most cases taking this money to the corrupted person's account.

organisation's corporate plan. The bureaucratic role of the Ministry of Finance in financing certain activities based on the approved budget motivated bargaining for funds between enterprises and the MOF, and reduced interest in economic efficiency and the effectiveness of services or products provided (ibid). The lack of available information and low contribution of management accounting to quality information provision, scientific management and cost techniques, may be a result of inadequate qualifications, since management and finance accounting skills in some organisations were underdeveloped or virtually nonexistent; or the lack of integrated IT systems due to the inability to update current accounting systems (ibid).

Accounting can clearly play an essential role in providing information that enables better cost control and pricing decisions as well as better management of cash, inventory, accounts receivable, projects, and fixed assets (Pallot, 1998). However, the present examination and evaluation of current accounting practices in Saudi SOEs in general, and government budget-supported organisations in particular, shows that accounting systems have had little impact in providing adequate quality information which can be used for pricing, planning, and controlling day-to-day management and other managerial decisions (Al-Dehailan, 2004).

Due to the lack of adequate cost and managerial accounting systems and integrated information systems, the quality of information is insufficient to help decision makers draw a clear picture of the financial results of the various departments and activities of enterprises or achieve effective internal control (ibid).

3.6 Summary

This chapter aimed to explain the literature that related to management accounting control systems and the changes that occur in it due to the changes in ownership, particularly privatisation. The chapter started by defining the concepts and the framework of management accounting control systems. The literature related to the changes in the MACS and its relationship to privatisation was investigated.

Most of the literature in this chapter argued that privatisation would change the MACS in any organisation. However, there were other authors who questioned this argument, as they believe that privatisation alone would not change the MACS without changes in other elements, which are the external environment, organisational culture, and organisational structure.

The chapter described the aspects of the management accounting control systems and the elements of organisational context that were used as a basis for the investigation in this study. The literature showed that due to privatisation there would be changes in the ten aspects of management accounting control systems as follows:

- **Objectives setting and Strategy:** organisations would set their objectives on a commercial basis rather than on a social basis. Moreover, all management levels in all departments would participate in the process of setting objectives.
- **The Budgetary Process:** organisations would have autonomy in setting their budgets. In addition, budgets would be used as evaluation and control tools within organisations.
- **Incentive systems:** organisations would develop competitive reward systems based on fair evaluation systems of the employees' performance. In addition the organisations would become more concerned about staff development and training.
- **Accounting Systems:** the accounting system would provide qualitative and quantitative information and reports for internal control purposes, decision-making purposes, as well as placing more emphasis on fair presentation of the financial situation for investors.
- **Effectiveness (PMS) and Balanced Scorecard:** organisations would develop more sophisticated approaches to use performance indicators to measure performance at different levels in the organisation. These approaches would include both financial and non-financial indicators. An example for a comprehensive approach is the Balanced Scorecard.
- **Costing Systems:** organisations would use more sophisticated approaches (for example ABC) to manage costs effectively and to help the organisation in setting prices.

- **Organisational Structure:** structures would be clearer in terms of responsibility centres and they would be more focused on meeting customers' needs.
- **Organisational Culture:** organisations would make an effort to change their employees' culture towards the organisation by providing them with training programmes. These attempts would have an effect on the employees in terms of understanding their accountabilities, changing their views towards customers, and moving their mentalities from a bureaucratic mindset to a commercial mindset
- **External Environment:** the relationship between organisations and regulatory bodies would be clearer in terms of responsibilities and requirements, which would lessen government involvement in the organisation's policies. In addition, there would be changes in the kind of stakeholders, which would lead to changes in their relationship with the organisations, as their requirements would change. This would affect the kind of information that organisation has to provide based on each stakeholder's needs.

Chapter 4. Research Methodology and Methods

Introduction

Having discussed theoretical research issues, this chapter then describes and justifies the research methodology and data collection procedures used in undertaking the research.

It concludes by stating the specific objectives of the research in the light of discussions in previous chapters regarding privatisation in Saudi Arabia and changes on management control systems. It justifies the choice of the two companies in question and the use of the case study method as being the most appropriate for this particular research. Thus the structure of the chapter is as follows:

Section 1: General categories of research classification;

Section 2: Qualitative approach to research;

Section 3: The research design;

Section 4: Data collection types: primary and secondary including justification for use of the case study method.

Section 5: Data collection methods including Interview design, procedure and analysis of data.

4.1 Classification of Research Methods

Hussey and Hussey (2003) classify research into four categories, based on its purpose, process, logic and outcome. Table 4.1 Categories of Research shows these categories.

Table 4.1 Categories of Research

Type of Research	Basis of Classification
▪ Exploratory, descriptive, analytical or predictive	Purpose of research
▪ Quantitative or qualitative	Process of research
▪ Deductive or inductive	Logic of research

▪ Applied or basic	Outcome of research
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Source: Hussey and Hussey (2003)

Three types of research, described below, can be distinguished on the basis of their purpose.

1. Exploratory research examines possible reasons for a particular practice; it will be based on hypotheses that will be developed and then tested on a larger scales. This research is considered ‘open’, uses flexible data collection methods such as the case study technique, personal observation and historical analysis of secondary material, and involves the collection of a wide range of data (Hussey and Hussey, 2003). This approach is usually adopted where there is a paucity of literature in terms of previous studies. As a technique it is useful when ranking research questions in terms of priority and helps to gather early information on practical problems that may be encountered during the research (Aaker *et al.*, 1995).

2. Descriptive research is used extensively in social science studies (Aaker *et al.*, 1995). In a business context, it involves the description of the specific activities of a company or a group of companies. Descriptive research identifies and collects data on the characteristics of a particular problem, describes phenomena as they exist and examines problems at a deeper level than an exploratory study (Hussey and Hussey, 2003).

It fulfils at least four different purposes, viz.:

- Provides a clear picture of some aspect of the social environment;
- Describes the characteristics of certain research problems;
- Estimates the proportion of people in a specific population who behave in a certain way;
- Makes predictions.

3. Analytical research goes further than descriptive research by trying to explain how and why a certain problem exists. It looks for causal relationships among the variables identified in order to understand the phenomenon or problem that is being studied. (Hussey and Hussey, 2003).

This research can be classified as descriptive research for the following reasons: (1) it will provide a clear picture of MACS changes in Saudi privatised companies, (2) it will

examine other possible reasons for the changes in MACS, and (3) it will provide suggestions for governments undertaking future privatisations on how best to improve MACS within the privatised companies.

4.2 Research Approaches

Different methodologies can be used for collecting data from various sources. Data collected can be classified as qualitative when it consists of text describing situations, individuals or circumstances around a phenomenon, and quantitative when the information is in a numerical form (Huberman and Miles, 2002, Blaxter *et al.*, 2001).

Denzin and Lincoln (1994) claim that both qualitative and quantitative approaches to data collection can be used appropriately, irrespective of whether the research philosophy involved is positivist or interpretive.

Theoretically, the nature of the research problem dictates the choice of methods; in practice, however, constraints such as time and funding greatly influence the researcher's choice of methods. As this research will be qualitative in nature, point 4.2.1 explains the approach in depth and briefly highlights differences between qualitative and quantitative approaches.

4.2.1 Qualitative research

The term 'qualitative method' covers a range of interpretive techniques that seek to:

'Describe, decode, translate and otherwise come to terms with the meaning, not the frequency, of certain more or less naturally occurring phenomena in the social world' (Van Maanen, 1983).

It refers to a kind of data-gathering technique, which includes document reviewing, interviewing individuals and conducting focus groups and observing phenomena (Paton, 1980).

Morgan and Smircich (1980) argue that qualitative research is an approach rather than a particular set of techniques and that its usefulness and appropriateness depends on the nature of the research issue being studied.

Qualitative methods yield data which are “rich, full, earthy, holistic, ‘real’; their face validity seems unimpeachable; they preserve chronological flow where that is important, and suffer minimally from retrospective distortion... Furthermore, their collection requires minimal front-end instrumentation” (Miles, 1979, p.560).

Kirk and Miller (1986) assign the following steps to any qualitative approach to research: invention, discovery, interpretation and explanation. Similarly, Hignett and Wilson (2004) identify five key points which distinguish qualitative from quantitative methods: words and pictures, rather than numbers; few cases, many ‘variables’, instead of the reverse; sampling developed during study, rather than pre-assigned; iterative analysis; and reflexivity as to the role of the researcher.

Remenyi (1998) asserts that qualitative methodology reflects

a theoretical point of view that advocates the study of direct experience taken at face value; and which sees behaviour as determined by the phenomena of experience rather than by external, objective and physically described reality (P: 46).

With reference to a positivist tradition, qualitative projects largely serve the purpose of exploratory studies, which then lead into more structured or quantitative studies (Deshpande, 1983; Tashakkori and Teddlie, 1998).

Qualitative research is also often used as a first step in the design of structured interview surveys (Hakim, 2000).

The approach differs from quantitative research in its concern with interpreting meaning in textual rather than numerical data through the use of statistical methods. According to Hakim (2000), one of the greatest advantages of qualitative research is the validity it lends to the data, as they are normally collected in sufficient detail for the results to be taken as true, correct, complete and believable reports of participants’ views and experiences.

In spite of this, qualitative research suffers from a major drawback in the sense that the small number of participants who are usually involved may lead to concerns being raised about the representativeness of the sample (Hakim, 2000). Thus, qualitative research is concerned with the depth rather than the breadth of data.

Miles (1979, p.590) notes that

Qualitative data tend to overload the researcher badly at almost every point: The sheer range of phenomena to be observed, the recorded volume of notes, the time required for write-up, coding, and analysis can all be overwhelming. But the most serious and central difficulty in the use of qualitative data is that methods of analysis are not well formulated.

Qualitative research also suffers from the problem of subjectivity, as the chances that researcher him or herself could act as a measurement tool are increased as compared to quantitative research (Walter and Gall, 1989).

Several features define the nature and design of qualitative studies: taking a holistic approach in investigating a phenomenon; performing the study in a natural setting so as to make the conditions as close to reality as possible (Walter and Gall, 1989). This second feature has the benefit of allowing more flexibility and responsiveness to the 'multiple realities' that the researcher is faced with while investigating a complex field situation. A further feature is selecting the sample for observations purposively rather than randomly, which has the benefit of helping the researcher avoid missing samples that could be considered as 'outliers' under a random selection process.

Easterby-Smith *et al.* (2001) lists two basic ways to analyse qualitative data:

1. **Content analysis** involving studying the frequency of occurrence of key phrases in texts or interviews. Here, although the researcher may grasp the key concepts in the data, it will be difficult to understand the reasons for their occurrence.
2. **Grounded theory**, which recognises the difficulties involved with analysing large amounts of non-standard data produced by qualitative studies. Therefore, rather than imposing an external structure, research involving grounded theory derives its structure from the data (emergent themes and patterns), this structure is therefore grounded in concepts used by the social actors themselves.

Table 4.2 lists some of the differences between quantitative and qualitative approaches. However, Remenyi (1998) argues that since research into strategic issues merits the collection of data concerning 'how', 'why' and 'what', the two approaches can often be used complementarily. Furthermore, qualitative and quantitative methodologies are not opposites or divergent; rather, they are concerned with different dimensions of the same phenomenon. At times, these dimensions may appear to conflict with each other, but even in such cases, the underlying unity may become visible on further exploration.

Table 4.2 Qualitative vs. Quantitative Approaches

	Qualitative Approach	Quantitative Approach
Types of question	Probing	Limited probing
Sample size	Small	Large
Amount of information	Substantial	Varies
Requirements for administration	Interviewer with special skills	Interviewer with fewer skills
Type of analysis	Subjective, interpretive	Statistical, summation
Hardware	Audio recorders, projection devices, video recorders, pictures, discussion guides	Questionnaires, computers, printouts
Degree of reliability	Low	High

Source: McDaniel and Gates (2002)

Because of the nature of the information that was needed for this research a qualitative approach will be used. The research needed detailed information on the pre-privatisation and post-privatisation situation in Saudi Arabia, as well as the opinions of respondents, which can best be provided by a qualitative approach and would be difficult to obtain from questionnaires.

4.3 Research Design

This section describes the research design that was used to conduct this project, beginning with a review of the literature on the changes in management accounting control systems due to the changes in ownership status. Following the literature review, the research questions were framed and the case-study method was selected to investigate the research questions. Sequencing of data collection was done. Interviews were first conducted with selected top, middle and lower level of managers in the companies chosen for the case study. The qualitative data was analysed using content analysis.

4.3.1 Literature Review

The literature review examined previous research on the topic, which included research projects and bibliographic material relevant to the topic. The Literature Review chapter (chapter three) discusses the concepts of management accounting control systems and its framework. It also describes the components of management accounting control systems and the changes that occur when there is a change in the ownership of the organisation (i.e. privatisation). In addition it investigated the expected changes that might arise in the organisations under study in Saudi Arabia.

The research objectives emerged from the review of the management control systems literature and therefore were informed by previous research findings. A gap exists in the literature in terms of research carried out on management control systems changes in Saudi Arabian private companies.

4.3.2 Research Objectives

The aim is to study two newly privatised Saudi companies in depth. The objectives are as follows:

- 1 To investigate the nature of change in management accounting control systems in the two post-privatisation Saudi companies;
- 2 To determine the factors other than privatisation that led changes in the management accounting control systems in the selected companies;
- 3 To examine whether privatisation improve management accounting control systems or not;
- 4 To examine the impact of cultural, political and structural factors on the changes in the management accounting control systems of Saudi privatised companies;
- 5 Propose recommendations drawn from findings relating to Saudi privatised companies that might assist the government of Saudi Arabia when it privatises other organisation.

To address these objectives, the following research questions were developed:

1. What were the changes that appear in management accounting control systems in privatised Saudi companies?
2. What were the factors that affected the changes on the management accounting control systems other than privatisation?
3. Does privatisation improve management accounting control systems?

This is not intended to be a comparative study of the changes in management control systems in different countries, rather a comprehensive analysis of the changes in management control systems in two specific organisations, in one country, namely Saudi Arabia.

4.4 Data Collection

Two types of data are available to researchers: primary and secondary. Collection methods for each and their advantages and disadvantages are discussed below.

4.4.1 Primary Data

Primary data is that which is directly collected for the first time by the researcher from primary sources (Rummel and Ballaine, 1963).

Ghuri *et al.* (1995) argue that in cases where secondary data is not sufficient to answer research questions, primary data should be collected.

Methods of primary data collection include case studies, participant observation, interviews and questionnaires. Since the primary data technique used in this research is the case study, the following subsection explains in some detail the concept, advantages, and disadvantages of the case study method.

4.4.1.2 The Case Study Method

Over the past fifteen years, several writers identified a need for researchers to study accounting, and in particular management accounting, in its practical setting using case

study research (Otley, 1984; Scapens, 1990; Macintosh and Scapens, 1990, 1991; Scapens and Macintosh, 1996; Boland, 1993, 1996; Humphrey and Scapens, 1996).

Yin (2003) states that the case study method represents a comprehensive research strategy comprising particular techniques for collecting and analysing data. Case study research can cover a broad range of basic methods of data collection, include information from a wide variety of sources and increase the robustness of analysis of issues. Methods are used in a variety of ways by accounting researchers', for example, they are used to describe, illustrate, experiment, explore and explain most accounting and control issues.

However, the various uses of case studies rely on quite different theoretical and methodological perspectives (Scapens, 1990) and the particular use made of case study research methods will depend on the nature of the research questions, epistemological stance and methodological position of the researcher (Scapens, 1990; Otley and Berry, 1994; Nandan, 1997).

This particular study will take the form of an explanatory case study using an interpretive methodology. The two case studies in this thesis are used to explain the reasons for observed practices in a specific context rather than to produce generalizations.

Hussey and Hussey (1997) describe the case-study approach as an extensive investigation of a single instance of a phenomenon of interest. For Yin (2003), a case study represents an empirical inquiry that investigates a contemporary phenomenon within its real-life context and which is particularly appropriate where the boundaries between phenomenon and context are not very apparent. Thus, the best application of the case study method is when in the opinion of the researcher the context of the phenomenon being investigated has an effect on the phenomenon itself.

On the other hand, Stake (1995) argues that the case study is not a methodological choice, but rather a selection of what is to be studied. Yin (2003) lists the most important data sources for use in case studies as documentation, archival records, interviews, direct observation, participant observation and physical objects.

Table 4.3 list the strengths and weaknesses of each of these data sources, which researchers should consider. Most of the weaknesses can then be minimised through the use of triangulation.

Table 4.3 Strengths and Weaknesses of Six Sources of Evidence

Source of Evidence	Strengths	Weaknesses
Documentation	Stable– can be reviewed repeatedly. Unobtrusive– not carried out as a result of the case study. Exact– contains exact names, references and details of an event. Broad coverage– long time span covers many events and many settings.	Retrievability– can be low. Biased selectivity, if collection is incomplete. Reporting bias– reflects (unknown) bias of an author Access– may be deliberately blocked. Danger of false or unreliable documents.
Archival Records	(As above for documentation). Precise and quantitative.	(As above for documentation). Accessibility for reasons of confidentiality.
Interviews	Targeted – focuses directly on case study topic. Insightful– provides perceived casual inferences.	Response bias. Inaccuracies due to poor recall. Reflexivity– interviewee says what interviewer wants to hear.
Direct Observation	Reality– covers events in real time. Contextual– covers context of event.	Time consuming. Selectivity– unless broad coverage. Reflexivity– event may proceed differently because it is being observed. Cost– hours needed by human observers.
Participant Observation	(As above for direct observation). Insightful into interpersonal behaviour and motives.	(As above for direct observation). Bias due to investigator’s manipulation of events.
Physical Artefacts	Insightful into cultural features. Insightful into technical operations.	Selectivity. Availability.

Source: Adapted from Yin, 2003:86

Case studies offer the possibility of understanding the nature of accounting in practice both in terms of the techniques, procedures, systems and the way in which they are used. Using a qualitative case study approach, researchers are now beginning to shed light on the way in which accounting systems permeate organisational, social and political relationships. (Covaleski and Dirsmith, 1983, 1986, 1988; Macintosh and Scapens, 1990, 1991; Broadbent et al., 1991; Jones and Sefiane, 1992; Alam and Lawrence, 1994; Hoque and Hopper, 1994; Power and Laughlin, 1996; Boland, 1993, 1996; Scapens and Macintosh, 1996).

In conclusion, the case study approach results in the balancing of different methods as it gives the researcher the option to choose from multiple techniques of data collection.

4.4.1.2.1 Justification for Using the Case Study Method

A qualitative case study method has been adopted in this study for several reasons.

First, the case study offers the possibility of a more holistic understanding of the nature, context and process of change in management accounting control systems from the point of view of the participants. It deals directly with each individual case in its actual context (Bromley, 1986; Scapens, 1990).

At the same time, it carries implications about the extent to which the resulting analysis is applicable to other, similar cases. Thus, rather than working from the top down, i.e. from abstract theory to individual or particular case, the case method works from bottom up, from the analysis of particular case to the development of 'case law' (Al-Aiban, 1991).

Second, the lack of large-scale abstract and general concepts in social and behavioural sciences makes individual human beings and social organisations the relevant units of study.

Third, the case study enables a researcher to interact with what is being researched and the research environment itself, allowing for a better understanding of the context of the control.

Fourth, a case study offers the opportunity for one aspect of an area of interest to be studied in some depth within a limited time scale.

Finally, interesting issues emerging from the interpretation and analysis of study can be easily crosschecked with other materials in the case study. The information obtained will give a more accurate and representative picture than a single research method because case studies draw on data gathered by many methods (see table 4.3).

Although this study focuses on only two organizations, the results are not intended to be used as a basis for generalization. In other words, this study has not been conducted with generalization in mind.

The aim is to describe and explain, in a rich and detailed manner, how and where changes occurred in management accounting control systems and what their

consequences were for organizations and members. The explanations offered are neither designed to test any priori assumptions nor sought to establish causal relationships.

The choice of factors, events and data for analysis, although no doubt coloured by the researcher's own judgement, have been vouched for in this study and kept in check in a number of ways (e.g. multiple sources of data). The process of using multiple methods and sources of collecting data in order to provide evidence on a particular issue is known as 'triangulation' (Ryan et al., 1992).

Triangulation dictates that different methods and resources are integrated when drawing conclusions. Thus the individual strengths and weaknesses of the various methods are identified and applied in such a way that all strengths and weaknesses counterbalance each other.

Triangulation can therefore be seen as a strategy that aims to overcome problems of validity and bias. It serves two main purposes, viz., confirmation (Denzin, 1970) and completeness (Jick, 1983). To further ensure the validity and reliability of this study, the researcher adopted the following strategies.

First, the researcher spent an adequate amount of time in the research setting, established an adequate relationship with the participants and used both examination of documents and interview techniques.

Second, the researcher used a tape recorder to record the interviews to produce transcripts, which allowed a good degree of assurance and reliability.

Third, the researcher took notes while the interviews were in progress. This reduced the chance of losing data should mechanical fault arise and allowed close attention to be paid to interesting topics.

4.4.1.2.2 Reasons for selecting the two Saudi privatised companies

This research is conducted in two Saudi privatised companies namely Saudi Telecom Company (STC) and Saudi Electricity Company (SEC). These two companies were selected for several reasons. These reasons are:

1. They are the first companies that have been privatised in Saudi Arabia. Both of the companies were privatised on the same time. The time since these two

companies were privatised until conducting this research is enough to reveal the affects in MACS in both companies therefore the changes would be noticeable.

2. Both of the companies still have employees who worked in the companies before privatisation. Subsequently, those employees can describe the situation before privatisation and identify the changes clearly.
3. The researcher has personal and friendship communication in both companies. These relationships can help in obtaining more and clearer information.

4.4.2 Secondary Data

Secondary data has been defined as having been gathered previously and for purposes other than the requirements of the current research. An alternative definition is “published information which has been collected for some information need” (Stewart and Kamins, 1993). Secondary data are mostly historical, and do not require access to respondents or subjects. The major sources of such data are books, periodicals, governmental and official publications, theses, dissertations and other similar sources. The defining distinction between primary and secondary data is that the person who finally draws conclusions from the latter is not the one who collected it (Stewart and Kamins, 1993; Rummel and Ballaine, 1963). As a consequence, secondary data have the disadvantage that they were not designed specifically for the needs of the current research. Therefore, it is imperative that the researcher test secondary data for accuracy, bias and soundness (Zikmund, 2000).

Saunders *et al.* (1997) classify secondary data in three categories:

- a) Documentary secondary data, including written documents such as reports, minutes, transcripts of speeches, books and journals, and unwritten documents, including films, pictures, drawings and video recordings;
- b) Survey-based secondary data, which has been collected for other purposes by other researchers; and
- c) Multiple-source secondary data, which comprises a combination of types a) and b) before the researcher uses them.

Saunders *et al.* (1997) contend that secondary data are largely used in the case study and survey types of research, but have also been used in experimental studies.

Churchill (1995) advocates that researchers should start with secondary data, and only when such data are not sufficient for the purposes of the research should they look for primary data.

Use of secondary data can save much time and money (Churchill, 1995; Ghauri *et al.*, 1995) and can help researchers compare different research methods in order to select the most appropriate approach to collecting primary data (Ghauri *et al.*, 1995).

4.4.2.1 Reasons for using secondary data

Researchers are increasingly dependent on the use of secondary data. Nachmias and Nachmias (2002) list three basic explanations for this:

(1) Conceptual-substantive reasons

In some subjects and fields of research, and for some research problems, e.g. those involving political and historical issues, the only data available for researchers may be secondary. Such data can assist researchers to gain a better grasp of the historical context of the research problem by analysing data collected earlier on similar issues. Secondary data may also be used for comparative purposes.

Hyman (1987, p.17) believes that

Secondary analysis of a series of comparable surveys from different points in time provides one of the rare avenues for the empirical description of long-term changes and for examining the way phenomena varies under the contrasted conditions operative in one [or several] society [ies] at several points.

(2) Methodological reasons

Secondary data is also popular because of the methodological advantages provided.

These are:

1. Reliable and accurate secondary data provide opportunities for *replication*, which means that the current research can appear in a number of future studies, giving it more credibility;
2. It is possible to use longitudinal research designs, as the data can often be available over a period of time;
3. Secondary analysis may enhance the measurement by expanding the scope of independent variables used in the operationalisation of concepts;

4. It enables the researcher to increase sample size and the number of observations, leading to more encompassing generalisations.

(3) Economic reasons

A third reason for the increasing dependency on secondary data it is less expensive than primary data.

4.4.2.2 Disadvantages of using secondary data

The major disadvantage of secondary is that, at best, it will only be an approximation to the kind of data the researcher would like to employ in testing hypotheses (Nachmias and Nachmias, 2002).

There is bound to be a considerable difference between primary data collected personally by the researcher with specific research purposes and intentions in mind, and the data others have collected for other purposes.

A further problem with secondary data is the issue of access. Researchers might face difficulties in finding data related to the research problem, which might be inaccessible because the original researcher has not put them in the public domain. It is not mandatory for researchers to make their data available for secondary users.

Finally, if the researcher lacks information on how the data was collected in the first place, it may to some extent compromise secondary data analysis, as this information is important in determining any potential source of error or bias and any problems with internal or external validity (Nachmias and Nachmias, 2002).

Whatever type of data is collected and whatever method is used, issues of validity and reliability arise and those related to the research in question are discussed below.

4.5 Data Collection Methods:

Data was collected in this study through a combination of interviews and documentary evidence. Several data collection methods were used in an attempt to reduce the risk of the researcher missing important data that might be relevant for analysis. In fact, these multiple methods enabled the researcher to collect far more data than could be used. To ensure that data collection was properly carried out, regular contact and constant

discussions with the supervisor were maintained throughout this study. Such close supervision ensured that the focus was maintained within the framework agreed at the outset.

The process of data collection was organised and conducted in two stages: interviews and organisations' documentation. The interview stage entailed a series of intensive semi-structured interviews. The sources of the second stage included a review of organisations' documentary evidence. Although organisational documentary evidence was collected and used in the analysis and discussion of the issues that arose in this study, the focus of the study was essentially on the interviews. The following is an outline of the interview objectives, design and procedures.

4.5.1 Semi-structured Interviews:

One of the most important sources of case study information is the interview (Yin, 2003). An interview can be defined as a face-face verbal interaction between two people where one of the persons involved, the interviewer, asks the other person, the interviewee, questions so as to gather information on his/her opinion or beliefs in his/her fields (Alsbab, 1990).

Many studies have suggested that personal interviews are the best method to gather information, although information on facts and certain opinions can also be obtained through other means, such as by post, email or telephone. However, some information can be obtained only in one-to-one interviews, particularly if the interviewee is an academic (Campbell, 1980).

Interviews, in general, are more strenuous than other approaches in terms of gathering data and analysing the results. Arranging interviews with people can also be difficult if they hold positions of importance, e.g. decision-makers in either governmental or private organisations (Hibberd and Bennett, 1990).

Interviews can be used in a number of ways: as the main vehicle of research, merely as an exploratory device that identifies variables and relations, to suggest hypotheses and guide research, or as a supplement to other methods of research. In the course of this study, interviews were used as the vehicle of the research.

The interviews in question were conducted with employees who played an important role in the control systems. The major objective was to provide a description and an

analysis of the control systems and the perceptions of the major control systems participants.

Interviews were designed to explore the real worlds of the interviewees to enable the researcher to gain insights into how they saw the main issues of this study, i.e. influences and consequences of privatisation on management accounting control systems, impact on members' behaviour and the impacts of external and internal factors in the control systems (Yin, 2003).

The process of conceptualising and conducting qualitative research interviews can be divided into four steps: defining the research question, creating the interview guide, recruiting participants and carrying out the interviews (Symon and Cassel 1998).

Bottlett (1987) lists a number of factors which can influence the quality of the interview: the selection of people who will participate in the interview, making all the adequate and necessary preparations for the interview, having a pre-planned design for the interviews and the questions, carrying out a dry run before the interview, ensuring the reliability of the information obtained, recording the interview, recognising the necessity that the researcher should have background information on the interviewees and having an understanding of the goal of each question.

4.5.1.1 Advantages of Interviews:

Semi-structured interviews were particularly appropriate for this thesis because they gave those interviewed the opportunity to discuss the issues in a way they could control. Arksey and Knight (1999: 81), argue that the significance of interviews is evident:

... When we need to ask numerous open-ended questions, or open-ended probes, such open-ended questions are important in allowing the respondents to say what they think and to do so with greater richness and spontaneity.

At the same time, interviews maintain control over the order of sequence in which the questions are answered and they provide a sense of focus on the reflected verbalised thoughts of the interview subjects, thereby providing valuable insights into the subjective understanding of the individuals' life worlds (Stone and Holland, 1996).

The interview method provides opportunity for follow-up and enables the interviewer to clarify and answer questions in cases where difficulties in understanding what is meant

by a particular question are encountered by the interviewees. An interview clarifies the world of beliefs and meaning of participants rather than their actions because what people claim to think, feel or do does not always agree with what they actually do.

Interviews have the advantage of high response rates when compared with other techniques as a result of the interaction between the interviewer and the interviewee. The response rate can be as high as 95% (Nachmias, and Nachmias 2002) and general population samples tend to produce this rate (De Vaus, 1996; Oppenheim, 1992).

Interviews are considered to be the most appropriate method of data collection, as it makes it possible to check accuracy, as well as to verify and/or refute the data obtained through dialogue and observations (Kerlinger, 1973).

Finally, Fraenkel and Wallen (1993) re-emphasise that the main advantage of conducting face-to-face interviews is that it makes direct contact with respondents possible.

In-depth interviewing is a method involving intensive one-one interviews with a small sample of respondents in order to understand and explore their perspectives on a particular idea or situation. One of its major advantages is that the interviewer is able to gather much more detailed information than can be obtained from other data collection methods, such as surveys. It provides the interviewer with the opportunity to introduce a particular topic if it has come up during the discussion. The interviewer should allow the discussion to flow as naturally as possible since some topics are bound to arise without being explicitly raised by the interviewer.

Furthermore, interviews provide access to many different groups of people and therefore much varied information, so clarification of words and concepts are easily accomplished. An interview is a more effective and visible method and can be easily combined with case study material. It also allows for detailed exploration of the important 'how' and 'why' questions (Yin, 2003). Interestingly, the interviews in this study allowed for the examination of actual relations between various control elements and the level and types of involvement that each had in the control systems.

It should be noted that postal questionnaires were not used in this study because of limited contacts between researcher and the researched. A survey method would not have permitted an in-depth investigation of control systems nor would it have enabled explanations of observed control processes.

In addition it would not have given any opportunity to clarify questions or overcome any unwillingness on the part of participants to answer particular questions. It is important to note here that a postal survey or questionnaire would have been open to misinterpretation of questions as well as the possibility of non-cooperation in completing it. In addition, there was no guarantee as to who had completed them.

Low response rates, particularly when respondents have no special interest in the subject of the questionnaire is another problem, as is a lack of opportunity to follow through a particular reply (which is possible in an interview) and the difficulty in adequately establishing casual connections between the different variables (DeVaus, 1996) when analysing the collected data.

Furthermore, postal questionnaires ignore the historical, political and socially constituted nature of control systems because of its grounding in rationalist thinking (Preston, 1991). This ignores the individual as an active agent involved in constructing and shaping control systems in organisations (Tsamenyi, 1997).

Criticising survey research, DeVaus (1996: 7) has argued that:

Surveys just look at particular aspects of people's beliefs and actions without looking at the context in which they occur. Taken out of context it is easy to misunderstand the meaning of behaviour.

He further argues that:

Surveys seem to assume that human action is determined by external forces and neglect the role of human consciousness, goals, intentions and values as important sources of action. (Ibid, p.8)

Any research must take people's beliefs, values and goals, which motivate behaviour into account "when developing and evaluating why people behave and think as they do" (ibid, p.8)

Furthermore, ethnographic methods such as direct observation and longitudinal study, which have the advantages of spending more time on the research sites and repeating data collections over a long period over interviews, were not suitable for this study. Both methods are time-consuming and more importantly require resources that were not available to the researcher.

Direct observation is difficult in the sense that the researcher cannot be at the place of an incident because he/she does not know where and when it will occur and even if the occurrence of the instance is known, the presence of the researcher may interfere with it (Gummesson, 2000).

Longitudinal studies are also difficult in the sense the researchers find it very hard to get funding to complete them, as in the case of this study (Hakim, 2000). A further disadvantage that is specific to longitudinal case studies is that the analysis of data from a longitudinal study is substantially more complex than other equivalent analysis of other methods because they involve large data files (Hakim, 2000).

A further drawback of both these methods is the possibility of the researcher being captured by the organisation as he/she is trying to create a more personalised relationship with study members to promote their active interest in the study.

4.5.1.2 Disadvantages of Interviewing:

The disadvantages of using interviews are to some extent a reflection of their advantages. Primarily, interviews are much more expensive than postal questionnaires, travel costs and call-backs being examples of some of their expenses.

Another disadvantage is the amount of time needed at the data processing stage. Coding, i.e. classification of data collected and briefing are examples of the time consumption problem (Ryan et al., 1992). In using interviewing as a mechanism of studying social phenomenon possible bias is another limitation. This is likely to occur as a result of some motivation on the part of the respondent or interviewer or both to falsify information (Al-Aiban, 1991). While recognising these limitations, interview research is still considered to be a better approach in explaining and exploring control systems in its actual organisational context.

4.5.1.3 Design of Interview Questions:

Semi-structured interview questions were developed for this study (see Appendix A)¹⁴. These questions were used only as a basic guideline during the interview to ensure that all relevant topics were covered, to provide a direction for questioning and to help the

¹⁴ Questions were prepared initially in English and were then were translated to Arabic since English was not the first language of the participants. Hence, the interviews were conducted in Arabic, (see Appendix A), transcribed in Arabic and then translated into English to be used in the analysis.

researcher conduct the interview in a systematic and comprehensive fashion (Berry, 1976; Otley, 1976; Patton, 1987; Murshed, 1989; Hoque, 1993).

In most cases, supplementary questions were asked, particularly when initial responses needed further elaboration or when new issues emerged in the course of discussions. Questions were redrafted to suit a particular manager or accountant and special circumstances, or when the original questions were unclear and/or interviewees misinterpreted them.

It could be said that the questions were in a continuous state of refinement as interviews progressed. Therefore, it is more accurate to describe the interviews as discussions designed to achieve understanding of managers' and accountants' views and opinions on the issues rose. They allowed participants to express their views about the different aspect of their respective organisations and control systems. All interviewees had to see the questions before interviews were conducted.

The interview questions were divided into five sections. In the first section, interviewees were asked general introductory questions about their time in the organisation, the position they held and their experiences.

In the second section the interviewees were asked about the external environment, which included regulatory bodies and the Government, and its impact on management accounting control systems. This section sought their personal views, opinions and perceptions of the external environment and control systems based on their own experience during the time they had been working for the organisation.

The third section focused on the changes in organisational structures that had taken place in the two organisations since privatisation. This section asked the interviewees about their experience of the impact of the changes of the structures on the control systems.

The fourth section asked the interviewees about the changes in organisational culture. It sought their personal views on the effect on management accounting control systems.

The final section had specific questions for accountants. This section asked participants about changes that occurred in accounting information techniques and budgetary processes as control tools.

4.5.1.4 Interview Procedure:

As indicated earlier, data collection for the study relies largely on field interviews, which were conducted between early October, and end of December 2007. Although the original period of time for the study was 3 months, the two organisations in question allowed further calls and personal checks, which led to an extension.

Initially, access was arranged in advance with the management of the two organisations. A letter explaining the objectives of the study and the possible involvement of employees was sent to the two organisations. This was followed up by telephone calls to each organisation, during these calls the researcher was able to discuss the reasons for and objectives of the research and the need to conduct the interview.

As a result, permission to continue with the research was received from the Managing Director and Director General in the two organisations and allowed the researcher access to all relevant material and documents during the course of the study. This also enabled informal discussions with employees and managers to be held in order to solicit their views, perceptions and impressions about management control systems and privatisation.

Twenty-five people from the two organisations were identified and chosen for interviews (see Table 4.4, and Table 4.5). It was felt that a larger number of interviews were both impractical and unnecessary due to the likely redundancy in the later interviews. The general consensus in the two organisations was to involve only managers and employees directly involved in management control systems that were there before privatisation since other managers and employees would have little or no knowledge of the management accounting control process.

Almost all related managers and employees in the two organisations were interviewed. The extent of coverage was intended to make the research more representative of the two organisations.

Interviews were conducted during on-site visits, times varying in length from half an hour to two and a half hours. Every interview started with a statement of the importance and objectives of the study. The main purpose of this statement was to eliminate any doubts the interviewees might have about the purpose of the research, to assure interviewees of the confidentiality of information provided and to emphasise the importance placed on the view of the respondents regarding their perceptions and attitudes towards control systems and the impact of privatisation.

Table 4.4 Numbers and Description of Interviewees in STC

<i>NO</i>	<i>Description</i>	<i>Refer to as</i>	<i>Experience</i>
1	Director of Corporate Performance.	Interviewee 1	He has worked for the company since 1994. He worked in the budgets department; then he was in the team, which changed the accounting systems from governmental to commercial systems. He was the head of the BSC team.
2	Financial Control Professional.	Interviewee 2	He has worked in the company since 2003. He worked in different companies before. He has a BA in finance.
3	Senior Analyst, Corporate Care.	Interviewee 3	He has worked in the company since 2001. He has an MSc in finance.
4	ABC revenue Analysis Manager, ABC Cost Accounting.	Interviewee 4	He has worked in the company since 2002. He worked first as an income analyst. Then he became the Director of the Income Analysis department.
5	Director, Regulatory Studies & Support, Regulatory Affairs.	Interviewee 5	He worked in the company from 1984-1994; then he came back from 2004-date. He was in the Planning Department. Then he was the Director of the Engineering and Planning Department. When he came back he became the Director of Regulatory Studies & Support.
6	Head Business Development Office, Senior Advisor-Organization.	Interviewee 6	He has worked in the company since 2002. He has an MBA and a PhD in business administration. He has an extensive academic experience
7	Strategic Planning Director, Strategic Planning.	Interviewee 7	He is an LSE graduate. He has worked in the company since 2000. He used to work for the Central Bank. He worked in Strategic Planning. and has been the Director of the Strategic Planning Department since 2004.
8	Financial Reporting Director.	Interviewee 8	He has worked in the company since 2000. He worked in the Credit & Collection Department for 4 years. Then he moved to the Financial Reporting Department.
9	Director, Financial Control.	Interviewee 9	He has worked in the company since 2001. He has an MSc in accounting. He worked in different companies for 15 years before he came to STC.
10	Outside Network Section Manager, Regulatory Affairs.	Interviewee 10	He has worked in the company since 1998.
11	General Manager of Accounting.	Interviewee 11	He has worked in the company for 22 years. He worked first in the Income Department. Then he went to USA to do

			his MSc and PhD. He came back before privatization. He was the head of the team, which was responsible for transferring the accounts from the Ministry of Finance to the company. After the company was established, he became the Director of the Cost Accounting Department for 4 years, and then he became the General Manager of Accounting.
12	Director, Budgeting, General. Admin. Financial Planning & Budgeting.	Interviewee 12	He has worked in the company for 20 years. He worked in the Planning Department. Then after privatization he worked in the Financial Planning & Budgeting Department and now he is the Director of the Department.
13	Director, Credits accounts, General. Admin. Accounting.	Interviewee 13	He has worked in the company since 1991. He worked as an accountant. Then he worked in the Budget Department. After privatization he continue to work in the Budgeting Department. Then he moved to work in the Alzakah (tax) Department.
14	Head of Financial Affairs	Interviewee 14	He has worked in the company since 2001. He has an MSc from the USA. He has extensive experience in different companies and accounting firms.
15	Accountant, Budgeting Department.	Interviewee 15	He has worked in the company since 2001. He has a BA in accounting. He worked in different companies before joining STC.
16	Accountant.	Interviewee 16	He has worked in the company since 2003. He has a BA in accounting. He worked in different companies before joining STC.
17	Director of HR Development Department.	Interviewee 17	He worked in the company from 1984-1994. Then he went to USA to do his MA and PhD in HR management. He came back to the company in 2002. He has worked in the HR Development Department since 2002.

Table 4.5 Numbers and Description of Interviewees in SEC

No	Description	Refer to as	Experience
1	Executive Vice President & CFO	Interviewee A	He has worked in the company since 2004. He had huge experience in different companies before he joined SEC
2	Director, Accounting Department	Interviewee B	He has worked in the company for 27 years. He started as an accountant. He worked in different departments before he become the Director of the Accounting Department.
3	Director, Management Accounting Department.	Interviewee C	He has worked in the company since 1982. He was sent by the company to finish his

			MA and MSc in accounting in the USA.
4	General Manager, Finance Department.	Interviewee D	He has worked in the company for more than 15 years. He has a BA in accounting.
5	Director, Financial Reporting Department	Interviewee E	He has worked in the company since 2001. He has a BA in finance. He worked in different accounting and finance firms before joining SEC.
6	Accountant.	Interviewee F	He has worked in the company since 2000. He has a BA in accounting. He worked in different companies before joining SEC.
7	Accountant.	Interviewee G	He has worked in the company since 2000. He has an MSc in accounting. He worked in different companies before joining SEC.
8	Executive Director of HR Development Department	Interviewee H	He has worked in the company since 2004. He has an MBA from USA. He has extensive experience working in different companies before joining SEC.
9	An engineering	Interviewee I	He has worked in the company for 23 years. He was in different places and different cities around Saudi Arabia.

During the interviews questions introduced by the researcher led to discussion. In the preliminary stages of the fieldwork, discussions were held with a number of accountants in the two organisations to obtain a broader view of the existing accounting and control systems. From these discussions, a short report on the background of the industry, Government, market and the two organisations under scrutiny and detailed descriptions about the mechanics of the management accounting and control systems was prepared. Every possible precaution was taken to ensure that descriptions and facts about the organisations and their control systems were error-free. A transcription of each interview was produced and submitted to every interviewee for confirmation of the facts.

The interviews were tape-recorded and notes of selected key issues were also taken at meetings in order to help the discussion. It is commonly accepted that tape-recorded interviews have both advantages and disadvantages. It allows everything to be documented and permits the interviewer to be more attentive to the interviewee and may also increase rapport between interviewer and interviewee (Hoque, 1993).

However, during an interview a tape-recorder may lead to biased responses when interviewees are commenting on confidential or sensitive issues. It was expected that when it was possible to use tape-recorders reliance on notes would be minimised and

the researcher would be free to concentrate on responses. Otherwise, notes were taken when confidential information was revealed and discussed. Also, it was found useful to take notes of selected key issues to achieve several objectives: firstly, to help formulate new questions during the interviews when participants showed special interest in certain areas; secondly, to help review the discussion when replaying the tape for writing the manuscript text; finally, to allow the researcher to be aware of the documentary evidence deemed relevant during the interview and to serve as an aid in the collection of those documents.

4.5.2 Documentary Evidence:

As indicated earlier, the purpose of collecting documents was to understand the historical development of each organisation and to examine accounting and control systems. Historical data proved to be very useful in revealing regulatory, social, political and economic forces. The researcher believes that past events were useful in understanding changes in social, political and economic situations in Saudi Arabia. Because the research is both a theoretical and empirical analytical study, it made full use of official documents to collect evidence.

Examples of these documents are:

1. Government documents, annual reports, press releases, media reports, corporate plans, financial plans, production plans and internal memos;
2. Published and unpublished journal articles, books and newspapers;
3. Internal forms, archival records, paperwork and progress reports.

Documents relating to the two organisations were collected during on-site visits. In cases where documents were not of immediate use or where the organisations had multiple copies, permission was obtained for the researcher to keep a copy. Although some documents were returned at the end of the study, permission was obtained to take notes.

These notes were combined with the other sources to analyse the data. The documentary stage continued to the last stages of the thesis to constantly modify and review the theoretical chapters using new material available in the area of the research focus.

4.6 Summary

This chapter has reviewed and discussed the research design and methodology issues that researchers need to deal with. Additionally, it has attempted to explain briefly the features of qualitative research and to justify the adoption this approach, using interview and documentary approaches in the collection and analysis of the data. Saudi Telecom Company (STC) and Saudi Electricity Company (SEC), as Saudi privatised companies, were the case study for understanding the changes in MACS because of privatisation. In-depth interviews with different levels of managers in both companies were conducted to provide data on their experiences and ideas concerning these particular issues. Documents from both companies were collected in order to achieve triangulation. This allowed a richness of data and a comprehensive treatment of the changes on MACS in both companies to explore the effect of privatisation and provide other factors that might change MACS rather than privatisation.

Chapter five will deal with the analysis of the qualitative data obtained from interviews and documents.

Chapter Five: The Changes in Management Control Systems after Privatisation

Introduction:

The aim of this chapter is to examine the changes that happened in the organisations under study after privatisation and is based on the findings from interviews and supporting documents that have been collected from the two companies.

The chapter is divided into two main parts. The first part explains the changes made to STC's management accounting control systems. These changes will be discussed in the following sections: planning and budgeting, Balanced Scorecard (BSC), ABC and costing systems, accounting policies and accountability, reporting systems, performance evaluation, relation to external environment, HR and reward systems, changes in organisational structure, and changes in culture. The second part of this chapter is going to illustrate the changes to SEC's management accounting control systems using the same sections as for STC. The last section will summarise the main changes that have taken place, highlighting similarities and differences between the two companies.

The discussion of the results includes quotes from interview respondents. As all of the interviewees wished to remain anonymous due to the sensitivity of the issues explored, they are referred to by number or letter, as shown in Table 4.4 and Table 4.5, which indicates roles and places in the hierarchy. All the interviews were conducted in the Arabic language, and subsequently translated into English by the researcher.

5.1 Changes to STC's management accounting control systems:

As a result of privatisation, the aspects of the management accounting control systems had been changed. These changes will be explored in the following sections.

5.1.1 Changes in Planning:

As most of interviewees mentioned, before privatisation STC was a state owned company whose objectives and strategies were based on Government plans. The Saudi Government viewed telecommunications as a public service - and non-profit making obligation that had to be provided.

The company at that time had no strategic vision apart from following Government orders. As one of the interviewees stated:

Before privatisation we only had one goal, which was to provide the service as instructed by the government regardless of the revenue that we could make or the losses we could incur. At that time we undertook lots of projects without even asking about the cost or the profit. We used to have orders from the Ministry to undertake a project: the cost of it would be stated but of course we didn't know anything about the profit. The system basically was: this is the money; spend it on this and this and this. As employees, we had no company goals, departmental goals or even personal goals. (Interviewee 11)

Before privatisation STC suffered from financial inefficiency due to having a multiplicity of projects and objectives. Many of these were not profitable, for example providing services to *unprofitable areas*, or engaging and sponsoring certain social events that were of no benefit to the company.

The majority of senior managers at STC gave reasonable justification for this, which was that usually STC received grants from the Government to continue services viewed as socially desirable. Thus the organisation provided services it would otherwise carry out differently if run on a purely commercial basis. Often they hired extra staff to fulfil their obligations, or set up a plant or provided services in a particular area to promote regional development.

Once competitors entered the market the Government ceased its involvement in this area, which gave STC more autonomy in setting its objectives and controlling its resources and spending. Thus after privatisation, STC started to set its own goals and objectives.

While conducting the field study at STC, the researcher observed that in every corner of the company's headquarters there was a notice setting out seven main objectives that the company wanted to achieve. Whilst the notice was in Arabic the English acronym for what it summarised – FORWARD - was also displayed. This is described as follows:

- F** Fulfil Mobile Potential
- O** Offer Wholesale Services
- R** Re-invent Home Communication
- W** Win Enterprise Customers
- A** Achieve External Growth
- R** Re-organise Internal Structure
- D** Derive Operational Efficiencies

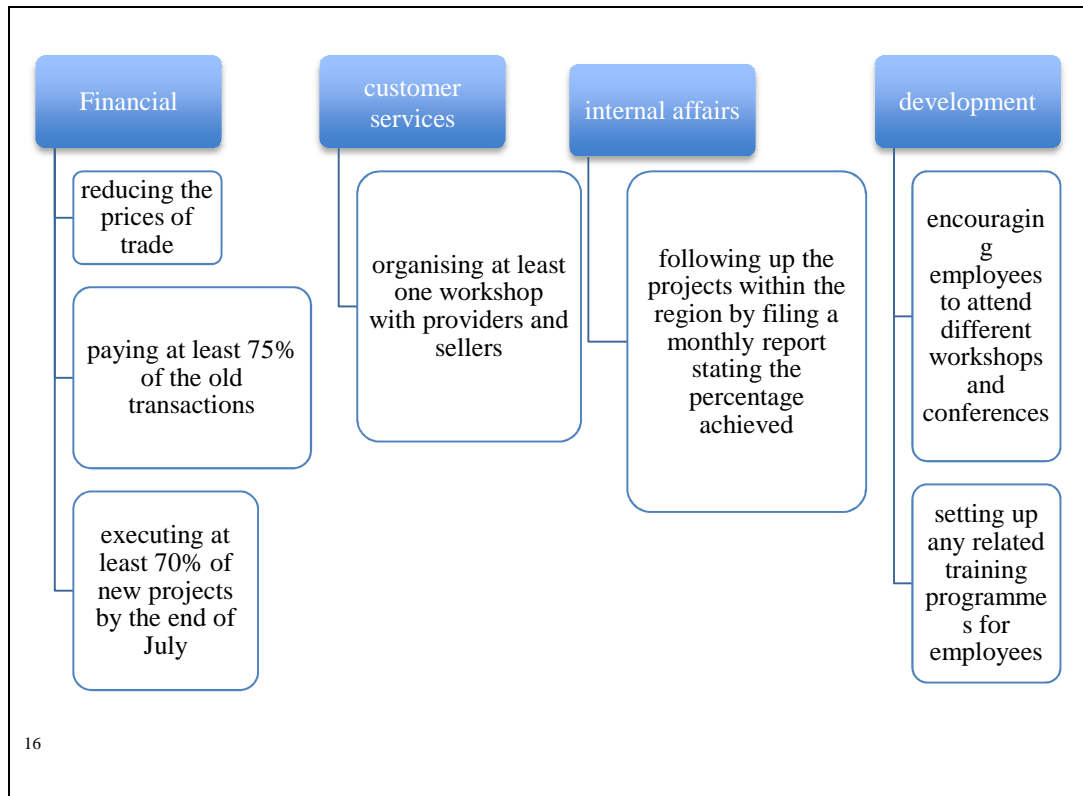
When the company established the FORWARD objectives, it tried to make sure that all employees at all levels understood it by organising workshops at all levels within the company and in all regions of Saudi Arabia. One of the directors stated:

Establishing objectives was a crucial requirement of the planning process. The major challenge for the top managers at that time was to make sure that the objectives of the company were clear and understood by all employees. We had to spend lots of money to organise workshops all over the company and everywhere in Saudi just to make sure that all employees understood what exactly the company wanted. (Interviewee 6)

Based on these clear objectives STC started to set clear plans for its operations. The company has 11 main departments: the Board of Directors is responsible for setting main goals for these departments. Thus plans were set by top managers and subsequently cascaded to lower levels of management. The President and the Heads of Department held meetings to break down the main goals that had been set by the Board of Directors. These goals were both financial and non-financial. For example¹⁵, the goals of the Director of Procurement in 2007 had four main categories, which were: financial, customer services, internal affairs and development, and each category had several detailed goals (see Figure 5.1). Since privatisation, STC has changed its objectives several times and subsequently made changes to its organisational structure (see section 5.2.9).

¹⁵ This example is based on a classified document that the research has collected from STC.

Figure 5.1 Goals of Director of Procurement in 2007



Source: Classified Documents from STC

It is clear from the above that the company has full autonomy in setting its goals and objectives. This autonomy has also affected the company's ability to set its own service prices: the situation now is that STC has the freedom to set prices, but has to have the approval of the Telecommunications Agency before applying them, thus preventing the development of a monopoly.

Since STC has been private I don't ever recall the Telecommunication Agency refusing the prices we have set. We always make sure that our prices are competitive and within the reach of the majority of people (our customers) (Interviewee, 1).

¹⁶ The usual situation with project payments: the company does not pay right after the project is ready, but they take some time or pay in instalments. Therefore, one of the goals of the Director of Production in 2007 is paying 75% of the old payments. Also another goal of the Director is leading negotiations for reducing the price of any supplies they need for any kind of trade through this department.

5.1.2 The budgetary process at STC:

Before privatisation, budgetary control at STC could be described as a primitive control system (Al-Dehailan, 2004). Budgets and the processes of budgeting were important only insofar as they provided management with an estimate of the total amount or volume of cash available, but were not used as tools that could be used to plan how the monies allocated were going to be spent.

In other words, budgets were originated based on the need to oversee rather than to control or direct spending. The planning and controlling processes were centralised at the Ministry of Telecommunications and the Ministry of Finance. Both Ministries developed them into the final budget, which was part of the government budget *by gathering information* related to the draft budgets (interviewees 1, 11, 12 and 13). There were no formal discussions or consultations with the departmental managers or the company's top managers. In fact company managers did not have any input into the budget whatsoever. Hence, when the budget was prepared, no consideration had been given to the impact on any part of the company, even though figures written into the sales budget, for instance, would have clear repercussions for production, materials, finance and other budgets. One of the interviewees who worked at the company before privatisation states that:

When we were under the government, we were just responsible for spending the money. We spent the money based on the Ministry's instructions... We did not have any contribution to preparing the budget.... even the projects; we were merely told to execute certain projects regardless of their benefits to the company. (Interviewee 13)

The above statement shows that the government was only concerned with allocating cash.

As a result of privatisation, the budgeting system was established. The new process has clear guidelines outlining each Head of Department's tasks, authority and responsibility at each stage. Nevertheless, it still took the company several years to come up with clear guidelines. The guidelines were made to assist the company in achieving its strategic goals, therefore they were

Subject to changes based on the changes on the company structures and Strategic goals (interviewee 12)

The guidelines were finalised in 2003. Details of the budgetary process will be discussed in the following subsections.

5.1.2.1 Preliminary Stage

The fieldwork investigation revealed that the first actual step in the formulation of STC's budget is the preparation of the budget circular. An Executive Committee that meets to discuss and set a time frame for the following year's budget development prepares the circular. Members of the committee include the President, Vice President, Directors of the Finance, Corporate Strategy, Personnel, Home and Enterprise Departments together with the Chief Accountant. During this meeting, the Committee decides on what to include in the circular. It will usually contain a summary of the financial conditions, budget timetable, growth rate, cost savings and the responsibility of each Head of Department based on the company's key goals and strategic aims.

The circular is then distributed by the Director of the Finance to all Departmental Heads to develop their own individual budgets. Heads of Departments have to inform employees under their supervision about the instructions for budget preparation and monitor their work. All departments are required to adhere to what is in the circular. (Interviewees, 11, 12, 13)

5.1.2.2 Preparation stage:

After receiving the circular a preliminary meeting is held between the President, Chief Accountant, five Department Heads: Personnel, Home, Enterprise, Network and IT, and sometimes other Heads of Departments. The purpose of this meeting is to set preliminary expectations for the proposed budget and emphasise the need for co-ordination across departments so that all parties are working on compatible plans. The IT and the Network Departments are advised to work in a co-operative manner with the three other main Departments (Personnel, Home, Enterprise) in developing the quantitative budgets since their budgets impact on each other and the rest of the company.

The Chief Accountant is the one who is responsible for co-ordinating the whole budget effort between the various Departments, especially Personnel, Home and Enterprise. After the preliminary meeting or meetings, each department is then required to prepare its own detailed budget. (Interviewees 11 &12)

After the preparation of all department proposals, the co-ordinator (Chief Accountant) gathers all proposals, examines them and prepares a draft budget. The Chief Accountant is authorised to discuss any budget with any Head of Department if he is not satisfied that his budget has been prepared in accordance with the guidelines. After examining all proposals, the Chief Accountant calls the first official budget meeting to review the drafts.

It is obvious that STC uses the top-down, bottom-up; top-down approach. The process starts from the Head of the company to the Departments with the circular, budgets then go and back from Departments to the President for approval and then are returned back to Departments (see: Drury, 2008; Anwar, 2007).

5.1.2.3 Review Stage:

Obviously, the budgetary process including the review stage requires an iterative approach. Each draft budget has to be repeatedly adjusted until all the budgets are mutually consistent. Therefore, several budget meetings are held in which changes are made to the original drafts until an agreement among departments is reached.

In STC, a Budget Committee of which all members of the Executive Committee are members holds these meetings. Unlike the Executive Committee, the Budget Committee includes all Departmental Heads. The President chairs the Committee: its aim is to discuss the implications of each budget on the rest and assess whether the various budgets fall in line with overall organisational objectives.

It is noteworthy that the empirical investigation (Interviewees, 11,12,13 &14) revealed that joint co-operation in the review stage often leads to difficulties in reaching a final budget that is acceptable to all departments. Departments disagree with each other's estimates, disagreements create tensions and conflicts between heads of departments because:

- (1) Each head of department has influence over the content of the budget. Although some consultation is usual, the degree of influence varies dramatically from one head of department to another;
- (2) The public sector mentality¹⁷ that some department heads still have makes them so obstinate when it comes to their department's proposal.

Indeed, one of the Department Heads stated that:

We used to suffer from old generation people when it came to the review of the budget. They each thought of it as their own department and were driven by a need to get what they wanted regardless of the implications of their specific budget requirements on the overall budget. We are getting lucky lately as the new policy of the Board of Directors is to keep them away from the Head of Department positions even if they could not get rid of them. But there are still some of them here. (Interviewee 12)

It can be argued that each figure entered into a budget is the result of a discussion and bargaining process between the Head of Departments, their employees and the top management.

5.1.2.4 Approval Stage:

Budgets are approved based on the recommendation of the Budget Committee. After reviewing the budget, the President and Chief Accountant meet with the Board of Directors to present the budget to them. The Board discusses and approves the budget at this meeting. Although the Board's approval is considered a routine procedure, the approval is undertaken to legitimise the budget and to ensure that the budget is seen as an official valid document. This then creates a practical implication that binds the organisational actors. All heads of departments and managers have to operate within the final budget.

¹⁷ Most of the interviewees stated that the main problems with old employees (governmental), that they don't like changes. They also have a lot of bureaucracy in their way of work. They are not active when it comes to teamwork as they resist ideas come from others and don't like to be ordered by others specially if they are younger.

5.1.2.5 Execution and Feedback Stage:

After the Board approves the budget, it is sent by the co-ordinator to all Heads of Department. The interviews showed that, once a department receives its budget, it could proceed with its activities. A monthly report is then prepared to compare the department's actual performance with its budget. The checking of the actual results against the budgeted figures provides information on the course affairs are taking, and this normally leads to changes in the way things are being done, or in the plans and budgets themselves, or in both.

This report shows variances and in some cases it shows what action has to be taken. All Heads of Departments are accountable for achieving their budget and they will be held responsible for any variances. The comparisons also help to improve the budgeting procedures in later periods.

The interviews showed that if the Head of Department were responsible for a variance then it would affect his bonus. One case cited was that a Head of Department was asked in writing by financial control about certain variances. Since his answer was not convincing they requested a meeting, which found him directly responsible for the variances in question. This had to be reported to top management, which subsequently cost him his bonus and eventually his position in the company. (Interviewee 17)

5.1.3 Costing Systems

Before privatisation STC was following the MOF regulations and rules on its costing system. One of the interviewees (11) stated that:

When the company was governmental we didn't care about the cost of anything as all projects came from the Ministry and our job was only to execute the project and spend the money they gave us as they indicated.

After the company was privatised it applied a traditional costing system until 2003. The only reason for that, as it was mentioned by one of the respondents, was the lack of qualified people, knowledge and time to develop an alternative approach. Interviewee 11 stated that:

When privatisation started in STC we had a lack of qualified people who were able to apply such sophisticated systems as ABC. We also needed to be able to apply a system that enabled us to calculate our costs. We found that the best way was applying the traditional costing systems, as we had some staff that were familiar with these and recruit qualified people to train current staff for the new system.

The above statement shows that the plan for applying the ABC was in the mind of STC managers, however the decision to use a temporary (traditional) system and delay the application for ABC was well justified. As discussed in chapter 3, to apply ABC for the first time, time, knowledge, and effort are needed: initially STC did not have these.

Although it was clear that STC gradually reduced its overall basket of prices, accompanied by very substantial improvements in profitability as well as in the range and quality of services, some managers still expressed their dissatisfaction with high costs. They expected more cost reductions to have taken place after cost and management accounting systems had provided a technical role enabling better-informed cost control and pricing decisions. This was coupled with better management of cash, inventory, accounts receivable, projects, and fixed assets. A senior manager remarked:

Reasonable justification for the high level of costs could be the dramatic changes, which led to the need to outsource most of the technical issues to consultancy companies. However, this judgment could be ambiguous, especially since adequate management and cost accounting systems existed beforehand. The recent introduction of performance indicators and output measures in order to evaluate and compare achievements, and also the adoption of an Activity Based Costing system, should help to drive financial and non-financial transparency and accountability and clarify the picture of cost-benefits and responsibilities (Interviewee 12).

5.1.4 Implementation of the Balanced Scorecard:

One of the main problems that faced STC when it became a private company was how to turn strategies and subsequent plans into realistic targets for employees, since these would be used to monitor and evaluate personal and department performance. This major deficiency led the company to search for a new technique that could solve the problem; ultimately this was in the form of the Balanced Scorecard (BSC).

At STC, a comprehensive plan was prepared for the implementation of BSC in early 1999. The initial BSC was implemented in a specific pilot department in 2000. At the end of that year top management realised the benefits of BSC and decided to implement it in all company sectors and departments. In 2001 the Department for Total Performance was set up to be responsible for implementing BSC and for sorting out any problems.

Top management was looking for a specific system to help the company measure employee performance against company strategy to achieve total control. STC needed to

Measure employee satisfaction and deliver its strategy in a proper way... therefore the BSC was found to be the system that might help them (Interviewee 12)

A further interviewee believed that STC stimulated its employees using BSC:

“... STC tried to make the employees aware, especially at middle and high levels about the importance of BSC for the company. It provided them with many seminars about BSC ... they also attended many BSC events in and outside Saudi Arabia” (Interviewee 1).

STC decided to convert BSC applications from manual to automatic. The director stated:

A lot of BSC software was available but we were very careful to choose a suitable system that may meet our requirements...therefore, we decided to choose CorVu¹⁸ (Interviewee 1).

The software was installed at the end of 2002 for the whole company.

At STC strong leadership, commitment, and participation by top management were required to achieve successful implementation of BSC. A Saudi Telecom interviewee who was a member of the BSC implementation team stated that:

The BSC team firstly explained the BSC concept to all the top management individually... all executives agreed that the BSC could

¹⁸ *CorVu* is a Software brand, made by American company to provide Performance Management and Business Intelligence solutions for mid- to large-sized companies throughout the world. It is a pioneer in the automation of the Balanced Scorecard; it provides an easy way to view the current performance, strategy and key business drivers of a company (<http://www.corvu.com/>).

support the company in the short and long term.... Top management and senior staff were very supportive and committed to BSC and they always discussed BSC results in their meetings... In 2002 the company decided to link the executives' compensation and rewards with the BSC's results. (Interviewee 1)

In essence, STC appointed a special team for BSC. The appointed employees were committed to the BSC project and possessed key attributes such as being strong team workers, acceptable levels of experience in performance measurement, and fluency in speaking English¹⁹.

The interviewee reported

STC provides employees with detailed guidelines for BSC implementation in PowerPoint and Word, in Arabic and English languages.

In essence, STC believed that the BSC connected the company with its customers in a proper way “... BSC enabled us to use appropriate measures” (interviewee 12).

STC's Balanced Scorecard has about 25 measures for the entire prospect “*create a customer survey to measure our customer satisfaction and have their comments*”. In addition, in 2003, the STC created its strategy maps as an improvement to its BSC.

The BSC system was integrated into the company's systems. “... *The company found no difficulty in integrating BSC with other systems*” (interviewee 1). The BSC team established a so-called ‘KPI library’ to assist the departments to determine their KPIs.

The BSC project had to be transferred from a strategic process to the implementation of a management control system in a more operational sense. Therefore, the distribution of the BSC implementation project plan had to be cascaded from the top to the bottom level.

As previously stated, STC had a clear plan for BSC implementation. Top management agreed all its steps; the short-term plan was to implement BSC within 14 weeks at high

¹⁹ The reason for choosing speaking English employees is that the software is in English, and the training they are going to have is in English under American trainers from the software company.

company level (Figure 5.2) whilst the long-term plan was to implement BSC for the whole company in three years.

However the interviewee believed that

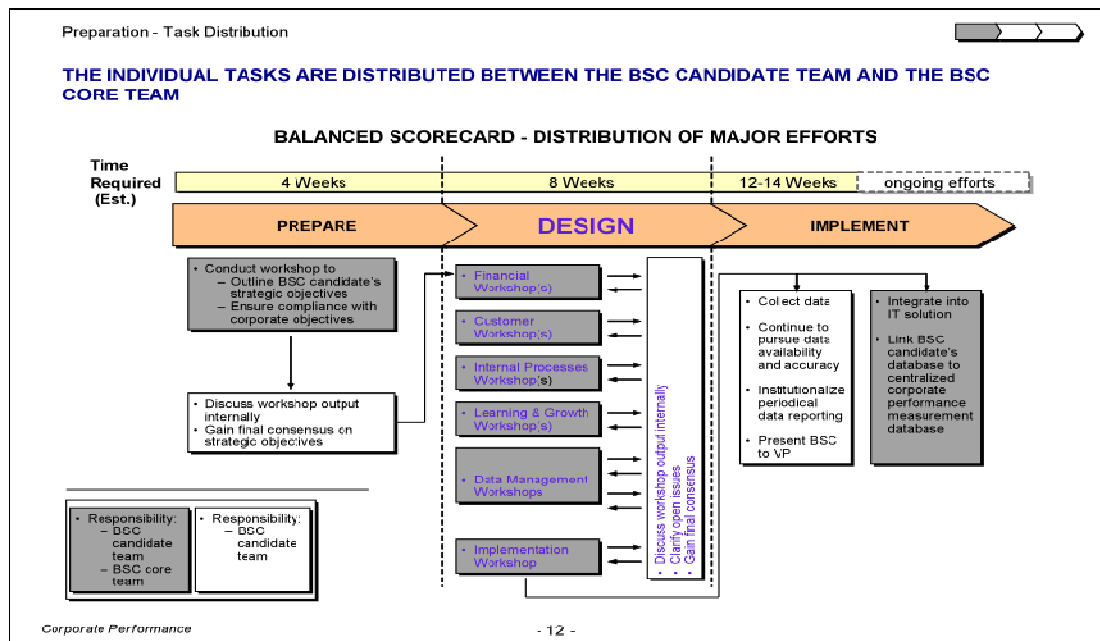
The top management attempted to accelerate the implementation plan in less than two years ... because they realised the benefits gained (interviewee 1)

As noted, STC had an adequate information system. This was utilised to help the BSC team, as well as special software for BSC implementation, to cascade BSC from the top to the bottom level.

STC also planned to roll out the results between its departments. The interviewee stated

BSC processes and results cascaded from top to bottom ... and were rolled out between the different departments. I strongly agree that BSC plays an important role in our company ... each BSC result may help us to refine our measures or processes... as evidence ... in 2002 the top management of STC put the BSC reports as a standing item in all its meetings. (Interviewee 1)

Figure 5.2 STC Initial Plan for BSC Implementation



Source: STC Documents (2005)

STC has achieved many benefits from BSC implementation. The BSC enables the company to fulfil its strategy and assess measurements regularly. Interviewee (1) pointed out

The BSC helps the company to fulfil its strategy by linking the measures with the company's strategic objectives ... BSC also helps us to assess the measures themselves.

The BSC results also assist the company in delivering information to the right personnel, in the right format, at the right time, and in the right quantity. The interviewee also indicated

We found that the BSC helped us to discover and resolve problems ... take the right actions ... and develop new performance standards

While the possible benefits of BSC are obvious, its implementation across organisations may encounter many obstacles. The interviewee from STC said that

We encountered a few obstacles and challenges in the first implementation of BSC such as culture and integration obstacles ... but I believe the most important one was the resistance from some employees ... But we resolved this problem by convincing those employees that BSC is for measuring and improving performance, not to blame them (interviewee 1).

The above statement proves the difficulties of changing the mindset of the Saudi Telecom staff into that appropriate for a commercial service provider, which is attractive to customers, competitive in the marketplace, and is able to make its service activities profitable.

A senior manager revealed that the introduction of the Balanced Scorecard concept created significant changes in measuring and managing the performance of the business units, not only from a technical viewpoint but also from a financial and commercial one. He stated that:

The development of a new information system went along with the development of the Balanced Scorecard. At the time of the decision to adopt the Balanced Scorecard, there was no clear vision on the

management control structure to be developed for Saudi Telecom. Nor was there a clear strategic vision on STC's position in the market and on its position within the Saudi market. The introduction of the concept was a process of muddling through because there was no strategy and clear objectives, nor did we have any experience with target setting, and there was a lack of financial and commercial information. The development of the Balanced Scorecard made clear that a discussion about strategy and objectives was needed, and gave an insight into the information that should be gathered. The concept of the Balanced Scorecard would help us to get a clear picture of the effectiveness and efficiency of our activities and relations with our customers. Also, it would support the discussion about our strategic possibilities and strengths and weaknesses. (Interviewee 12)

5.1.5 Changes in accounting policies and accountability:

In the past, the Ministry of Finance (MOF) stipulated that the organisations under study must fulfil its requirements and submit their reports on a cash basis (Al-sughayer, 2001). But as a result of privatisation, both the Telecoms and the Electricity Company changed from cash based to accrual based accounting.

It is clear the MOF required these organisations to maintain their accounts on a cash basis in order to provide their services within budgeted appropriations. The nature of the Government's goals at that time was to keep spending within budget whilst achieving an acceptable level of service and this was the main reason for the Government requiring cash based accounting from organisations.

However, there was no clear reason for not adopting systems that would achieve their objectives, provide decision-makers with more information for control and planning purposes, and determine the accurate cost of providing these services.

Organisations that maintain their accounting records in accordance with adequate accounting standards, national or international, and whose information is subjected to independent audit, will report higher quality information (Ruffing, 1993). Therefore, compliance with accounting standards will enhance financial accountability as it contributes to the reliability, consistency and transparency of financial information. Moreover, it provides a good base for valuation, which is the most important issue in reform transactions²⁰ (IFAC, 2001).

²⁰ In the case of Saudi Arabia; one of the reform transactions for the Saudi economy was privatisation.

STC faced an accounting change from a cash to an accruals base as a result of privatisation. This change has had a radical impact because the lack of information in the previous system made the valuation of most assets difficult.

The interviews showed that STC faced a very serious valuation problem when opening its accounts, not only because of the previous adoption of a cash based accounting system, but also due to the absence of ownership documentation for some of its real estate, where it had only the right of use.

Moreover, engineering managers' reports were not integrated and clearly reflected in the financial reporting. Before privatisation, the engineering managers in Governmental organisations only cared about achieving projects within the budget agreed regardless of its cost, even if they could manage it at a lower cost. Therefore the engineering manager's reports usually contained detailed technical information with little financial information, which made it useless for any financial reports (Interviewee 11). However, when privatisation took place, the company opened its accounts not only by following Saudi Accounting Standards but also in accordance with American Accounting Standards. A general manager described these events as follows:

The use of government accounting in the Telecoms sector left a heavy legacy. There were no accounting records of assets, any ownership documentation of some of the lands that we used to provide our services. It took us a long time with national and international consulting companies to come up with the opening balances. Although we had used cash based accounting before, we also had other reports that were used internally by our line managers but these reports were not integrated and were mainly prepared and used by engineering managers. The old records at the Ministry of Telecommunications helped a lot in providing the opening balances. When we opened our accounts, there was an intention to engage in a joint venture with an international company so we followed both Saudi and American Accounting Standards to be ready to list and trade our stocks locally and internationally on the New York Stock Exchange. (Interviewee 11)

The same general manager explained the difficulty of asset valuation in the following comment:

Asset valuation was very difficult because the majority of records of historical cost did not exist. There was no comprehensive record of the assets or their historical cost. There was no comprehensive record of

land and buildings owned or occupied by the company. The valuation team had to use numerous methods to collect the documents needed to open the balance sheet. The former supervisor at the Ministry had some documents that helped, and, because the majority of network repair and maintenance was conducted by external contractors, the team also used their records because they maintained detailed asset records that were often more complete and accurate than those maintained within STC. (Interviewee 11).

Due to the lack of previous accounting systems, Interviewee 11 also revealed that the company had had to invest heavily in order to open its new accounts:

Due to the lack of quality information obtainable from the previous accounting systems the STC was forced to pay millions for accounting firms to open its new accounts. In the beginning we had a contract for millions with a large accounting firm just to bring all our documents together in order to help open the new accounts. Then we had to have another large accounting firm value our assets and prepare the first financial statements, and also another large accounting firm to audit our accounts. We now realise the crucial need for cost and management accounting to provide accurate, reliable, relevant, and timely information for decision makers since an accurate cost system is very important as a result of privatisation and potential competition. These tasks were impossible to do on our own so we were forced to engage the services of consulting companies to help us establish most of these systems. (Interviewee 11).

One of the problems that faced STC before and after privatisation (but prior to the market becoming competitive), was that it had huge accounts receivable due to the lack of collection, or as a result of the nature of its main customers since it had to provide its services to other governmental ministries and their departments or to “special people” regardless of their ability or intention to pay²¹.

This could have seriously weakened its ability to finance or update some of its assets and systems, and achieve its planned objectives. But after competitors entered the market, the Government was forced to deal with STC as a regular supplier: these days recovering debt is no longer a problem.

²¹ Those “special people” might include some Royal family members or some other powerful people in the country who have no intention to pay, thinking it is not necessary to pay the Government any money since its perceived existing wealth means it does not need any further finance.

However, as one of the interviewees pointed out, STC still sometimes cannot treat certain special Government Departments as normal customers and they have to be more flexible towards them in relation to debt collection²².

While the majority of managers in STC revealed that organisational restructuring was very difficult due to the previous Government environment, they argued that the new accounting tools and techniques provided an essential communication language for the new commercial environment. In the past there had been no pressure to pay attention to the financial results of each organisational unit, to clarifying supplier-customer relations, or to market developments (interviewees 1, 11, 12, 13). Therefore, there was an urgent need to set up a new system to provide management information about aspects of financial and customer operations, for example, customer needs for specific services and the need to open new markets in new regions, as well as general market information.

Managers showed more awareness and recognised the necessity for sufficient cost and management accounting systems to provide adequate information for controlling and planning. In order to meet the new challenges, the company established new divisions, such as cost accounting using the Activity Based Costing system (ABC), asset management²³, independent internal auditing²⁴, and performance indicators using the BSC. There was a need to manage the various organisational units in such a way that the employees within the units would become aware of not only their technical performance but also their financial and commercial performance.

The financial statements that organisations prepare for external purposes are dependent on the nature of the accounting system they follow and the extent to which professional accounting standards are adopted. STC prepares its financial statements according to Saudi Professional Accounting Standards' requirements²⁵, therefore the contents of its financial statements are standardised. It is now easy to obtain the annual reports of the company in Arabic and English.

²² The implication is that they sometimes have to accept slow payment. Nevertheless the situation has improved since competition: the company is now responsible for its own debt collection even if it is still a slow process. The number of these Governmental departments has been reduced therefore it can be said now that only very high levels of the Royal family can be late with payment: others have to pay on time.

²³ This division is aims to use the best techniques to manage the company's assets, and make sure that the assets are used properly.

²⁴ This will be covered later in a separate section.

²⁵ It was mentioned earlier that they also prepared their financial statements according to US GAAP. That was only at the beginning of the company, because there was a plan for joint venture project with a US company.

Some managers revealed STC paid a great deal of attention to providing reliable and relevant information in its annual financial reports in order to build a high level of confidence for the company's potential investors. The move towards privatisation pressured STC to maintain its records based on acceptable standards of measurement and reporting and to disclose fully financial statements audited by independent auditors. The majority of managers described the reform of STC as a successful experience, despite weaknesses or limitations, because of its pioneering status in Saudi Arabia. Although STC had not yet solved all the restructuring problems, competition would put pressure on the company to become more concerned not only with maximising profits, but also with reducing costs and paying more attention to performance accountability and value for money.

5.1.5.1 Performance Evaluation:

As discussed earlier, before privatisation the main job of the company was following MOF orders regarding projects. At the same time the main responsibility of the company was merely to spend the Ministry approved budget and therefore the need for locating KPIs was unnecessary.

After privatisation and for the purpose of measuring the organisation's performance, STC had adopted the Balanced Scorecard system in order to provide high-level managers with comprehensive, integrated and timely financial and non-financial information linked to the key strategic goals of the company (Interviewee 1).

STC had an awareness of performance indicators, specifically (i) financial in terms of meeting the budget and (ii) non-financial in terms of the quantity and timing of production. The organisation set the indicators in light of the required services and available budget and the Board of directors approved the indicators after examining them (Interviewee 11).

STC has a set of financial performance indicators such as: Internal Rate of Return (IRR), Modified Internal Rate of Return (MIRR), Net Present Value (NPV), and Undiscounted Pay Back and Return on Investment (ROI). STC also has other, non-financial indicators, such as customer satisfaction, and numbers of new subscriptions. (STC documents, 2007).

5.1.5.2 External and Internal Audit:

Saudi companies are required to provide their financial statements for an independent and objective check; however the role and effectiveness of external auditors²⁶ vary from organisation to organisation for a number of reasons (Al-Dehailan, 2004). The main causes of differences are the nature of the organisation's ownership as well as the sources of finance.

As indicated earlier, STC had to spend a huge sum of money to open its accounts when it was privatised. One of the main reasons for that was the absence of auditing. Most managers at STC pointed out that neglect of the audit role before privatisation had led to the organisation being charged substantial sums to set up new accounting opening balances.

If we had had effective external and internal auditors, we would not have had to spend such a huge amount of money setting up new accounting opening balances. Such a lack of information could have been avoided (Interviewee 11)

Saudi Telecom has three different bodies for auditing. The first is the independent internal auditing department, second are two external auditing firms and third is the Audit Committee (see below).

The main job of the independent internal auditing department is to provide continuous reports to the Audit Committee to which it is connected directly (and is above the Finance Department). The Audit Committee are members of the Board of Directors; its remit is to be responsible for reviewing financial reports.

The major work of the Committee is financially supervising the work of top management and the Finance Department before they seek the final agreement from the external auditors.

STC has selected competent audit firms to provide an independent opinion on its accounts²⁷. The external auditors are accountable before all external users for the

²⁶ Saudi Commercial Law forces companies to use two external auditing firms for auditing and approving their financial statements.

²⁷ STC has two auditing firms. The first one is an international firm, Price, Waterhouse & Coopers. The second firm was Deloitte & Touche until 2007, and then it has used Alomari & Co., a Saudi based firm.

company's financial statements. Their responsibility is to make sure that the company's financial statements present the financial situation of the company fairly²⁸.

Some managers showed their frustration at the weak role of the Board of Directors in general and in the Audit Committee in particular. A senior manager blamed the Board of Directors for some of the mistakes and contradictions in managing the company:

I think that, in a company like Saudi Telecom, which was having a boom time in terms of services and revenues, a highly competent Board of Directors was needed to guarantee an adequate level of corporate governance. We received an adequate level of autonomy without a sufficient level of accountability. To be honest, the Board of Directors was supposed to play a more effective role than they did. Unfortunately, some of them were not able to perform their role effectively and did not want to leave it to the people who had that ability. (Interviewee 12).

Further, most interviewees showed a notable level of concern about the importance of ensuring the quality and reliability of their services. A senior manager in STC described internal control practices as follows:

Our internal audit department receives high support and is directly linked to top management, especially the deputy president because of his accounting background. We deal with and derive benefit from the external auditor. We visit branches, prepare annual reports about all activities and give our recommendations. (Interviewee 8).

The above indicates that the high level of concern was due to top management's awareness of the importance of the role of internal audit. The internal auditors are responsible for reviewing all the financial transactions and reviewing the work of the Financial Department in detail and reporting it to the Audit Committee in order to obtain final approval from the external auditors.

5.1.5.3 Capital Management and Investment Appraisal:

Before privatisation, if the company wanted to undertake major new projects, it first had to seek approval from the Ministry of Post and Telecommunications. If the Ministry

²⁸ Saudi legal requirement for financial statements are requires fair presentation.

approved the projects, further approval then had to be sought from the MOF for funding.

The problem here was that the process was very slow and in the end the MOF could turn round and say 'No'. In addition, since projects were not effectively prioritised there was a danger that it could approve one project and yet reject a more important one.

Since STC was privatised and therefore became self-funding, a more focused approach has been followed in order to achieve specific goals and objectives. The new methodology has ensured that projects, after following the internal approval process, have a positive cash impact on the organisation. The new approach is based on commercial studies and the expected economic benefits and competitive advantages gained. Interviewee 12 stated that:

Nowadays our approach has changed radically. There is a greater drive to minimise project expenditure through re-negotiation for prices with vendors. There is improved support for justification of projects including cost benefit analysis. Budget discipline and the approval process have improved and only value adding projects are executed.

Most projects involve a multi-disciplinary approach where each party contributes according to their area of expertise. Accountants and engineers work together to look for costs and benefits in the early stages of a project's proposal; accountants then take full responsibility for financial evaluation and presentation to decision makers. Once the proposal is completed it is presented to the Management Committee²⁹ in the form of a detailed written report and oral presentation. Once approval by the Management Committee has been given, the second stage is to present it to the Board of Directors for final approval.

Projects track a multi-level process that includes preparation by the sector, evaluation by finance, initial approval by the Management Committee through to final approval from the Board of Directors. (Interviewee, 7)

STC uses the Capital Asset Pricing Model to calculate the Weighted Average Cost of Capital (WACC). This rate provides STC with a minimum hurdle rate

²⁹ The Management Committee has members on the Board of Directors. Those members were selected based on their financial and engineering backgrounds. The main job of this Committee is to make sure of the financial suitability of a new project.

with which to evaluate projects. Only projects that exceed the Weighted Average Cost of Capital are accepted.

It is worth mentioning here that STC has a target to achieve 10% of its annual profit from international investments by 2011³⁰.

5.1.6 External environment:

The MOF had the role of pre-auditing³¹ Government entities. SOEs were viewed as separate legal entities. However, due to the accumulated deficits in the country's budgets as well as in most SOEs, it found no better option than centralising the accounts of budget-supported organisations, collecting their revenue in the Central Bank, and providing them with their required budgets.

After privatisation, the situation in STC has changed as it has more autonomy in its accounts and revenue. However, as the Government is the biggest shareholder in STC, the MOF has to receive regular financial reports. Nevertheless its role in dealing with revenues and budgets no longer exists.

Before privatisation the only regulatory body that the company was dealing with was the Ministry of Telecommunications. The Ministry was in fact running the company; therefore it is difficult to say that it was regarded by the company as a regulatory body. However, after privatisation and especially after other companies entered the Saudi market, STC now deals with two regulatory bodies. The first is the Telecommunications Agency, which is mainly concerned with providing fair competition in the market. The Agency usually requires frequent reports about each service provided by STC, but does not require any detailed financial reports. The second regulatory body is the Saudi Stock Agency. This agency aims to make sure that each Saudi company is following the financial standards required by law and that financial statements are presented to all users in the correct way.

³⁰ The President of STC is quoted in a recent newspaper interview of saying that in 2009 STC achieved 21% of its annual profit from international investment. (Aleqtuesday newspaper, 2009, www.aleqt.com)

³¹ Pre-audit means an examination of vouchers, contracts, etc., in order to validate a transaction or a series of transactions before they are paid for and recorded.

Results of the interview survey for STC revealed that most respondents were satisfied with their organisation's level of compliance with statutory obligations and internal rules and regulation. In addition they believed that the statutory regulations were fair to them and it did not prevent them from doing their job properly.

However, some felt that there were times where these obligations, especially to the Telecommunications Agency, prevented the company from providing certain profitable services at the right time. The Agency is more concerned about fair markets and occasionally will stop or delay STC from providing certain services in order to allow another company to gain entry to the market. This issue was the main concern for most interviewees.

One of the interviewee expressed his concern as:

Yes, some times the Telecommunication Agency annoys us by delaying our services but if we look at the bigger picture, it is for our benefit. This action would provide competitors access to the market, which will give us the motivation to improve our own company's performance. If the Agency allowed us to do what we want no other company would be able enter to the Saudi market. We would monopolise the market.... In the end it is good for us. (Interviewee 6)

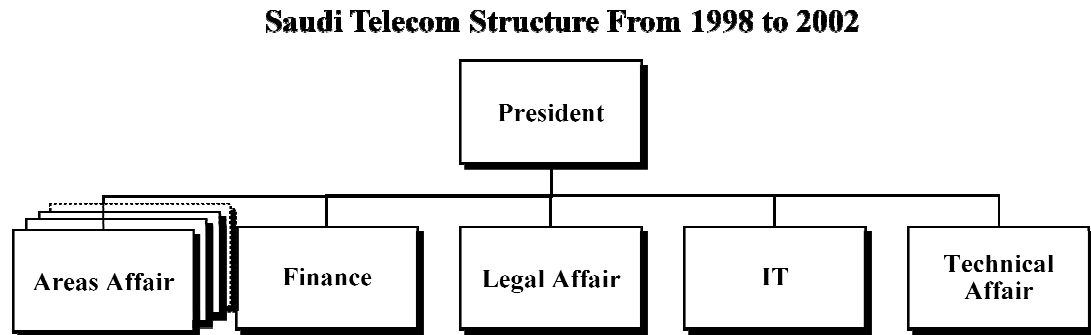
5.1.7 Organisational Structure:

The Saudi Telecom sector was part of the Ministry of Telecommunications until the Government decided to privatise the sector. As a result of privatisation, the company had to come up with a suitable structure to help it to achieve its goals and objectives. Since the sector was privatised in 1998, STC has been through three organisational structure changes.

The first was immediately after the privatisation in 1998 until 2002 (Figure 5.3) but was only viewed as temporary since the company was in transition. This initial restructure was not based on the goals and objectives of the company since it had not had enough time to determine what they would be (Interviewee 11).

However some interviewees did not consider it to be any kind of structural change, arguing that the difference amounted merely to changes in the names of some positions³².

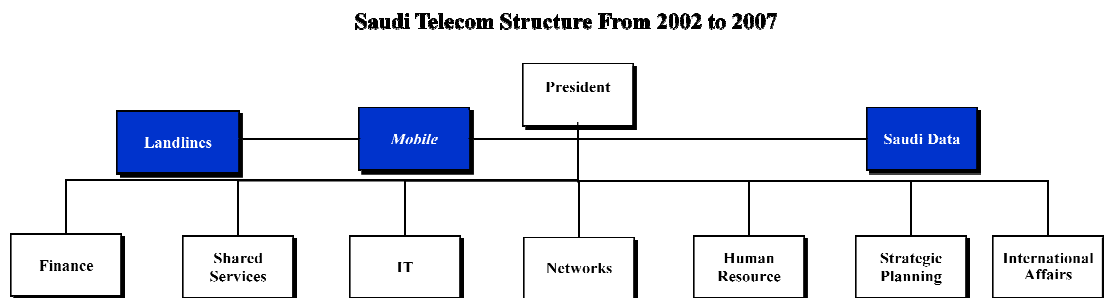
Figure 5.3 Phase One of the STC Structures.



Source/ STC classified documentations, 2008.

The structural second change took place between 2002 and 2007 (Figure 5.4). This was based on the changes in the philosophy and vision of the company, which was now focussed on its product range (Data, Landlines and Mobiles). At this stage the company was more concerned about maximising its service provision. Its key objective was to demonstrate to the Saudi customer base that it was capable of providing the most up-to-date service possible. (Interviewee 13).

Figure 5.4 Phase Two of STC Structures.



Source: STC Classified Documents, 2007.

Interviewee (11) was astute in his comments on problems facing the company after Phase Two changes:

³² For example, before privatisation the Deputy Minister occupied the position of President.

We had a tough time in adapting to the new 2002 structure, as there were several obstacles. We suffered from the lack of a clear picture of the top management, we faced a lack of support from middle management as they didn't understand the purpose of the change and didn't provide us with the information we needed. We faced lot of people who didn't believe in the change and we suffered from people who just talked without action.

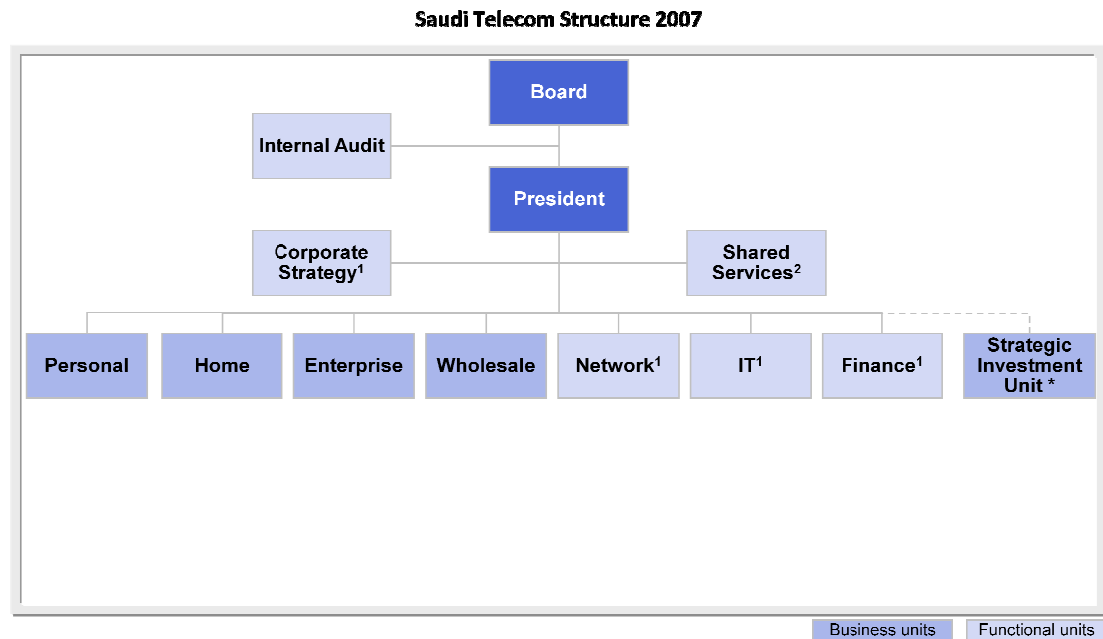
From the above statement it is evident that the core problem with the structural change lay mainly with people who were against it. The company managed to solve this problem by either changing the attitude of the people concerned or changing personnel. This will be discussed in next section.

The noticeable issue during that period of time was the absence of competitors. The absence of competition is an indication of the reason for changes leading to a phase three restructure in 2007 (Figure 5.5).

When competitors entered the Saudi market STC was forced to act in order to continue to attract more customers. It was forced to change its goals and objectives and in consequence had to restructure to achieve the new objectives. These were based on “customer centricity”.

In the previous structure, the main three departments on the company were related to products but in the new structure the main three departments were related to customers (Personal, Home, and Enterprises).

Figure 5.5 Phase Three of STC Structures.



Source: STC Classified Documentation, 2007

From the above, it is clear that STC has changed its structure based on the changes in its goals and objectives.

Thus to summarise, the first change was as the company moved from being a Government controlled organisation lacking credibility in the marketplace to one of autonomy. Its aim was to attract and gain the trust of the Saudi market and convince customers that it was able to provide all the services it needed.

Changes in phases two and three were the result of competition entering the marketplace. The company had to maintain its competitive edge and continue to attract new customers. However, the focus shifted from a product-based approach in phase two to a market, i.e. customer base, in phases three.

5.1.8 Changes in Culture:

Before privatisation, STC suffered from two cultural issues. The first was a Government-based bureaucratic mentality; the second (internal) issue was a predominantly engineering mentality.

As explained in point 5.1.4, STC faced employee problems when implementing the BSC. During that time the company managed to convince the workforce that its introduction as a measure was for positive evaluation of performance and not one designed to allocate blame. However this was only part of the solution: it still needed to change the mindset of its employees to ensure acceptance of any changes resulting from its introduction.

A general manager described the situation regarding the organisation's cultural situation as follows:

We had two main kinds of attitude problems: the first one was a non-business Governmental bureaucratic mentality The attitude of those people was that they believed that they were going to get paid, and promoted anyway so why should they bother themselves. The second was with us, the engineering people who wouldn't listen to anyone else in the company and thought they understood better than others and were always right. (Interviewee 1).

From the above it is evident that the company had to change the culture of two kinds of employees.

The first were front line employees who dealt directly with customers and at the same time suffered from the 'governmental bureaucratic mentality'.

The second concerned employees whose attitude affected the internal organisation and were suffering from both a 'government bureaucratic' and an 'engineering' mentality.

To solve these problems the company made a contract with an American company³³ with offices in Turkey, the reasoning being that whilst indigenous Turks would have a good understanding of the Arabic and Islamic mentality, they would also bring a Western business approach to the situation.

The project was in two phases: the first was to conduct a series of lectures, seminars and workshops with front line employees into how best to deal with customers.

The second was a long-term plan with both front line and inside employees. This long-term plan entailed lectures, seminars, workshops, and long training courses outside

³³ This company was called Peppers & Rogers Group. Peppers & Rogers Group is a management-consulting firm, recognized as the world's leading authority and acknowledged thought leader on customer-based strategies and underlying business initiatives. Founded in 1993 by Don Peppers and Martha Rogers, Ph.D., Peppers & Rogers Group invented the term 1to1® marketing to illustrate the importance of *treating different customers differently*, and transformed the concepts into practical methodologies driving financial results for companies. <http://www.peppersandrogersgroup.com>

Saudi Arabia. The long-term plan was aimed at employees who wanted change and were selected by the consultants. If it was thought that employees did not want to co-operate with the new direction of the company they were offered a 'Golden Cheque', described below.

The need for the change in the accounting system forced cultural change within the company. One general manager described how crucial this need had been in changing the organisation's environment from one of being highly bureaucratic to becoming more autonomous.

He commented:

The establishment of new accounting systems was critical in shifting the culture from an engineering one with an emphasis on physical production, to a commercial one in which the emphasis was on markets and finance and in which accountants, public relations personnel, and marketing managers significantly increased their power relative to engineer. Also, a clear mission statement and objectives helped in driving new definitions of roles and responsibilities so that meaningful corporate plans, budgets, cost and performance reports could be established. (Interviewee 14).

The move that STC took to change its organisational culture was costly and time consuming. But the benefits that the company was seeking were ambitious and worth it.

A manager stated that:

We spent hundreds of millions on the culture project. It was so costly and it took lot of time to be done. But we were happy for that as we managed to change our employees' attitude towards customers, competitors, and the need to accept changes in a positive way. The other cost we spent was on getting rid of people who don't want to change. That was another issue. (Interviewee, 6)

5.1.9 Human Resources Development and Reward Systems:

Before privatisation, STC's employees lacked any motivation to be creative (Interviewee 17). Since the company was part of the Government, employees were

merely concerned with ‘getting the job done’ rather than thinking about ways to improve or add any new creative aspects to it:

As a government employee, your job was to follow orders and rules that came from the Ministry and to get the job done. The Ministry people thought they were able to make plans and tell you what to do, you didn’t tell them what to do. (Interviewee, 6).

A further issue was that employees would receive their salaries (and could even be promoted) regardless of whether they achieved set targets. The result led to no clear differentiation between those who were and were not doing a good job. Reward and advancement was based on two things: personal connections with high level company or Ministry employees, and successful completion of service at a designated level which would lead to automatic promotion to the next grade. (Interviewee 1).

When STC was privatised, it was faced with two common issues that impaired its employee’s effectiveness and performance: overstaffing and lack of qualifications. However with autonomy came the ability to introduce programmes to reduce the number of employees. As a result, STC, due to the boom in its services and revenues, has been able to encourage employees to take early retirement and attract new competent employees by establishing what it called the “Golden Cheque System”. Whilst this system has cost the company millions of Dollars just to get rid of unwanted employees³⁴ it has resulted in the company being able to reduce its number of its employees from 22,000 in 2001 to 17,000 in 2007. The target is to reach 12,000-13,000 employees by 2011 (Interviewee 17).

On the issue of lack of qualifications, especially financial and commercial, a general manager explained how the company overcame that problem with the following comment:

The lack of management in-depth knowledge and experience with financial and commercial aspects resulted in the adding of financial and commercial expertise to top management and to the seeking of direct help from external experts. Without the help of consultancy companies it would have been difficult to achieve the changes in the company. They made an essential contribution in smoothing the change processes and in helping to adopt new accounting practices. Also, attracting competent

³⁴ Unwanted employees is a term used by an interviewee number 17 to describe the kind of unqualified, resisting changes, and governmental mentality employees.

people from the private sector was very important, especially in finance, accounting and commerce, because consultants needed competent people to be able to understand and implement the new systems. (Interviewee 11)³⁵

Some managers expressed the view that the radical change processes were more difficult and took more time because the appointment of top management had been based on engineering rather than financial and commercial knowledge and experience. The majority of managers indicated a significant increase in the power and influence of accountants³⁶ during the process of privatisation. A general manager gave the reason for the high demand for competent accountants and the new role played by accounting. He stated that:

After privatisation, without sufficient quality information and adequate accounting systems, it would have been difficult to have a common language of communication. The roles of accounting and accountants were changed tremendously in order to facilitate the political and organisational change. This was not only through the technical provision of information necessary for the parties involved to complete transactions but by changing perceptions and setting the power of accountability. The number of qualified accountants employed increased substantially and most of them came from the commercial private sector. (Interviewee 11).

Dramatic changes have also been made to the Board of Directors. Before privatisation almost 90% was comprised of engineers (Interviewee 17), now most members have financial and commercial backgrounds (Table 5.1).

Table 5.1 Qualification of Board of Directors Members on STC.

Qualification for the member of Board of Directors on STC	
Number	Qualifications
1	B.A in Economics in 1979, MSC in Economics in 1981, PhD in Economics 1986. The Director of the Saudi Monetary Agency.
2	M.A in Public Administration. Governor of Public Pension Agency

³⁵ It was obvious from looking at the CVs of most people who work now in the company that they were attracted to join the company in recent years. The company made radical changes in the people working in the finance department and top management between 1999-2003.

³⁶ From 1970s to 1990s, Saudi culture valued engineering and gave it high social respect and high income. Based on the nature of the then Government's goals to establish new infrastructures the focus was on engineering.

3	B.A in Finance. MSc in Accountancy. The Deputy of Finance Ministry for Budget and Planning.
4	M.A in Finance, MBA,
5	Deputy Director General of Technical Affairs & Information in Saudi Customs, Ministry of Finance. BA, MSc, PhD in Information Technology.
6	Business Man, B.A, and M.A in Engineering and Business Management.
7	Business Man, B.A; MSc; and PhD in Accountancy.
8	M.A, and MSc in Telecommunication Engineering.
9	B.A and MSc in financial Accounting.

Source: STC documentations 2008.

One of the main issues in STC is the evaluation of its employees' performance. It distinguishes between two levels of employees, viz., those on grade 12 and above (middle and top management) and those under grade 12 (lower management). Each level has two main performance evaluation indicators (PEIs) based on the nature of the work.

The first PEI is entitled "Achievement of Objectives" and is applied in a similar way to both levels of employees. This contains financial, customer, and learning and growth objectives according to the managerial level and nature of work.

The second is based on "Competencies". Managers on grade 12 and above have 10 indicators as follows: leadership, functional knowledge, team working, communication, planning, commercial awareness, problem solving, corporate relationship, time management and customer focus.

Competencies for those under grade 12 are divided into two sets, the first being "Core Competencies": functional knowledge, team working, customer focus, commitment, quality and accuracy, time keeping and attendance, and asset management and care. Inability to achieve acceptable grades in these areas could lead to loss of job.

The second set are "Optional Competencies", containing the 10 indicators of the top and middle managers competencies to which is added 'Safety'. If lower grade management employees manage to achieve three or more of the optional competencies they will be entitled to attend company "Leadership Training Programmes".

It is noticeable from the above that STC used BSC to evaluate its employees.

Another interesting issue on STC is the loyalty of its employees. A general manager stated that:

We make a contract with a neutral party to study the loyalty of our employees every year. The aim is to find out what should we provide as bonuses for our employees. We are in a competitive market; if we don't keep our good employees we might lose them. Apart from bonuses we sometimes provide them with financial facilities like zero rate loans and scholarships for them or their kids to study abroad. (Interviewee, 17).

It was obvious that the majority of managers interviewed believed that privatisation would encourage employees to perform well and give them rewards based on their individual performance.

5.2 Changes in SEC's Management Accounting Control Systems

The previous section discussed the changes that happened in Management Accounting Control Systems in the first company in the study (STC). The following sections will explore the changes in these same systems within the second company in the study – Saudi Electric Company (SEC).

5.2.1 Changes in Planning:

Although SEC has moved towards privatisation, which creates pressure to meet targets for financial performance and reliability of services and to ensure resources are used as efficiently as possible, it is still considered a public service provider committed to continuing to provide its services at a consistent and affordable price (Al-Dehailan, 2004). The majority of managers interviewed suggested that privatisation could help eliminate non-commercial objectives and make management more aggressive and focused on developing new business initiatives. However, most maintained that the company could not operate effectively without having a reasonable level of autonomy in its budget setting and decision making processes, having clear plans and objectives, developing a cost accounting system, enhancing the role of internal auditing, and

motivating the role of the Board of Directors to achieve financial and non-financial performance accountability (Interviewees B, C, D and E).

They stressed the need for an integrated information system to achieve a timely, reliable and relevant information system. All interviewees confirmed that SEC still doesn't have enough autonomy in setting its goals and objectives. It still operates under Government objectives and plans, the majority of which are based on social rather than commercial factors. Interviewees B and C also commented that whilst SEC might sometimes propose changes or suggest new objectives they were still subject to Government (Ministry of Electricity) approval.

5.2.2 The budgetary process:

Although the budgetary process at SEC is similar to the process at STC two main differences occur in the preparation and approval stages.

First, the goals and objectives come mainly from Ministry of Electricity, especially for new projects. On the basis of objectives SEC then has to prepare its own detailed objectives and from there prepare its budget guidelines. The budget for SEC has to have a full recommendation from the Budget Committee within SEC. The President and Chief Accountant meet with the Board of Directors to present the budget, which is then discussed by the Board and approved.

After gaining approval from the Board of Directors, the President and Chief Accountant then seek approval from the Ministry of Electricity and the Ministry of Finance. This involves meeting the Deputy Minister and his team and presenting and defending the budget, and this is the second difference from the process at STC. The approval of the two ministries legitimates the budget and creates a legal implication that binds the organisation.

The big involvement of Government at SEC's budget approval stage shows the limitations of SEC's autonomy in relation to its budget since one of the Ministries may disagree with any part of the budget and change it. In addition the Government will fund some of projects even if they are not commercially profitable.

5.2.3 Costing Systems:

The aim of the current traditional cost system being employed in SEC was not to achieve financial accountability but to monitor operations and production. A manager described the current costing system in the following way:

The current cost system could be described as aggregated information since we have three major activities: generating, transmission and distribution, each one being considered as a cost centre that has sub-cost centres. It is difficult to compare costs and effectiveness or benefits because it is an aggregated system. The details might exist in the technical departments. You can tell from the high maintenance expenses that there is a low awareness of cost benefit or cost effectiveness, because technical people are more concerned with meeting the level of production with a specific quality of services and continuity. (Interviewee C).

SEC has not adopted the Activity-Based-Cost system and is still using the traditional cost system. SEC faced difficulty directing and allocating its expenditures between activities to rationalise its expenditure and decisions as indicated by the same manager:

It is difficult to rationalise expenditure without having a good cost system and knowing how high some costs are and what costs less. The current system does not distinguish, so any reduction will not be logical. Frankly speaking, the current accounting system is just about revenues and expenditures and the expenditures are not entirely correct. The information system is ambiguous and the current databases are not accurate. For example, it is difficult to obtain an accurate cost for any product or service. In the absence of accurate data, therefore, it is difficult to reach an adequate decision. (Interviewee C).

From the above statement it can be said that the current costing system is geared to aggregate measurement, doesn't disaggregate and therefore fails to provide useful internal information.

A manager gave an illustration of the lack of allocation costs, not only in overheads but also in material and labour costs:

The cost system should help to provide aggregated information. However, it cannot provide accurate information for achieving adequate costing and pricing. It is a traditional system and there is no incentive to develop it because I don't think it will be used as an accountability tool.

The variation in the allocation of material costs sometimes comes from an inaccurate direction in the transaction when we record the accounts. It is the same for labour costs, if the cost centre has, for example 15 employees when we examine the centre we may find more or less. So the cost system is an aggregated system not a detailed system. (Interviewee C).

The inaccurate allocation of cost was a big issue in SEC. Most senior managers in the company expressed the need to develop their old cost system by adopting an Activity Based Costing system (ABC) to provide adequate costs, especially with the new trend towards commercialisation and competition.

The feeling was that the organisation had to become more concerned about determining adequate costs and prices in order to ascertain how much it has to spend to provide services in a commercially oriented environment and still achieve an adequate profit margin.

The pricing policy in SEC is one of the main reasons that the company does not pay much attention to cost systems³⁷. One manager commented that:

The company receives a list of the prices for the services that it provides from the Government; the prices do not always cover the cost and sometimes they are not even close - so what difference is a new costing system going to make? Whatever we say to Government the cost is, they believe us, and they cover it for us, so why should we change? (Interviewee A).

The above statement confirms that since SEC has no control over pricing its services, it has become irrelevant for it to know the accurate cost of its services. This is because it knows the Government will cover the difference. Therefore, it is obvious that there is a lack of motivation on SEC to change its costing system.

However, one manager at SEC revealed the increasing amount of attention the organisation's President is paying to the need to determine the cost of providing services:

Our President is highly concerned about the cost of providing services. We have established a new department to monitor service and costs for

³⁷ The Saudi government has full control over pricing of the electricity service in the country for political and social reasons.

every project; in the near future the private sector will be encouraged to come and build, operate and own the new projects and we will buy and distribute their electricity production; therefore, it is necessary to know how much it costs us to provide these services in order to pay a reasonable price to private providers. (Interviewee A).

The above statement shows how competition is likely to motivate the company to change.

The above practices reveal the very small impact accounting information has on internal decision-making in SEC because it cannot provide a useful database for pricing and other managerial decisions. The current cost system could be classified as underdeveloped or inefficient. The lack of available information and low contribution of management accounting to quality information provision, scientific management and cost techniques, could be a result of the low importance attached to accounting information, because line managers are more concerned about meeting the specifications for their products, mainly in terms of completion dates and improving production efficiency.

Financial implications tend to be ignored because of the lack of cost information on a systematic basis. The suggested logical reasons for that are: the domination of the company by engineers, lack of competition which reduces the need to change, and the involvement of Government and its readiness to provide whatever cash is needed.

5.2.4 Implementation of the Balanced Scorecard:

At the Saudi Electricity Company (SEC), the BSC does not exist. Interestingly, out of 8 people from different management levels, mostly in the financial department, only one person could answer the question about BSC without asking to have BSC explained to him. That person was the only interviewee who had worked in a totally private company before working at SEC. He was fairly new to SEC and it was obvious from his point of view, that the others still had a public sector mentality, leading to a rejection of the need for innovation and vision, the need to compete with others, the ability to make quick changes and adjustments, and a desire merely to follow orders. The interviewee who could identify the meaning of BSC said that the reason for not applying BSC, which he thinks would be very useful for the company, was:

... Yes SEC is a public listed company and considered as a private company, but in reality and based on the way management in the company operates, we are still a sort of public owned enterprise.... We cannot apply BSC because first, the top management won't understand it, second it will conflict with the Government way of running the company... BSC is a system for the whole company and if you want it to work properly you should apply it in every department starting from top management; it requires lots of strong leadership and huge participation by top management and the problem is that these people still have a public sector mentality. (Interviewee G)

From the above, it can be argued that SEC has to make radical changes in the nature of top managers and the culture of its employees. In addition, Government has to give the company more autonomy in its policies and open the electricity market up to competition.

However, interviewee G mentioned that although a proposal had been made by one consultant to apply BSC to the company he still maintained it would not work because of the aforementioned reasons³⁸.

5.2.5 Changes in accounting policies and accountability:

According to the IFAC (1989), state-owned enterprises should operate reporting systems consistent with accrual based and other generally accepted accounting principles. However, although SOEs are supposed to implement accrual based accounting, they are not homogenous, since some use cash based accounting and others follow accrual based accounting, depending on the legal requirements and enforcement of implementation (Ruffing, 1993).

Before privatisation, SEC, as with STC, was required to fulfil and submit its reports based on cash based accounting systems by the MOF in order to supply its services within budgeted appropriations.

³⁸ In early 2010 the company announced a plan for applying BSC. They stated that they would start in the Human Resources Department as a Phase 1. Phase two would be in the Generating, Transformation, Distribution, and Customer departments. Phase Three would be Regulatory, Internal Audit, and Finance departments. Phase four would be Top Management. The plan would be completed by 2014; the programme contained workshops and training days.

Nevertheless, as a result of privatisation, SEC changed from cash based to accrual based accounting in 2002. The change from cash to an accrual basis in SEC has had a radical impact because the lack of asset values made establishing the opening balance sheet difficult.

Some managers revealed that the East regional company led the process of consolidation because it maintained its accounting records with more reliable and informative accounting systems than the other companies. The more informative systems in the East regional company were possibly due to the nature of its ownership, since the Saudi Arabian Oil Company (Aramco) owned a high percentage (41.12%) of the company.

Nevertheless, the Saudi Electricity Company faced fewer valuation problems than the Telecoms Company because the six small and the four main regional companies (East, West, Central, and South) had maintained their accounting records using accrual based accounting in accordance with National Accounting Standards³⁹. However, the small projects that were under the governance of the Electricity Enterprise had used cash based accounting which presented difficulties due to lack of accounting records for their assets. During the consolidation period, the net assets of these small projects were valued by a national accounting firm at almost SR 1.2 billion, which represented only a small portion of the company's total assets (SR 90 billion).

Although these ten regional companies prepared their accounting using the commercial accounting system, and their accounts were subjected to independent audit, Government ownership influenced their accounting practices since they were required to follow accounting policies advocated by the parent Ministry (the Ministry of Industry and Electricity, now Ministry of Water and Electricity). Comment from Interviewee D, a general manager:

Although we used to follow Saudi Accounting Standards and choose our accounting policies from these standards, sometimes when we sent our accounts to the Ministry it would force us to change some accounts, especially if we had high operating expenses. It would ask us to capitalise them to reduce losses but now, after the cessation of Government subsidies, I think intervention from the Ministry will also

³⁹ Saudi Commercial Law requires the use for National Accounting Standards.

stop and new harmonisation of accounting policies will help us to present our accounts more fairly. (Interviewee D)

The above statement clarifies the role that Government was playing in SEC by the politicisation of accounts. The involvement of politicians in the accounts of SEC could be viewed as one of the reasons the Saudi government made the move towards privatisation.

Moreover, the ten companies' accounts were consolidated without asset valuations, causing possible major problems in the future because of unfair asset values. One manager pointed this out:

Merging all the accounts of these companies into one set of financial statements without valuation of their assets is a major issue that has to be solved because of the inaccurate historical costs of the previous accounts. Moreover, this company has its stocks on the stock market and accounts are supposed to be presented in a reliable and credible way to investors in this company. (Interviewee A)

As it was the case in STC before privatisation (see 5.2.4), SEC has huge accounts receivables. There are two possible reasons for that: (i) the lack of collection, (ii) the nature of their main customers, since it has to provide its services to other Governmental ministries and their departments, or "special people" regardless of their ability or intention to pay.

From a purely commercial point of view, this could seriously impair its ability to finance or update some of its assets and systems, and achieve its planned or desired objectives. However SEC overcomes this problem by financing its projects from Government funds.

In the case of bill collection SEC has no autonomy as it has to follow the Government system and orders. The problem is that whilst SEC is considered a private company, when it comes to cash the MOF considers it to be a Government asset.

Besides the huge accounts receivable, SEC also has huge accounts payable because it receives fuel and oil from the Government owned company, Aramco. It is obvious that SEC has a huge debt. The fuel bill and certain other contractors cause this debt. The

only logical reason for that is that SEC uses the privilege of being the only company that supplies a very important service (electricity).

Also the main debtor is a Government owned company (Aramco) and, as explained by senior managers, this is a serious issue that should be solved before any further action towards reform⁴⁰.

SEC not only has more than SR 14 billion accounts payable, including SR 6.7 billion and SR 5 billion for Aramco and contractors respectively, it still uses the old tariff for fuel which is cheaper than the new tariff. According to the new tariff, an additional SR 4.7 billion would be added to the accounts payable if used (Electricity Annual Report, 2006).

Furthermore, SEC has a shortage of quality accounting information that is attributed by one senior manager (Interviewee C) to the inability to update their current accounting system and lack of an integrated IT system that would help to provide reliable internal reports. Another senior manager (Interviewee E) confirmed differences in information provided by many related departments' internal reports, and also the weakness of other systems, such as costing and warehousing.

SEC needs to improve the quality of its information provision; maintenance and warehouse systems need greater control in terms of cost benefit and effectiveness, especially with the trend towards increasing commercialisation and the ready availability of qualified engineers.

Although SEC has no difficulty in acquiring and attracting qualified people, it still has inefficient management and cost accounting systems which are very important for determining accurate costs of providing services, rationalising costs, providing clear justification for the provision of services below costs, and facing potential competition (Interviewee C).

An accountant at SEC expressed his concern about the warehouse system, stating:

In a sector like the electricity business, warehouse items worth millions should be accurately monitored. Unfortunately, we still use the old system and whereas most or maybe all the other electricity companies have been updated with new systems because they care about costs, we are providing the service, which is the main concern, whatever it costs. (Interviewee F).

⁴⁰ There is a proposal about dividing the company into three different companies: production, transmission, and distribution and also allowing competition.

Another problem, which should be noted at SEC, is that it is not always possible to obtain sufficient information because of (i) the lack of communication between departments and (ii) the fact that more use is made of engineering reports than those of the accounting department (which would more accurately reflect transactions and events).

One manager commented on the lack of communication between departments as follows:

The engineering staffs are the people who provide the information upon which top management decisions are made and the finance department just records what has been done. (Interviewee E).

Some managers expressed their frustration at the new reform because they considered it a temporary solution to the poor performance of the weak companies. They revealed that the Government had asked the stronger companies to take over the weaker ones, which could subsequently lead to the stronger turning into weaker.

One manager expressed his concerns with the current proposed mergers as follows:

Now the government has not only stopped subsidies but has also merged its General Electricity Company (GEC) projects with the six small companies and the four regional companies. While the regional companies complained of a lack of autonomy, finance, incentives and poor performance and effectiveness, which impaired the motivation of management to act commercially, small companies were worse and the GEC needed radical accounting and managerial changes. Their employees also complained about low salaries and benefits. Therefore, the recent reform is not an easy task. It needs clear vision to achieve successful reform because, without adequate autonomy, sufficient power of collection, clear planning, and reliable information, the new consolidated company would possibly collapse. It is difficult to serve for so many years and then see your salaries and benefits decrease. With the current situation, restructuring the companies may frustrate some employees in terms of their salaries and benefits or their positions (Interviewee B).

Another further manager explained the previous accounting practices of the GEC projects as follows:

The former GEC projects did not maintain their accounting records based on an accrual accounting basis nor did they have a cost accounting system. We faced difficulties in implementing our accounting systems there because of the lack of its financial employees' qualifications so we convinced some of our staff to work there and train their employees. A national accounting firm valued their assets. The result of the valuation was less than SR 1.2 billions, which represents a small proportion of the total assets of the consolidated companies (SR 90 billions). Also, the net assets of the former six small companies, based on their audited financial statements, represented only a tiny proportion of the company's capital, no more than 0.16%. However, if some or perhaps all regional companies needed serious development in cost and managerial accounting, the others definitely needed radical accounting change. (Interviewee D).

Some managers did not consider the merger with six small companies and the GEC a major concern because of the minor impact of the assets of these companies on the total assets of the Saudi Electricity Company. However they did express their concern about the reliability of the previous regional companies' financial statements because they were consolidated without asset valuation. A general manager explained his concern in the comment below:

The process of reform jumped to harmonising the companies' accounting policies and procedures without stopping at the companies' assets, which seriously needed to be devalued. The adoption of new accounting policies that were not followed by the former 10 companies resulted in making non-recurring adjustments of more than SR 2 billion. Technical asset valuation should have taken place so that the results in the financial statement were fairly presented. Before consolidation, and due to the yearly deficits, sometimes we were forced to capitalise some operating expenses in order to reduce yearly deficits. Therefore, figures were unreliable and could have led to inappropriate decisions, whether for the short or long term. Also, whilst the amounts of shares in the Centre Region Companies were double the East Region Company, they had a lower level of reliable accounting information than in the East Region Company, which raised further concerns". (Interviewee C).

The above comment provides evidence that electricity companies had been forced to adopt income increasing accounting procedures to reduce the level of deficits by deferring current expenditures to the future. This possibly resulted from either the high degree of freedom allowed by existing accounting standards to choose the accounting policies that promoted the company's best interests, or from weak pressure to

implement the accounting standards since the Government did not want to show that its enterprise was making big losses.

SEC is now required to have its financial statements certified by an independent professional auditor. The Finance Department is responsible for preparing these annual statements as indicated by an accountant at SEC:

We, in the finance department, prepare the financial statements and send them to the President and his deputies. They go over them so they are ready for the Board of Directors. (Interviewee F).

The interviews showed that one of the big issues in SEC is the weak role and ineffectiveness of its Board of Directors to enhance organisational performance, planning and control. This weakness is the result of many factors, including

- (i) A lack of relevant qualifications, which results in members' inability to make clear, rational decisions (members are chosen based on trust or specialist knowledge and experience as old government employees); inadequate autonomy; and
- (ii) Lack of accurate information and insufficient attention paid to costs, since cost awareness does not seem to go beyond the short-term because of inadequate accounting systems which provide unreliable information and impede effective control, pricing and planning.

Some interviewees suggested that lack of sufficient internal and external control also contributed to the Board of Directors' ineffectiveness⁴¹.

Interviews also showed a lack of autonomy in terms of pricing. SEC does not have any level of independence on the issue of pricing as the Council of Ministers decides the price of services. If the price does not cover the cost, the Government makes it up and pays the difference.

⁴¹ The Board of Directors had major changes to its member profile in late 2009 when most of old members left the Board and were replaced by other qualified, experienced members. However most of the new Directors are still engineers.

The interviews showed that SEC had a quite good level of freedom in terms of generating adequate financial resources for both operations and capital expenditure, due to being able to borrow and retain income.

However, although SEC dominates the market by providing a monopoly service, it also has to provide its services to local government, which leads to difficulty in collecting accounts receivable, so it lacks cash.

Furthermore, although it retains its huge income and uses it to recover its expenses, this requires a sufficient degree of cash management in terms of short and long run investment and a good sense of cost allocations.

A group of senior managers in SEC (Interviewees B, C & D) expressed their concern about virement. They attributed the high transfer between expenditure headings as planned in the budget to the organisation's lack of planning, clear vision and objectives. Most managers expressed their concern about high asset maintenance expenses, which they mainly attributed to MOF not requiring an effective budgeting system.

In SEC, in order to convince current and potential investors about the company's new plan, some managers expressed the need for sufficient autonomy over collection and pricing, as well as adequate accounting systems that accurately reflected the cost of providing the services. They revealed some frustrations about the company's future because the current situation is unclear. Some of them stressed that reforming the electricity companies needed more effort than telecoms because electricity would not experience the same boom in services and revenues unless the government was courageous and made huge investments, not only to enhance the current infrastructure but also to ensure more advanced quality information to achieve sufficient planning, control, and performance accountability.

The SEC prepares its financial statements according to Saudi Professional Accounting Standards' requirements; therefore the contents of its financial statements are uniform. It is easy to obtain the annual reports of the company.

A general manager in SEC stated:

For internal purposes, we also have internal reports that include more detailed information about the production and costs of every plant. In fact, most of the day-to-day problems are technical; however, they are

not presented in the financial report because of the lack of communication and the wide gap between the finance department and the technical or engineering departments. Although I'm quite confident that technical people care about the quality of production, and could provide sufficient information for efficient and effective decision-making, in the financial department we don't see the information in detail to assess its rationale, we just record aggregated information. The technical department determines the needs and after the contracts have taken place we just record. Why that expenditure took place or that asset has been disposed of, we are the last people to know the reasons. (Interviewee D).

From the above, it seems that engineers or technical managers are the main sources and users of the information and reports are presented in aggregated form without any basic disclosure of the techniques used to provide this information, especially to determine and allocate costs.

Nevertheless, its ability to attract highly competent engineers, who supposedly have adequate qualifications and knowledge of highly technical methods, should help to reduce the risk of providing unreliable and irrelevant information.

This issue was noted in STC before privatisation and still exists in the SEC, where engineers are usually the ones who lead. In addition, the above statement casts light on the weak relationship between the finance department on one side and top managers and the technical department on the other. It also reveals that the Finance Department has no real and obvious management accounting role.

A general manager in SEC expressed a very interesting view of the Financial Department as follows:

The most important issue in our organisation is to achieve the production target and to make sure there are no obstructions to meeting this. Financial issues should remain the concern of the finance department. Its role is to keep records of our transactions at the end of the year. They do not understand the core business, the production issues, so why do they want to participate in something they don't know anything about? As for the control issues, these should be our area of concern because we know our work better than others. (Interviewee I)

These remarks highlight the fact that some line managers view accounting merely as the documentation of historical data. Managers with a similar view to that expressed above may in fact be concerned about loss of power by allowing low level personnel or other

departments to monitor the economy, efficiency and effectiveness of their units' day to day operations, production or maintenance.

Surprisingly, some also do not recognise the value added of independent control, and using cost awareness in addition to production targets. They are the ones who determine spare part specifications and methods of maintenance, i.e. the budget needed. But who oversees the accuracy of their demands, their qualifications, etc.?

A completely integrated information system is required to achieve sufficient control and performance accountability.

The ten electricity companies had a good record of presenting reliable annual reports using the commercial accounting system, since they adopted Saudi accounting standards, which made issuance of the annual report after consolidation of the electricity enterprises' projects much easier.

SEC's financial statements may now show more quality information because at present it is partly privatised, i.e. it has investors as well as creditors that need to be satisfied with the information they obtain to evaluate the company' performance and for comparative purposes.

The issue of concern in SEC is the accuracy of the financial position as well as financial performance because of weak cost determination and allocation, which may result in inaccurate valuation of assets.

It was noticeable in SEC that there was undue delay in the reporting of its financial statements⁴² which might have impaired their relevance. This may be because it is a partly state-owned enterprise and operates without any competition and as a result external pressure is insufficient to motivate the provision of timely financial statements. Moreover, its information is insufficiently accurate, because the cost accounting system is inadequate. It is supposed to provide raw information for the accounts, but fails to do so because departments' internal reports are difficult to integrate financially as they are mainly technical. This reduces confidence in departmental results, leading to possible bias in financial statements.

Additionally, as a result of inaccurate information and delays in passing on information between the various departments of the organisation, it is not untypical for senior

⁴² For example, financial statements for 2005 were approved and released mid May 2006, those for 2006 were approved and published early June 2007, 2007 statements were approved and published mid May 2008.

financial managers to use their intuition and judgements when information is requested by external parties as an accountant disclosed:

To be honest, in some situations, we have no adequate way except using guesswork, shortcuts, making approximations and rule-of-thumb assessment to meet information demands. (Interviewee G).

A manager in SEC pointed to the inconsistency between annual reports as follows:

As regards timing, we prepare the annual report based on the rules and regulations of the MOF or the governmental accounting system, and within the three months after the year-end. The commercial accounts need another three months to adjust the fixed assets. The results will, of course, be late which may raise doubts about their usefulness for decision-makers and their purpose for the Board of Directors. It is difficult to compare annual reports; especially cash based ones, because there is no consistency between current and past years. (Interviewee E).

5.2.5.1 Performance Evaluation:

Interviewee (B) stated that SEC had an acceptable performance indicators system, which had been adopted in the East regional company. However, this system needed to be integrated and improved by using more reliable information derived from a more adequate cost accounting system.

The difficulty of setting and developing financial performance indicators appeared more clearly in SEC for a number of reasons, such as non-commercial objectives, lack of incentives, and lack of control.

A senior manager (Interviewee E) at the SEC confirmed this when he complained about the company's failure to set performance indicators in a clear format, which impeded effective examination of its performance. The company in most cases used estimates or budget reports, such as expenditure reports, sales reports, estimated revenues, and inventory reports, as performance indicators. Many senior managers confirmed this.

One manager described his organisation's performance indicators as follows:

The way we look at performance indicators is by the level of use of some or the entire budget- the percentage for every account. If our spending is just below the budget this is considered a good sign. But on the other

*hand, the new level of spending will be our actual spending level.
(Interviewee B).*

The frustration expressed in the above points to the lack of an adequate budgeting system to help achieve the organisational objectives of rationalising expenditure and obtaining sufficient control and accountability. The current budgeting system may thus de-motivate top managers and hold back their effort to look for new ideas that could increase their revenues. It is clear from the above statement that the main KPI is comparison of actual against budgets which means lot of financial indicators are used.

The overwhelming majority of managers reported non-financial indicators, e.g. the number of new subscribers, were very important to achieving their objectives. However, this high concern was not combined with cost benefit or even cost effectiveness, since most admitted these targets needed to be improved and compared with suitable benchmarks, which took into account the environmental circumstances and the culture of customers.

The majority of managers (Interviewees B, C, D, E) commented on the difficulty of using an international benchmark because of the special environment and climatic conditions of Saudi Arabia and also the lack of autonomy that held back any development.

The above suggests that the SEC had an awareness of performance indicators, especially non-financial indicators, in terms of the quantity and timing of production and also more financial indicators in terms of meeting the budget.

Although they provided justification for their current practices, interviewees from SEC did not confirm current-reporting practices satisfied their own needs and provided trustworthy information, whether for future requirements and trends or the present situation.

Thus reporting systems within SEC suffer from two shortfalls. First, the kind of information that is used, which is mainly engineering-based, containing much technical detail without providing enough financial information. This could be due to the lack of accounting techniques, and the nature of costing systems in use.

Secondly, the natures of internal users who are top managers are mainly in SEC engineers who primarily ask for technical engineering information. At the same time

Government related personnel tend only to focus on providing services within technical specifications and within predetermined financial allowances.

5.2.5.2 External and Internal Auditor:

Saudi Commercial Law requires that companies use two external auditing firms for auditing and approving company financial statements. SEC has two private Saudi auditing firms and an Auditing Committee⁴³ responsible for reviewing and approving the financial statements before they are taken to the external auditors.

In addition, since SEC has considerable government shareholdings, the GAB (General Audit Bureau) has a role and control over the company. The majority of managers in SEC expressed dissatisfaction with the ineffectiveness of the GAB's role and control over the companies: GAB auditors failed to see major problems because they lacked an overall picture of an organisation's practices and their role and its employees' qualifications are limited (Interviewees A, B, D, E).

The GAB's audit is considered a documentary or legal audit since it only looks at statutory issues. As a governmental unit, GAB officials suffer from a number of shortcomings, including lack of incentives, ineffective independence, weak training, and the civil service salary system, which possibly weakens the Bureau's ability to attract the best, most competent new staff (Interviewee A; Aba Alkhail, 2001).

5.2.5.3 Capital Expenditure Management and Investment Appraisal:

SEC was a state-owned enterprise following the rules and orders of the Saudi Government. Before privatisation SEC had no autonomy to manage its capital or its investment, but once it was privatised it became a partly self-funding company. SEC can now look for new projects but whilst it has enough autonomy to decide suitable projects, it still has to gain ultimate approval from Government. Usually the Government will not reject any project proposal unless the project is going to be based outside of the country. This is deemed to be for 'political reasons'. (Interviewee A).

⁴³ The Committee members are part of the Board of Directors.

One manager (Interviewee B) stated that the majority of SEC projects proposed directly and sometimes indirectly by the government were for social reasons. He mentioned that the government sometimes asked the company to provide services to certain areas that led the company to raise the need for new projects to extend its ability to meet the required services.

It can be argued that some projects that SEC accomplished have had no positive cash impact on the organisation since they were proposed by the Government to serve some social, non-profitable areas.

An interviewee summed up the difficulty that SEC face with any new project:

The problem with the electricity sector is that it is very related to politics so once you want to make any move you have to prepare yourself to face not only other companies but also maybe other Governments. We have a proposal for a project in another Arab country, very profitable, and it will help the company but now the negotiation is in the hands of the Saudi Government with that country. All what we can do is wait, maybe we will do it and maybe we won't. (Interviewee, B).

All new proposed projects involve the much-needed expertise of both engineers and accountants in SEC. Together engineers and accountants look for costs and benefits in the early stages of a project's proposal. Then the engineers take full responsibility to convince the Board of Directors through the Head of the related department (Generation, Transmission, and Distribution). Once the Board of Directors approve the new project, the head of the Board and the President of the company and the Executive Vice President for the related department have to take the new project to the Ministry of Electricity to gain their approval and sometimes ask them to facilitate it financially (Interviewee, D).

5.2.6 External Environment:

As we argued before SEC was part of the government, which was controlled financially by the Ministry of Finance. However, not all the electricity companies were under the direct control of the Ministry of Finance.

After privatisation, the situation in SEC did not change a great deal in relation to Governmental agencies such as the Ministry of Finance and the Ministry of Electricity. It is noticeable that the two Ministries still have huge involvement in different aspects of company policy.

Pricing policy is the first aspect since SEC has no autonomy on its services prices. The Government (MOF) will compile a list of services prices and it is usually the case that this leads to loss – in which case the Ministry will make it up to the company by paying the difference. Additionally, the Ministry of Electricity must approve any new projects and formulate key objectives and goals for the company. The company has to follow these mandates in order to make its own, more detailed objectives.

In 2004 the Saudi Government announced the establishment of the Electricity & Co-Generation Regulatory Authority (ECRA). The objectives of this Authority were to ensure that supplies of electricity were provided to consumers in the Kingdom were adequate, reliable, of a high quality and were priced fairly.

The ECRA established what it called The Electricity Law in 2006. The Law is

Central in the regulation and development of the electricity sector in the Kingdom. The general features of the Law cover provision of reliable services, protecting consumer's rights including reasonable prices, while protecting the rights of investors in the sector to receive a fair return (www.ecra.gov.sa).

It is obvious from the above that the establishment of ECRA was an action by the Government to move responsibility from the Government to a Regulatory authority to enable it to deal with the electricity sector. Although it would appear that ECRA is now doing the same job as the Ministry of Electricity it is nevertheless a positive step toward opening up the market and allowing competition.

For SEC the situation is much the same since the Regulating authority is still doing the same job as the Ministry with regard to pricing and new projects.

As one manager in SEC states:

We were dealing with only the Ministry of Electricity with regard to everything, but now since they established the Electricity Authority we have now to deal with both of them, the Ministry and the Authority. We

*know it is a temporary situation until they open up the market.
(Interviewee D)*

A second manager at SEC showed his dissatisfaction with the ECRA as he stated:

*We now have ambitious plans for our company but these plans are always faced with the bureaucratic systems of the ECRA and the Electricity Ministry. For example, we have a plan to restructure our company based on separating the three main organizational Units (Generation, Transmission and Distribution) to be companies under the Saudi Electricity Company. We also want to have a competitive market so we can have different companies, especially in the Generation and Distribution sectors. All these plans need hard work and healthy environment to attract other private companies. ECRA and the Ministry need to have radical changes on: 1) The pricing policies as they need to let the market decided the prices so companies can make profit by its production not by the support of the government; 2) The Government needs to provide opportunities for the Generation sector since it monopolizes this sector claiming it is for political and security reasons; 3) Give us the freedom to run the company in a commercial way.
(Interviewee A)*

The above statement shows how the some of the top managers in the company are not satisfied with their relationship with Governmental bodies and are requesting more freedom and autonomy. This demonstrates that the SEC is still restricted by rules and the Government's continued significant involvement. However some of the managers are optimistic and think only a few more steps are needed to get the reforms the company wants. (Interviewee H).

The only positive change in relations with the external environment is with that of the Banks. SEC after privatisation, and particularly in the last three years since 2006, now has the ability to negotiate with private banks for loans based on commercial activity. However SEC is still only allowed to take this action after gaining the approval from the Ministry of Electricity for the project and for the loan. For banks it represents a good business opportunity since the Government will implicitly guarantee the company.

An interviewee from the Saudi Investment Authority stated that:

For anyone who doesn't know the real situation for the company, SEC looks like a very normal private company. In reality, its situation is so complicated. You can say it is private and you can say it is governmental. For us we recommend any foreign investor who wants to buy shares in Saudi stock to buy SEC. We also recommend them to invest in any

project related to electricity such as when, from time to time SEC proposes building generation units⁴⁴ around the country. But most of them are always concerned about the influence of the Government on the company as well as the lack of competition and free market.

The type of project mentioned in the statement above is extremely typical. The company is trying to encourage as many private investors as possible to become involved in its development plans and help make payback for these projects easier.

5.2.7 Organizational Structure:

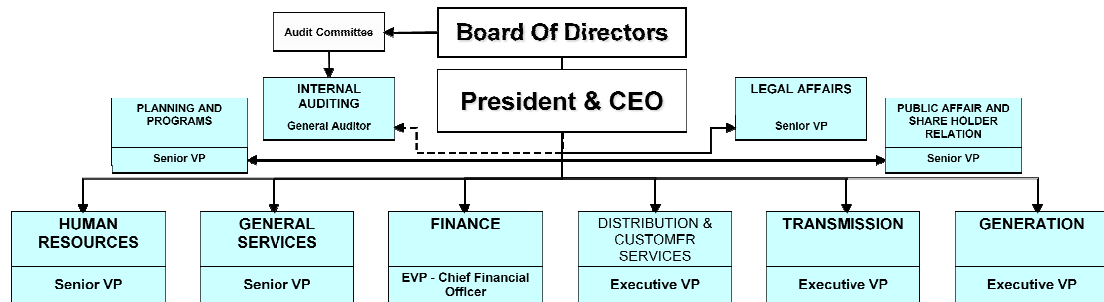
As discussed earlier, until privatization 10 separate companies provided electricity services and undertook Government projects. After privatization one of the biggest problems facing SEC (which was now only one large company), was that of how to restructure the company. Each company from the ten had its own structure and whilst on the surface they appeared very similar with regard to job titles and descriptions, they were in fact totally different in terms of salaries and qualifications needed for the positions. For example, the East Region Company had the highest salary and it required very high qualifications. For this reason, it took SEC three years to come up with a proposed final structure for the company (after a several proposed structures and lots of rejections from the Ministry and Board of Directors) (Figure 5.6).

At the beginning of 2003, the Board of Directors approved a new organizational structure, which was to be phased in gradually. The design of the structure was based on specialized activities such as organizational units, i.e. electricity activities, related activities and the supporting services needed to reinforce the overall company performance.

During 2003, phases 1 and 2 of this new organizational structure were put into effect; sectors and departments were specified and relevant job descriptions were outlined.

⁴⁴ These projects are based on private companies building generation units around the country, SEC subsequently agree to buy the power they produce for a certain length time. After the agreed time the company then takes over the unit.

Figure 5.6 SEC Structure



Sources: SEC Documentations, 2007.

It can be seen from the figure that SEC had designed its structure based on the services they provided, which were Generation, Transmission, and Distribution. However there were reservations about the restructure of supporting departments since they had the enormous task of dealing with all three main units. The proposal now being discussed is that the three units should become separate companies, each with its own supporting service department.

5.2.8 Cultural Changes:

One of the main problems for the public sector enterprises in Saudi Arabia is the mindset of its employees. Employees in the public sector suffer from a bureaucratic mentality, which resists change and is very slow in accomplishing tasks (Interviewee H).

In addition, due to the reverence paid to engineers by the majority of Saudi society in the past (see section 3.5) the electricity sector was dominated for many years by engineers in all decision-making processes.

After privatisation, SEC still suffers from the above problems. In fact, as the Government still has very significant control over the company: key positions in the company, namely the top managers (the President and the members of the Board of Directors) are still appointed by the Government and most of them are former or current Government employees. As a result SEC is unable to change the mindset of its employees. Since top management shares the same ‘mentality’ as other employees there is no initiative for change.

It was noticeable for the researcher, when visiting the headquarters of SEC that it was a Government facility – not in terms of the new offices and other buildings, more in terms of the way people dealing with him and how they worked. For instance, emails were hardly in evidence in any formal communications, the preference was for paperwork which consumed a great deal more time, effort, and money.

Furthermore, SEC still suffers from the domination of engineers over most of key positions except the Finance Department.

This was a worrying aspect for an accountant in SEC who complained about how difficult it was to deal with non-financial people:

In a lot of times we suffer from misunderstanding between top managers and us. They find it so difficult to understand our financial data that we provide them with. Most of the time they prefer technical terminology. We can't complain because they are the ones who make the changes as and when they want to. (Interviewee G).

This is logical since most of the key people in the organisation are engineers. However, the situation does seem to be changing on this issue: significant change in Board of Director qualifications has now led to approx. 50% of members having finance and economics qualifications (Table 5.2). This radical change in structure may encourage further change for future employees and the need for more finance and accounting oriented qualifications.

Table 5.2 Qualifications of Board of Directors Members on SEC

Saudi Electricity Company	
No	Qualification
1	B.A in Electrical Engineering in 1982, MSc in Electrical Engineering in 1985, PhD in Electrical Engineering 1989
2	Former president of SEC.
3	B.A in Electrical Engineering, MSc in Electrical Engineering
4	B.A in Computer Science in 1990, MSc in Computer Science in 1994, PhD in Computer Science 1998
5	B.A in Economics, MSc in Economics in 1980, PhD in Economics 1985

6	B.A in Industrial Management in 1982, MSc in Economics in 1993.
7	B.A in Accountancy in 1981, MSc in Accountancy in 1983.
8	B.A in Accountancy in 1973, MSc in Public Administration. PhD in Public Administration in 1981.

Source: SEC Documentations, 2008.

In addition, one of the main problems with SEC's is that its employees are less open and have the government mentality, which consider all information as a top secret information and cannot provide anyone with it. This problem was the main problem that faced the research when meeting people in SEC as they gave him access to fewer members of staff even the research had a personal and friendship relationships.

5.2.9 Human Resources Development and Reward Systems:

Before privatisation the electricity industry suffered from different problems compared to those of telecommunications. These were overstaffing, qualifications of employees, salary, and employees' performance evaluation (Interviewees B, C, D, & I).

On the issue of overstaffing, SEC since privatisation has had enough autonomy to reduce its employees in two ways. First the company has started to reduce the non-Saudi employees and replace some of them with Saudi employees. The second is to plan to reduce the total number of employees.

One manager describes the situation of overstaffing as follows:

When the SEC was established, we had duplication of staff and lots of people doing the same job. This was understood, as there was more than one company. But now we are only one company. (Interviewee C).

The company plans to shed employees by offering them generous compensation packages. So far the company has managed to reduce the total number of employees from 31000 in 2000 to 27,601 in 2009 (SEC documentation, 2009).

On the issue of employee qualifications, the company has managed to attract some qualified employees from different companies, although still mostly engineers.

However, the company has been able to attract experienced and qualified employees to its headquarters in Riyadh.

One manager described how the lack of suitably qualified finance employees affected his region:

When I go to headquarters in Riyadh and see employees there I feel that the company has changed. They understand your requests and they can translate it financially. Nevertheless when I come back to my place I see the same company that I have known for 20 years. People here are same. (Interviewee I)

To try and improve the situation SEC has plans to improve the level of its financial employees around the country. It has started with staffing at its headquarters and is now moving out to its regions (Interviewee A). As highlighted in Table 5.2 earlier, change in educational profiles has reached Board of Director level with now almost 50% of members possessing Business related qualifications.

When privatisation took a place SEC also had a very major problem regarding employees' salaries. Some regional companies had considerably higher salaries for people in similar positions compared to others e.g. employees in the Eastern company earned more than double compared to their counterparts who were doing the same job in the Southern company. This issue took over two years to resolve and for the company to come up with a new salary system that satisfied all its employees (Interviewee I).

One manager commented that:

Before privatisation, as an employee at SEC, all that was needed was to come to work, do what you were asked to do, and it didn't make any difference if you did it sooner or later. All that mattered was to be nice to your superiors, stay in your job and hope that you would get promoted. (Interviewee I)

The above statement describes the situation in SEC before the privatisation. Unfortunately this situation still predominates. Interviewees I, G, D & B complained that it was all about relationships with superiors.

From the above, it is clear that there are no clear performance evaluation indicators for SEC's employees. Reasons for this are (i) there are no clear and specific goals and objectives for each employee and (ii) the old Government mentality remains in the regional branches of SEC.

5.3 Summary:

This chapter aimed to explore the changes in aspects of the MACS in both privatised Saudi companies, STC and SEC. This chapter used the aspects of MACS presented by Uddin (1997) and Ferreira (2002) and the three elements of organisational context t provided by Flamholz, Das and Tsui (1985). These aspects and elements were used as the basis of all interviews with all managers and accountants.

This chapter found that both companies responded to privatisation and MACS in both companies have changed. It was clear that MACS in STC had positive changes and had improved dramatically. On the other hand, MACS's response in SEC to privatisation was weak, and changes in its MACS were very limited.

The next chapter will discuss the reasons other than privatisation that affected MACS in the two Saudi privatised companies. The discussion in the next chapter will compare e aspects of MACS in both companies in order to identify the differences between them. Then the factors that have had an impact on MACS will be presented.

Chapter Six: Discussion

Introduction

This chapter presents a discussion of the key findings from chapter 5 and a critical analysis of the secondary documents provided by the STC and SEC with regard to their management accounting control systems. The discussion is guided by the research objectives that were set out in chapter four. Based on the findings of this study, the chapter also presents a model of the factors that affect the MACS and presents suggested changes that privatized companies should take to improve the efficiency of their MACS.

6.1 Changes in Both Companies Due to Privatization:

As we discussed in earlier chapters, Uddin (1997) provided a model of five aspects that were intrinsic to any management accounting control system. Specifically these were: (1) organizational objectives; (2) budgetary processes; (3) incentive systems; (4) accounting systems; (5) effectiveness. Ferreria (2002) added a further two aspects that were intrinsic to the MACS, viz. (1) the Balanced Scorecard (BSC) and (2) costing systems.

These above direct aspects were investigated alongside the three elements of organizational context identified by Flamholz, Daz and Tsui (1985) (organizational structure, organizational culture, and external environment) in this research.

All three sets of researchers claimed that there would be changes to these aspects as organizations moved from public to private status. Although this research originally used the 10 aspects as a framework, as a result of the research, the findings showed that other factors also contributed to the changes identified.

In particular, the influence of competition (growing competition in the marketplace), the changing relationship between accountants and engineers, and the extent to which

government restrictions were eased had considerable influence on the extent of change within the two respective organizations' MACS.

The discussion now will turn to comparing the findings from both organizations regarding each of the 10 aspects mentioned. The format throughout is to examine the effects of change of ownership (privatization) in management accounting control systems in both privatized Saudi companies STC and SEC and subsequently identify the reasons for the differences between the two companies in terms of their development (if any differences exist).

6.1.1 Organizational Objectives:

Before privatization both STC and SEC had key objectives that were formulated and set by the government, based predominantly on social and political factors and with very little consideration to commercial factors.

After privatization STC had autonomy in setting its own objectives and these were based on clear and achievable commercial outcomes. Significantly, management at all levels was involved in this objective setting process. According to the employees that were interviewed, the reasons for this autonomy and inclusion in the decision making process was the existence of competition, as competition forced the company to work in a commercial way. According to interviewee (I)

For the company to survive in a competitive market it should function on commercial bases which means starting first with setting up achievable commercial objectives.

In addition, another reason was the reduction of government involvement in the company's policies and systems. One of the interviewees (D) explained that governmental employees in Saudi Arabia couldn't think commercially. He stated

When we were government, all people were concerned was with pleasing the government by achieving its political and social objectives. Also people were bureaucratic and slow in the decision-making process.

At the same time, however, in SEC the main key objectives were still set by the government. The major difference was that in SEC the government still had huge involvement in the company, specifically due to the social and political importance of providing electricity to the nation: whereas people could hypothetically do without telephones and computers in Saudi Arabia, a continued supply of electricity was considered essential. In addition the 'nature of the sector' encouraged the government to free the telecommunication sector and monopolize the electricity sector. It can be argued that the technologies of telecommunication make the sector competitive in its nature and cannot be monopolized.

However, in terms of future developments and based on a press statement from the Minister of the Electricity, the government now has plans to open the market for other companies to invest in the electricity sector (Alriyadh Newspaper, 2010). This will force the government to ease its influence in SEC by allowing it autonomy in setting its own objectives to maintain a competitive position.

6.1.2 Budgetary Processes:

Before privatization the government prepared budgets for both organizations; however, these budgets did not reflect the real financial situation of the companies and were not used for internal control purposes. For example, budgets could not be offered as supporting documents to banks to get loans since they did not present a true financial picture.

After privatization, STC, as a result of setting its goals and objectives, had full autonomy to set its own budgets. Budgetary processes are now seen as a useful tool for management control within the company. In addition budgets in STC are used to help the company identify responsibility and accountability in each department since the directors of departments are directly involved in setting them.

SEC on the other hand, still has to gain final approval from the government since in most projects the government still provides the funding and maintains responsibility for

initiating any new projects. This is an indication of the continuing huge involvement of government in SEC and its policies.

6.1.3 Incentive Systems:

Before privatization both STC and SEC had incentive systems based on wage structures that were imposed by the government. Employee performance evaluation was bureaucratically based and depended more on personal relationships and time spent in the workplace than on effectiveness. These problems created a lack of creativity and incentives for improvement in both organizations.

After privatization, and as a direct result of the autonomy given to the company from the government to set its own systems and policies, STC changed its salary and promotional structure to one based on employee performance and educational background. Employees were therefore motivated to become more creative and concerned about achieving the goals of their departments and the company in general. In turn, the company was now keen to attract well-qualified people into the company. Whilst the autonomy that was given was a direct result of a more competitive marketplace, the response from employees meant that the company was able to maintain and improve its competitive position.

On the other hand, SEC still remains in a governmental wage structure, with promotion very much based on personal relationships as a direct result of the government's continuing involvement in company policy. Thus SEC continues to be run by government employees with a public sector mindset, caring only about:

Coming to work, doing what you were asked to do regardless of the efficiency, time, and cost of it, and making your superiors happy (interviewee, I).

This attitude can be linked directly to an absence of clear objectives for employees and unclear personal targets.

6.1.4 Accounting System:

Before privatization both STC and SEC had accounting systems based on government regulations with the sole purpose of ensuring that the money had been spent as agreed by the government.

After privatization STC changed its accounting system to a more commercial basis in order to provide other functions such as control and decision-making. The company changed from cash to an accruals base, as Saudi Commercial Law requires it.

In addition, accounting information in STC changed to contain both financial and non-financial information and was used for multiple purposes such as performance evaluation and control purposes. Information subsequently included in internal reports had more of financial basis than before privatization, such as ‘the cost or the benefit of a new station’ used to be, whereas it used to be more engineering based information, such as ‘the capacity of a new station’. This was due to changes in the personnel preparing reports and those who subsequently used them, i.e., the decision makers, as the company experienced the growing involvement of accountants and finance employees in the preparation of reports compared to that of engineers.

Furthermore, because of the autonomy that STC had, it became a self-funding company, able to initiate new projects and use up-to-date techniques for investment appraisal.

Post-privatization SEC, on the other hand, changed its accounting system to an accrual basis since it was required by Saudi Company Law in its capacity as a joint stock company to prepare its accounts in this way. However the company still suffers from huge accounts receivable, and weak performance evaluation indicators with little use of non-financial indicators. In addition it still has to gain approval from government for any major projects since, in most instances, they still initiate and fund these projects.

All of the above problems indicate the continuing involvement of the government in SEC policy making. However, if the market was opened up, these could be solved, as with STC and competition as a driving force for change. Nevertheless, in SEC engineers still prepare most of the internal reports since the key decision makers using

this information are still engineers. This gives an indication of the continuing relationship between accountants and engineers where engineers are still the more powerful.

6.1.5 Effectiveness:

Before privatization both STC and SEC measurements of effectiveness were based on their achievement of governmental goals and objectives and not profitability; use of sophisticated performance evaluation indicators was limited.

After privatization STC based its effectiveness on measuring profitability and used more sophisticated performance evaluation indicators containing financial and non-financial indicators (for example, NPV and customer satisfaction surveys). Once again, autonomy and a competitive marketplace were the driving factors for this change.

SEC remains in same position as before privatization with little improvement in its financial performance evaluation indicators. The company is still measured partly by achieving government objectives and partly by achieving its own company objectives, due to the mix of its objectives as discussed earlier in (6.1.1). For example, SEC was asked sometimes by the government to provide services to non-profitable areas and the company would be measured on its achievement of this target, even if it was not profitable.

6.1.6 Balanced Scorecard:

Before privatization both STC and SEC were following government policies and directions, which did not include use of the Balanced Scorecard (BSC).

Since privatization, which to re-iterate led to increased autonomy and motivation, STC has now adopted sophisticated and up-to-date systems such as BSC. These have now provided the company with more effective techniques for performance evaluation of employees and their activities; in addition, the company now has a specific BSC department. STC considered BSC as a clear and sophisticated system that would help the company to measure employees' performance as well as company performance. The

BSC uses clear financial and non-financial techniques for that purposes and “it is great system that you can cascade within the company department easily and clearly. It is a very good American system” (Interviewee, 1).

On the other hand, and at the time of the case study interviews, which took place in early 2008, only one person within the financial department in SEC knew what BSC meant. This gave the researcher insight into the type of person still working at SEC at that time: someone with a bureaucratic, government-based frame of mind, lacking in motivation for self-development and still following government directives.

However, of interest is an announcement by the Minister of Electricity in early 2010 that his ministry is now planning to open the sector for competition and allow foreign investors to enter the market by 2015 (Alriyadh Newspaper, 2010).

In turn this announcement was quickly followed by the President of SEC stating that his company was planning to adopt BSC as a comprehensive system for the company starting from late 2010, with a date for completion of 2014, thus providing a sound indication that pressures of competition are forcing the company to seek the most appropriate systems to improve performance and control processes.

6.1.7 Costing System:

As a result of privatization, and therefore the ability to set its own service pricing levels, STC has had the motivation to improve its costing system and use more sophisticated methods. In consequence the company has changed its system from using a traditional approach to adopting ABC, enabling the company to provide more accurate cost information for decision-making and controlling company activities.

SEC, on the other hand, lacks the motivation to improve its costing system as the government still sets prices for the company’s services and will cover the difference if costs exceed selling price.

This continued involvement of government in company policy is still causing lack of motivation for improving SEC’s costing system, using the system as a tool for

managing employee performance and company activity in the marketplace, and still results in a decision making process based on inaccurate information.

6.1.8 Organizational Structure:

Before privatization, structures in both STC and SEC reflected the government's philosophy of providing services regardless of cost and levels of profitability. For example interviewee (I) stated that:

When we were government, we were forced to provide services to small villages without any profitability just on the premise that it was government policy to do so.

Moreover, it was noticeable that neither organization had a strategic planning or costing department, since plans came from the government and costing calculations were the job of a ministry official and not a company employee.

Since privatization, STC has changed its structure three times as a result of changes in the company's main objectives. It can be seen that the first structure was based on the geographical areas that the companies serve and it was a temporary structure, as the government did not have by that time clear objectives. The second structure was based on the changes in the objectives and vision of the company, which was focused on its product range. The last structure was based on the new philosophy and objectives of the company, which were based on attracting customers.

These changes have had a direct effect on the reporting process and on the responsibility and accountability of departments. This is a reflection of the company's ability to change its philosophy and objectives as a result of volatility in the marketplace.

After privatization, although SEC modified its structure based on the services it provided (Generation, Transmission, Distribution), it did not undergo major structural change because the company lacked the motivation to improve its structure as the government still set the company's main objectives. Interestingly one interviewee (B) claimed that the changes in structure at SEC were merely a "renaming" of positions. As

an example he cited the position of the company President, which used to be occupied by the Deputy of the Minister and named as the Deputy Electricity Minister; the name was subsequently changed to be just that of ‘President’ with the same job description and duties.

It is worth noting from this case study that changes in structure are a result of changes in the organization’s objectives because of privatization. The relationship in this issue can be described as in Figure 6.1 The Relationship between Privatisation, Organisation, and Structure. This can clarify that changes in organizational structure are a response to privatization in general and changes in organizational objectives specifically.

Figure 6.1 The Relationship between Privatisation, Organisation, and Structure.



6.1.9 Organizational Culture:

Before privatization a government culture prevailed which meant that employees regarded customers as secondary to their own interests and working environment. In addition, working relationships were based on families, tribes and personal friendship and the effectiveness of these relationships resulted in promotion or non-promotion. In addition, a public sector mentality prevailed which meant that employees’ main concern was pleasing their superiors regardless of the cost and timing of their achievements. Furthermore this public sector mentality considered all information as highly classified governmental information and they worked in a very bureaucratic environment.

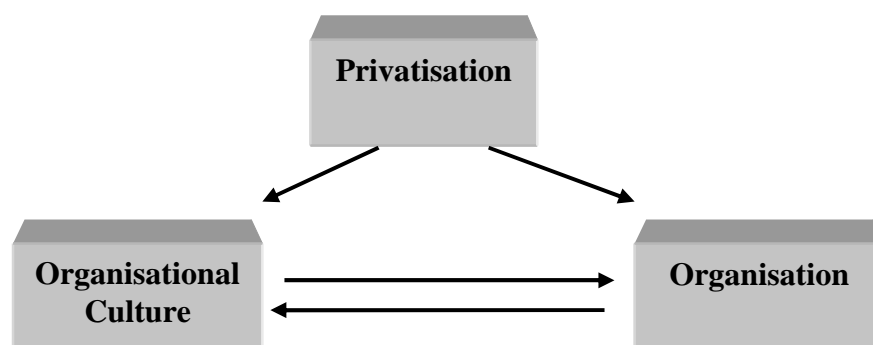
After privatization STC made a conscious effort to change the organization’s culture by providing training courses and seminars to educate employees into the ‘new way’ (of non-governmental reliance). If employees resisted change, a ‘Golden Cheque’ was given to the person in question and usually he would be replaced with someone willing to adapt to the new culture. It is noticeable that the company was forced to change the

attitude of its employees in response to a very competitive market by employing more people from accounting and business backgrounds.

On the other hand, SEC still suffered from a governmental mindset; government still had control over the company and therefore the attitude was that there was no need for change. This was the main problem that the researcher faced in collecting data on SEC, because of the remaining public sector mindset of SEC employees. Employees of SEC work in a very bureaucratic environment and they consider all information as secret government data. However, it should be noted that there was noticeable increase of the number of people who have an accounting and business background but top managers and decision makers are still engineers.

It is worth noting from this case study that changes in organizational culture can be a result of an organization's effort to change its employees' culture and a result of changes in objectives, employees' educational background, changes in the incentives system, and changes in the external environment. Therefore the relationship between organization and its culture can be described as a dual relationship, as both would be affected by privatization and would have an effect on each other (Figure 6.2).

Figure 6.2 the Relationship between Privatisation, Organisation, and Culture



6.1.10 External Environment:

Before privatization both STC and SEC were part of the government and both were only following government regulations especially those of the related ministry and the Ministry of Finance.

After privatization the Saudi government had to eliminate the Ministry of Telecommunication. After that and at same time as allowing competition in the sector, the government created a regulatory body with specific and clear requirements for STC and other telecoms companies. This regulatory body was called the Telecommunication Agency and had the main objective of providing fair competition in the market. The amount of information that the agency requires is less than before with the Ministry and it is more specific and more related to the purpose of the agency, which is to provide a fair market. Moreover STC now has to deal with different stakeholders such as shareholders and investors. Each one of those stakeholders requires different information, which has an impact on the reporting systems, costing systems, and accounting systems. For example, reports required by banks should provide different information than reports provided for shareholders. In addition, STC after privatisation has to follow the requirements of Saudi Commercial Law as the company now is a joint stock company.

After privatisation the situation in SEC did not change in relation to governmental agencies. It is noticeable that the Ministry of Finance and the Ministry of Electricity still have huge involvement in the SEC. For example, they set the prices of services and they have full access to all financial documents in SEC at any time. However the government has established a new agency to organise the electricity sector and reduce the involvement of the Ministry of Electricity, but this resulted in increasing the job that SEC has to do to satisfy both the Ministry and the Agency which consumes more time and cost. Both the Ministry and the Agency are considered as government, but they have different objectives as the government's concern is to provide the service equally to all Saudi people and the agency's concern is to organise the sector and make sure that it can be profitable, so as to be ready for competition. This resulted in conflicts about

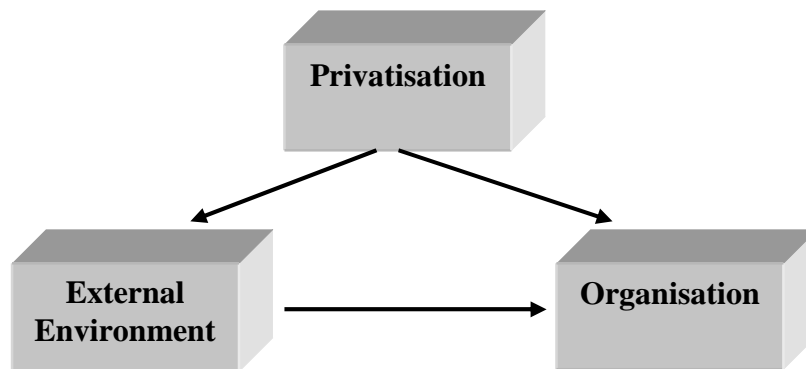
what SEC has to achieve, either provide the service equally to all people or try to be profitable.

SEC for shareholders and investors is like “investing your money with the government. It is guarantee that you won’t lose it” (Interviewee, D). This has a positive impact on the relationship with banks, as it makes it easier for SEC to obtain loan finance for new projects, as banks would consider it as lending to the government. The involvement and protection of the government prevents the company from having enough motivation to improve its systems and techniques. However, it is expected that this situation would change as the government is planning to open the sector to competition.

SEC after privatisation is considered as a joint stock company that must follow the Saudi Commercial Law. This can indicate that SEC’s external environment has changed but it has not changed as much as STC’s.

It is worth noting from this case study that the entry of privatization into the sector would cause changes to the external environment. These changes to the external environment would have an effect on the privatized organization. In other words, changes in organization would be a result of changes in the external environment because of privatization (Figure 6.3).

Figure 6.3 the Relationship between Privatisation, Organisation, and External Environment



6.2 Other Factors that have an effect on MACS:

From the above, it can be seen that STC has experienced a dramatic change in the aspects of its MACS, whilst the changes in SEC were very limited. Both companies are located and working in the same country and both of them has been through the same changes in ownership status, namely privatization, but they experienced very different levels of change. Indeed it should be noted that the government remains the majority shareholder in both companies, showing that the level of state ownership is not the most important variable.

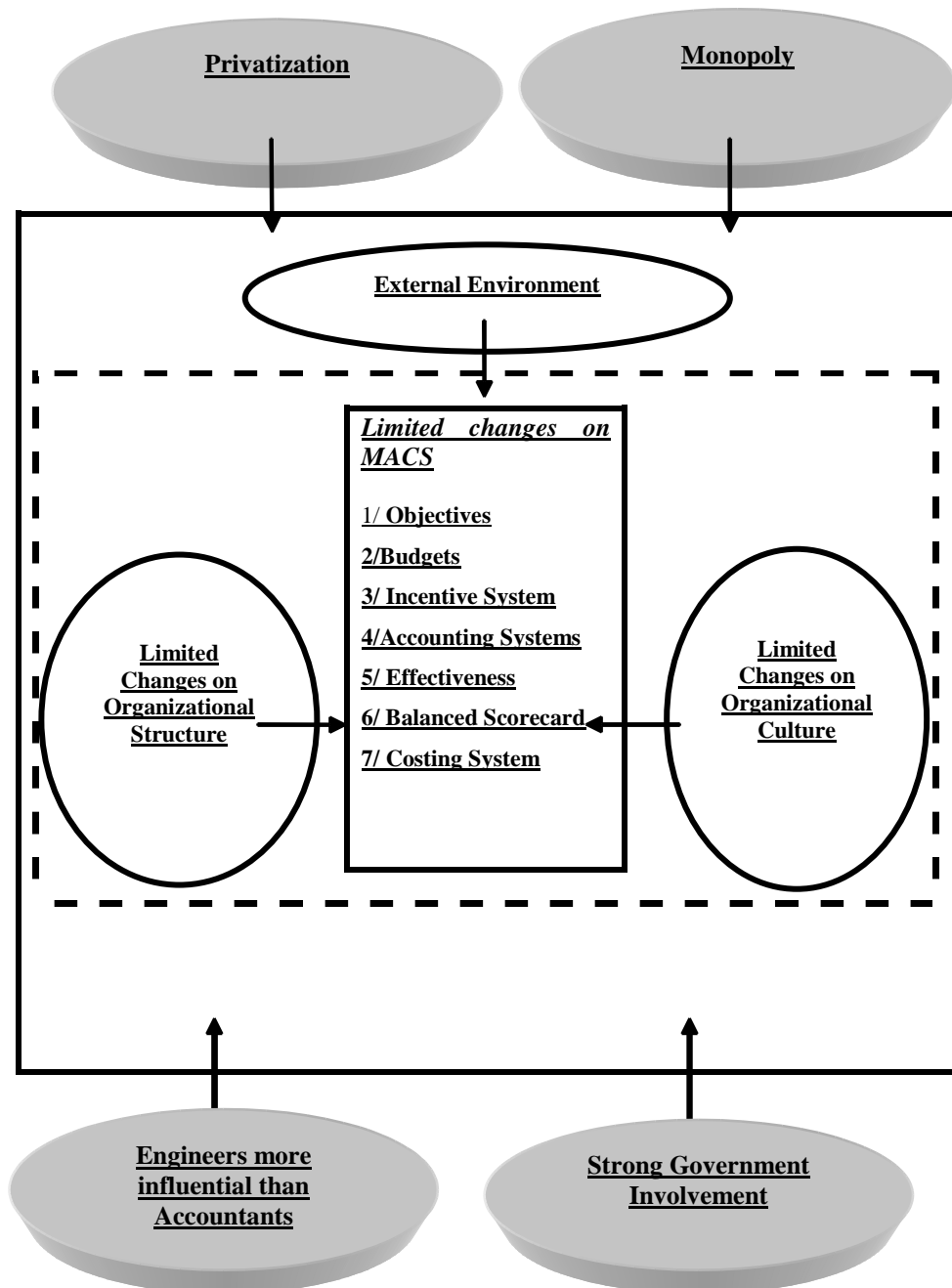
The results of the case study showed that privatization has a positive impact on MACS, but that it cannot inevitably work effectively and efficiently on its own. The study showed that organizations need, beside privatization, an interaction of other factors that can change MACS and lead to more efficiency and effectiveness. This study found out that there were three main factors that affected the level of changes in the MACS of the two Saudi companies after privatization. These three factors are: competition, the degree of involvement of the government, and the relationship between engineers and accountants (Figure 6.6).

It is notable that there is a key element that is common to all the factors that have impact on changes in MACS which is the people who are behind those changes. The main step for successful privatisation was the choice of qualified and suitable members of Board of Directors who are prepared to allow change and understand the needs for changes and how to make it happen. The kind of directors, consultants, and experts who are going to recommend and execute the changes and can run the company after privatisation in a very competitive environment is very important. The changes in organisational culture and structure are around employees and their ability to accept the changes and be accountable for the work. One of the three factors that affect MACS is the balance of power between accountants and engineers and how those people are qualified, responsible, and authorised to initiate and allow the changes in MACS.

This can be seen clearly at SEC as the people who are on the Board of Directors and serve as high-level managers still have a public sector mentality. Those people resist changes and run the company as a public sector enterprise, which prevents positive changes to MACS.

As we discussed earlier, SEC has experienced very limited changes in its MACS, as there were few factors that motivated the company to respond to changes in its ownership status. In the situation of the Electricity Sector there was a total absence of competition as the only company that worked in the sector was SEC. In addition, the Saudi government exercised major influence on the company's policies and objectives. Moreover, engineers were the most powerful managers in the company and most of the decision makers were engineers (Figure 6.4).

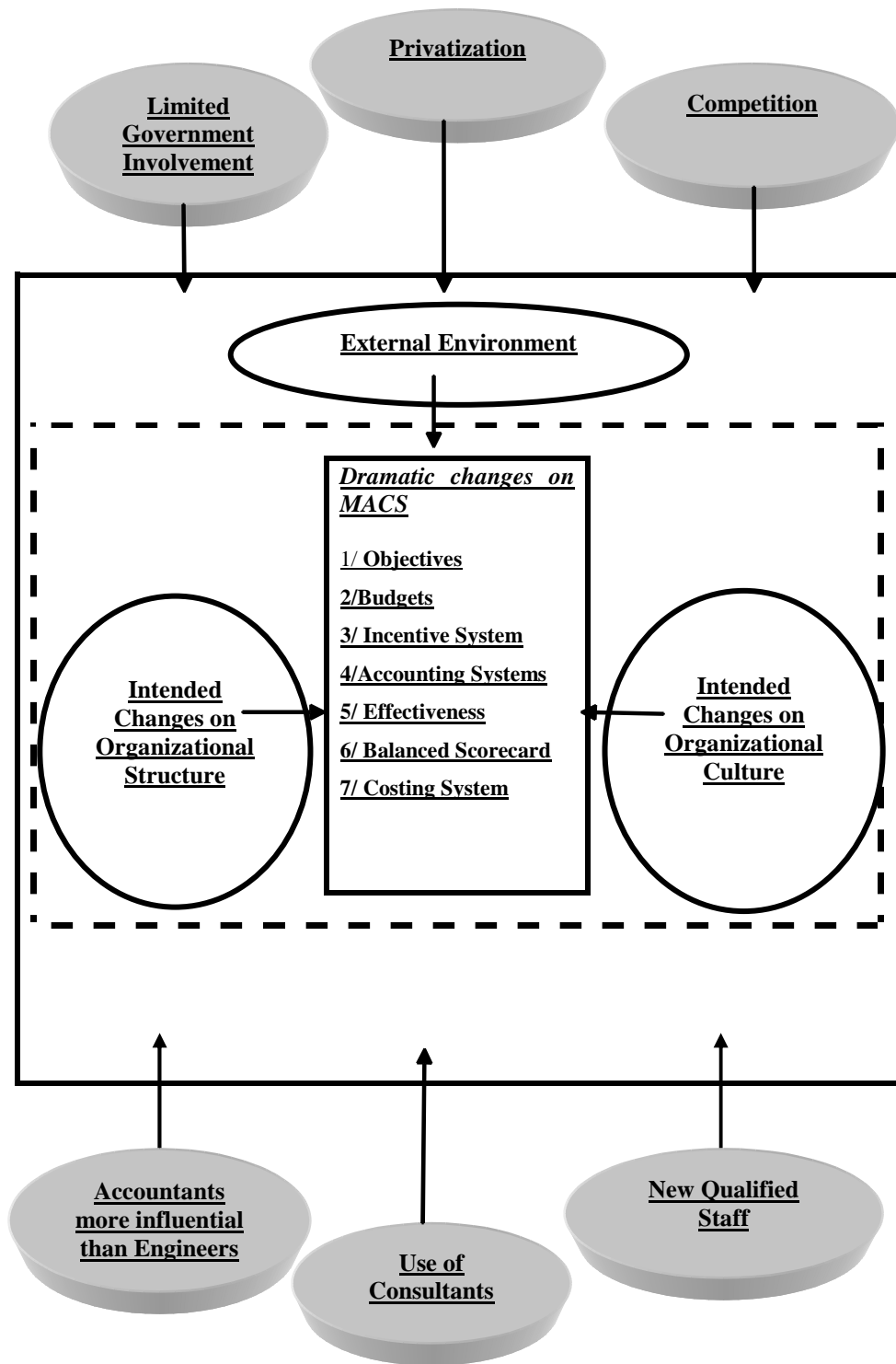
Figure 6.4 Factors that affect MACS at SEC



On the other hand, one of the first steps in the privatisation of STC was changing people in high positions. This helped the company to initiate changes in its MACS and improve them.

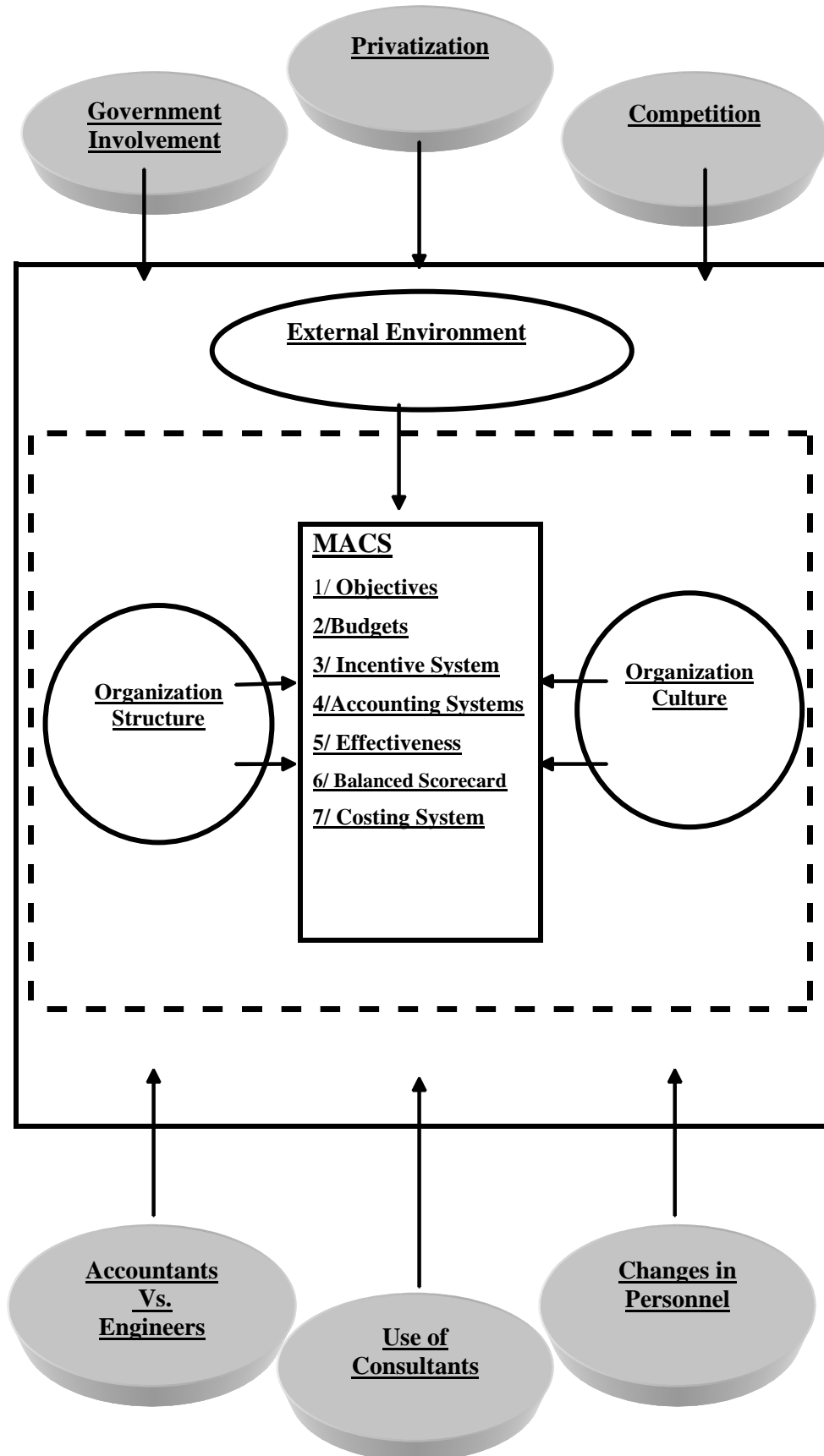
It can be said that STC has noticeable positive changes in its MACS, as there was dramatic application of the factors that motivated the company to respond to changes in ownership status. In the situation of Telecommunications Sector there are now three other companies that function in the sector, which makes the environment very competitive. In addition, there is very limited involvement of the Saudi government on STC policies and objectives and the role of the government has changed from a decision maker to become more of a regulator. Moreover, accountants are more powerful than managers in the company and most of the decision makers are accountants and finance employees (Figure 6.5).

Figure 6.5 Factors that affect MACS at STC



Combining the results from the two companies SEC and STC Figure 6.6 presents the model that this study concludes with. The model shows that the three elements of organization context can affect and be affected by the seven aspects of MACS as was argued by Flamholz, Daz, and Tsui (1985), Uddin (1997), and Ferreria (2002). In addition all aspects would be affected by privatization alone (Uddin, 1997; and Ferreria, 2002). But this study adds another three additional factors that would affect MACS, which are: competition, government involvement, and the relationships and balance of power between accountants and engineers.

Figure 6.6 Factors that affect MACS



6.2.1 Competition:

It was clear from the previous discussion that competition had a positive impact on STC. Opening the market was the motive for STC to change its objectives to be more commercial, change its budgetary process and use it as a control tool, attract more qualified employees and measure their performance based on achievement of their objectives. Competition was the motivation for STC to change its accounting system and overcome all its accounting problems. This can be noticed from when the company had problems with the government in accounts receivable and accounts payable before privatization. These problems remained the same after privatization but when the competition entered the sector the government was forced to find a solution for this problem by dealing with STC as an independent private company. Moreover, STC established a small division within the financial department called the forecasting division, which is concerned with market forecasts. This division was created after competition entered the sector and it is, as one interviewee stated (Interviewee, 8), that without competition STC would not make any market forecasts. Competition led STC to apply up-to-date and sophisticated systems that can improve the performance of the company and keep it competitive such as ABC and BSC. This supports what Kaplan and Norton (1996b) argued about companies' need to use measurement and management systems derived from their strategies and capabilities, if they want to survive in a competitive market. Competition forced STC to attract more qualified accounting and business professionals to enable the company to compete in the market. Competition forced STC attempt to change the beliefs and attitudes of its employees to be more market focused.

On the other hand, SEC still runs in a monopoly sector, which removes from the company the strong motivation which competition brings. During the data collection for this study the researcher noticed the importance of competition as a motivation for improving systems and processes. This derived from the frequently given answer that the researcher received when he asked about the reason for not changing; the answer was "Why should we change? We are happy as we are". This indicates the lack of motivation for change. In addition, it is noticeable that when the government announced that it would open the sector to other companies, SEC announced that the company

would apply BSC as a comprehensive system for measuring the performance of the company and its employees.

The relationship between competition and the two Saudi companies STC and SEC matches the claims of Aharoni (1991), who argued that the improvement of efficiency in an organization is more likely to be the result of a strengthening of the influence of market forces than of changes in ownership. He claimed that privatization alone, without the introduction of competition, may simply transform a public monopoly into a private monopoly and this is exactly the situation with SEC. Moreover, Conrad (1999) argued that once privatization is introduced in a country, competition should be introduced as well. This contrasts with the results of this study, as the telecommunication sector kept its monopoly status for almost 5 years after privatization and the electricity sector is still a monopoly, which means that it is not inevitable that the existence of privatization brings competition to the market. Bringing competition to the market can be the result of the reduction of the degree of the government involvement in the market, which will be discussed under the following subheading.

6.2.2 Government Involvement:

When the Saudi government privatized STC, but before allowing competition into the sector, it reduced its regulatory requirements and allowed more autonomy to the company. This reduction in regulation was greater after competition was allowed. This resulted in having clear and commercially based objectives for the company, autonomy in preparing budgets and using them for control purposes, creating a new incentive system based on employees' performance, allowing changes in the accounting systems and making it possible for the company to deal with the government as a normal customer and shareholder, autonomy in setting the prices for its services, which led to the introduction of sophisticated costing systems, using comprehensive and sophisticated performance measurements techniques and systems such as BSC. The reduction in government involvement allowed the company to respond to the changes in the market and provide the company with the motivation to change its structure to be more market responsive three times, and gave the company the flexibility to adopt new systems and provide new services and initiate new projects.

On the other hand, SEC still suffers from the huge involvement of the government in the way the company is run. This prevents the company from having the motivation to improve itself. This was noticeable when the researcher did his data collection on SEC, when he found most of the employees seeking to keep the government happy by just following orders without thinking creatively or trying to improve themselves. The remaining involvement of the government in the SEC contrasts with the argument that was initiated by Uddin (1997), when he claimed that privatization would reduce government involvement in company policies, whereas it supports the claims of Jones and Pendlebury (1988) that the involvement of government in setting organizational objectives leads to conflicts between the organization's and the government's objectives which consequently reduce the speed of improving the aspects of MACS. The involvement of the government restrains the organization from improving its financial systems and attracting more accountants and financial employees, which leads to an uneven power relationship between accountants and engineers, which will be discussed under the following subheading.

It can be argued that the reduction of government involvement can be considered as a result of competition. The situation of STC can be considered as evidence of that, as once the company faced real competition, it had to have more autonomy and, for example, had to sort out its huge receivable accounts relating to the government and "special people", as the company could not otherwise be competitive.

In most Less Developed Countries competition entered the sector as a result of the pressure of other countries and the World Bank to allow privatization and improve the economy (Uddin, 1997). Therefore, the reduction of the government involvement would be a result of competition. Nevertheless in the case of Saudi Arabia, which had no outside pressure for privatization, the government was willing to reduce its involvement and allow competition into the country.

6.2.3 Accountants vs. Engineers:

The change in the kind of information that was provided in control reports in STC was a result of changes in the people who prepare them and the people who use them (decision makers). Before privatization most of the reports that were prepared by engineers used very technical engineering language and terminology without paying attention to financial concepts such as the cost and the revenues of the services or the station, for example. This information should be now after privatization in a financial format even if it is engineering information (Interviewee, 11). Most engineering managers had had courses on financial reports and have at least one financial employee in their department.

In STC after privatization, there is more reliance on accounting and financial information rather than an engineers and technical information. For example, the concern about the technical engineering terms of services and the description of the new station that will be established were changed to be more concerned about the cost and revenue of the new services and the cost of the new station and its revenues. This reflects the power that accountants and finance people now have within the company. This resulted from the changes in the structure and manpower in the organization. For example, the Board of Directors changed from 100% engineers and governmental employees to a majority of accountants and businessmen.

On the other hand, in the SEC the majority of the members of the Board of Directors are still engineers or governmental employees. This affects the ability of the company's decision makers to understand any proposed changes in the MACS, especially any new system or techniques.

Another interesting issue is that as one of the interviewees (Interviewee, B) claimed:

Sometime I wish I were an engineer in this company. People here do not know what sort of job we do, and how important it is. But if you are a new engineer they will respect you and you have great personal relationship within the company.

The above statement reflects the respect for engineers over accountants that lead to the company following engineers' requests rather than accountants'. This can be a reason for sometimes rejecting changes proposed by accountants. An example for that was the reaction of all managers that were interviewed in this study about BSC as no one except one accountant new about it.

6.3 Summary

This chapter has presented a discussion of the major findings of this study derived from the qualitative findings and from internal reports and other secondary documents provided by the two Saudi privatised companies, STC and SEC, with regard to their management accounting control systems. The discussion is guided by the research objectives that were set out in chapter four. Based on the findings of this study, the chapter presents a model of the factors that affect MACS and suggests changes that privatized companies should take to improve the efficiency of their MACS.

Chapter Seven: Summary and Conclusion

Introduction

The research presented in the preceding chapters comprises an analytical study of changes in Management Accounting Control Systems (MACS). The intention of this study was to conduct a thorough examination of the changes on MACS in two privatised organisations in Saudi Arabia.

In recent years the MACS has attracted considerable interest, in practice as well as in theory. A great deal of literature on the MACS concept and its relationship to changes in ownership status (such as privatisation) has been published. Several surveys and studies indicate that the MACS have changed because of privatisation, but as privatisation is a new concept in developing countries such as Saudi Arabia, this research was designed to investigate the impact of privatisation on MACS in Saudi Arabia.

To address these issues, the following research objectives were developed:

- 6 To investigate the nature of change in management control systems in the two post-privatisation Saudi companies;
- 7 To determine the factors other than privatisation that led changes in the management accounting control systems in the selected companies;
- 8 To examine whether privatisation improved management accounting control systems or not;
- 9 To examine the impact of cultural, political and structural factors on the changes in the management control systems of Saudi privatised companies;
- 10 To propose recommendations drawn from the findings relating to Saudi privatised companies that might assist the government of Saudi Arabia when it privatises another organisation.

The aim of this chapter is to provide a review and conclusion of the entire thesis. The chapter summarises the main findings from the research and sets out conclusions, which can be drawn in each of the main areas. It also provides recommendations that might be of interest and assistance not only to the organisations studied but also to other organisations and governments, in bringing about improvements in management accounting control systems and sets out the contribution to the advancement of knowledge together with opportunities for further research. It also acknowledges the limitations of this study.

7.1 Summary of Thesis Content

This section summarises in turn the contents of each of the chapters of the thesis.

Chapter One presented an overview of the area of the study, research objectives and questions, methodological framework, importance and organisation of the thesis. The chapter presented several reasons for conducting this study. The most important reason was the lack of empirical literature and clear understanding of management accounting control systems in privatised Saudi Arabian companies. Hence, the thesis bridges the gap between theory and practice since this is the first major study ever to focus on MACS and changes that have taken place in them as a result of privatisation in the context of Saudi Arabia. It also investigates what other factors might have also influenced those changes.

Chapter Two provided an overview of the setting of the study, i.e. Saudi Arabia, and discussed the geography, demography and governance of Saudi Arabia and reviewed its business environment by looking at the major economic developments affecting it. The chapter examined the reasons behind the recent privatisation programme and its implementation. The chapter examined other experiences in some developed and less developed countries to investigate similarities or differences as bases for comparison. The chapter concluded that because of the special situation of Saudi Arabia as a less developed but rich country with a reasonably developed economy, this thesis would not expect the Saudi Arabian experience to mirror that of any other country.

Chapter Three gave a detailed explanation of management accounting control systems, and the impact of privatisation on MACS. It started by giving a general introduction to the concept of MACS followed by an explanation of the framework for MACS. The chapter explored the relationship between privatisation and MACS, it defined the aspects of MACS and explained the impact of privatisation on these aspects, and then it set out the changes that would be expected to occur in MACS in privatised organisations in Saudi Arabia. The literature revealed that privatisation would change MACS in any organisation; however some believed that privatisation alone would not change the MACS without the interaction of the three elements of organisational context which are the external environment, organisational culture, and organisational structure. The chapter examined in detail the changes that might be expected to occur in each aspect of the ten management accounting control systems' aspects.

Chapter Four reviewed and discussed some of the research design and methodology issues that researchers need to deal with. Additionally, it attempted to explain briefly the features of qualitative research and to justify the adoption of the triangulation strategy, combining the qualitative and documentation examination approaches to the collection and analysis of the data. It explained the advantages and disadvantages of the case study approach. In the case study of STC and SEC, in-depth interviews were conducted with top-level and other mid-level managers in different departments, providing data on their experiences and ideas concerning these particular issues. The validity and reliability of this study were discussed in some depth in this chapter. Internal validity and reliability were strengthened by using triangulation to minimise the weaknesses of the data collection methods.

Chapter Five provided a detailed description of the qualitative data collected. Changes that have occurred in the ten aspects of MACS in the two Saudi Arabian privatised companies were reviewed in each company separately.

Chapter Six provided a critical discussion and analysis of the qualitative data that were described in chapter five. The chapter compared the changes in MACS in the two companies to identify the differences and explore the factors that influence the degree of change. Factors that affect MACS other than privatisation were examined. A model (Figure 6.4) of the factors that affect the MACS in privatised companies has been developed.

7.2 Main Findings

Objective 1 set out to investigate the nature of changes in management accounting control systems in the two privatised Saudi companies (STC and SEC).

The analysis of qualitative interviews with the top, middle, and low levels of managers and the examination of the company's documentation showed that although the same government owned both companies, both of the companies were partly privatised to almost the same percentage, and both of them work in same political and social environment, there was a big difference in the level of changes in MACS in the two companies after privatisation.

Changes in STC were positively dramatic, and obvious in all aspects of MACS. On the other hand, the changes at SEC were very limited. For example there had been little change in some aspects of MACS such as setting the organisation's objectives and the budgetary process, and there were not any changes in some aspects of MACS such as the costing system and use of the BSC.

Objective 2 set out to clarify the factors other than privatisation that led to changes in the MACS in the selected privatised Saudi companies.

The analysis of interviews and documentation from both companies reveals that privatisation cannot be on its own the only factor that motivates changes in MACS. The study found that there are another three factors working together to improve MACS in any privatised company. These factors are: competition, government involvement, and the relationship between accounting and managers.

The key observation on these factors is that the first two have to be brought about by the government, as organisations cannot do so. It can be argued that once the government allows competition, it has to ease its restrictions on the privatised company, as governmental bodies cannot by their nature compete with private sector companies, especially when big international firms enter the market, as these private companies have the ability to respond quickly to market changes, whereas governments usually operate in a bureaucratic way. In addition government has to provide privatised companies with autonomy, as these companies have to have effective and sophisticated

accounting systems to clarify their costs, prices, and revenues in order to be competitive in the market.

The third factor is the result of allowing competition into the market and consequently the easing of the government restrictions. Privatised companies would be more commercial and more focused on profitability and as a result of that, the companies would pay a great attention to the kind of staff that they employ to include more people from a business and accounting background. This was the case of STC once the competition entered the Saudi Telecoms sector. Nevertheless it has to be mentioned that the Saudi government is the main shareholder and when it allowed competition to enter the market, it also appointed new members on the Board of Directors and increased the number of accountants and businessmen. Engineers are still the majority on the Board of Directors of SEC, in addition to the absence of competition and the huge involvement of the government in company policies.

The issues raised by Objective 3 examine whether privatisation improves management accounting control systems or not.

From the findings of this case study on Saudi Arabia, it can be said that privatisation for STC was a crucial step in improving MACS. It helped to establish a new regime of financial and accounting discipline using private sector accounting techniques that emphasised annual reports and their accompanying audit report, accrual accounting, implementation of corporate strategy, better use of budgets, and the introduction of financial management and information systems such as ABC and the BSC. Privatisation facilitated organisational environment and cultural change, from a highly bureaucratic structure to a more autonomous one, and from an engineering culture with an emphasis on physical production to a commercial culture.

On the other hand, the privatisation of SEC did not achieve the same level of change, as SEC lacked the motivation that arises from the existence of competition and suffered from the continuing huge involvement of the government in the company's policies, and the dominant role of engineers over accountants. From that, it can be said that privatisation on its own cannot change MACS positively. It can be argued that privatisation can be a motivation to encourage government to help companies to improve their MACS. The government can provide encouragement by allowing competition into the sector that has been privatised, and by easing the restrictions on

privatised companies; these would lead the privatised companies to provide accountants and business background people with power in their relationships with engineers.

This can be said to be the situation of less developed country such as Saudi Arabia as the government always control most economic aspects within the country and provides all services and production to people, which makes them depend on the government for everything.

Objective 4 raised elements of organisational contexts and their effects on the changes in the MACS of Saudi privatised companies.

It can be said from the analysis of the data that were collected during this study, that the cultural, political, regulatory and structural factors have had a great impact on the changes in MACS. This study found that organisations are effected by changes in the political and regulatory environment and have to respond to these, possibly by changing their structure, so as to be able to deal with the changed environment more effectively. So it can be said that changes in organisational structure can be a result of the response of the organisation to changes in political and regulatory environment.

In addition, changes in organisational cultural factors can be a result of the changes in national culture or changes in political, regulatory, social, and structural factors or the result of a conscious effort of the organisation to effect changes in its culture like the situation of STC. STC had a policy of trying to manage change in its culture. However, STC in some cases faced resistance from its employees to changing their culture and beliefs, so the organisation had to have a second plan, which was the ‘Golden Cheque’ and replacing such employees.

Objective 5 set out to propose recommendations to Saudi privatised companies and the Saudi government that might help companies to improve their current management accounting control systems and assist the Saudi Arabian government when it privatises other organisations.

These recommendations will be presented in detail in the following section.

7.3 Implications and Recommendations

From the analysis, the implications of the findings reported in this thesis can be summarised as follows:

1. Although a privatised organisation has to have autonomy in setting its objectives (Uddin, 1997, 2003), objectives cannot be set without taking into consideration other social, economic, and political factors. For example, one of the objectives of STC and SEC is to increase the number of Saudi employees in the companies.
2. A clear understanding of what the privatised enterprise is expected to achieve is crucial to improving its performance. Thus, objectives should be measurable and quantifiable since “what can be measured can be improved”. This can be seen at STC as most of its departments’ objectives were specified by numbers or percentages so they can measure them
3. A privatised organisation’s objectives should be kept a few as possible and priorities should be established; the cost of non-commercial objectives should be made explicit; financial and non-financial indicators should be introduced; and accountability should be based on results which require the condition of complete and appropriate information.
4. Effective change in accounting systems and budgetary process will most probably occur if it is preceded first by a change in the privatised organisation’s strategy and objectives and then a reorganisation of its administration and structure.
5. Government can ensure that SOEs are better prepared for privatisation by ensuring that they have suitable skilled directors, who are allowed sufficient autonomy and given strong enough incentives to strengthen control systems and improve the company’s values (Al-Dehailan, 2004; Bozec et al., 2004). One of the first steps that the Saudi government took when it prepared STC for privatisation was appointing suitable skilled directors and members of the Board of Directors.
6. Privatised organisations cannot control the changes in the external environment, which arise from privatisation but can only respond to them, but they can change their organisational culture by making efforts to change employees’ beliefs and the organisation’s values. In addition, organisational structure can be changed by efforts from the organisation to change it as a response to privatisation.

There are various recommendations that the Saudi Arabian government should consider when they are privatising other sectors and for privatised organisations to improve their management accounting control systems.

1. The accounting and control systems used in SOEs should be modernised. The lengthy instructions and procedures guiding accounting practices should be updated and simplified. Specialised units and departments should be established and highly skilled and professional staff should be recruited. This can be noticed clearly at STC when the company simplified its budgeting procedures and recruited highly experienced accountants and established special departments for budgeting, strategic planning and costing.
2. Different levels of managers should be given a greater opportunity to participate in setting objectives and in budget preparation. Possible benefits include (a) better understanding of assumptions underlying the objectives and the budget and direction of the organisation, (b) greater acceptance of the objectives and budgets as an attainable targets, and (c) clearer accountability centres. It was clearly noticeable at STC when the company allowed more participation from different levels of managers in setting their department's objectives, which made it easy for the company to measure departmental performance. In contrast SEC still has its objectives set by the government; this affects the way that its managers are accountable, as they just have to follow government orders.
3. The introduction of a reliable accounting system that collects financial and managerial information and prepares timely financial statements using generally accepted accounting principles should be a priority, if one does not already exist. The reasons for that are to provide SOE Boards of Directors and managers with sufficient information not only to monitor the performance of SOEs and allocate economic resources effectively, but also to generate confidence among potential investors and encourage their interest (Kennedy and Jones, 2003). STC applied a reliable accounting system and implemented a sophisticated standards that helped the company prepares its financial statements in an acceptable time. While SEC still suffers from delays in preparing its financial statements because of bureaucratic accounting procedures.

4. Therefore, to achieve successful reform, Saudi Arabian SOEs need to develop their accounting systems and maintain their accounts in accordance with generally accepted accounting standards in order to determine the current status and performance of the enterprise, and ensure that all necessary controls are in place to guarantee the efficient use of the enterprise's resources. For example, STC first used an US GAAP then switched to purely commercial Saudi Accounting Standards, whereas SEC used governmental procedures guides, now combining them with Saudi Accounting Standards.
5. An independent and effective state audit institution is needed to ensure adequate public accountability, check upon the economy, efficiency, and effectiveness, and assess the legitimacy and procedures of the transactions carried out to support the move towards privatisation. Furthermore, education and training are needed to provide employees with the specific technical and methodological concepts and procedures necessary to carry out an effective privatisation process. This can be seen clearly at STC when the company worked with two auditing firms in addition to the BT team before the privatisation. This helped the STC to overcome all the problems that faced the company on its way to privatisation. In addition STC recruited more educated employees and trained some of its employees to gain more education in accounting and finance.
6. This thesis found that the role and control of the General Audit Bureau (GAB) was ineffective. There is an urgent need to develop the GAB and enhance its role to secure effective monitoring of SOEs in order to facilitate the new government trend towards privatisation. It needs a sufficient level of incentives, independence, training, and competent staff. Its role should be proactive and not tied to the rules and regulations of the MOF. It was one of the main problems that faced STC at privatisation, as most of the data that were provided by the GAB were insufficient and people working there still had a governmental mentality and some of them were not qualified.
7. Although the Saudi government enjoys economic and political stability and does not plan at the moment to transfer the whole ownership of its vital infrastructure to the private sector, the current economic situation, the dramatically growing population, and the poor quality of some existing infrastructure requires further private sector participation, which in turn

requires a satisfactory investment climate, a strong market, reliable external controls and a strong independent regulator. To achieve privatisation successfully, it is essential to improve the accounting environment by increasing the role of the Saudi Organisation for Certified Public Accountants (SOCPA), developing stock markets, and enhancing the level of public awareness regarding the importance of accounting information through the media, accounting professional and education. It is noticeable that most of the accountants at STC after privatisation are members of SOCPA whereas this is not the situation at SEC.

8. The Saudi government should learn from the experience of the last three decades. In the 1970s and 1980s the emphasis was mainly on construction and accounting systems received little attention due to the budget surplus, which limited pressure for quality information for control (Al-Dehailan, 2004). However, the economic situation changed in the 1990s, since the increased budget deficit together with high population growth forced the government to rationalise its expenditure and use resources effectively. Although the government has ambitious plans, its objectives are difficult to achieve in a weak information environment due to inadequate current accounting systems, which may lead to waste instead of rationalisation and impair effective control, planning and decision-making. Therefore, there is a strong need to develop the accounting environment (governmental and commercial) in Saudi Arabia to effectively govern the new economic trends and support government plans for privatisation. The government role will change from a service provider to a service regulator, which requires the regulatory authorities to be more effective and informative. This was seen in allowing a bigger role for SOCPA in setting Saudi Accounting Standards and forcing Saudi organisations to follow them. Also the government paid more attention to the stock market and created a regulatory body for that market with strong and specific roles, which called Capital Market Authority.
9. The government should open the sector for competition once it has privatised an SOE in order to motivate the company to respond positively to market changes. Most of the changes at STC were motivated by competition, as the company has to respond to market changes and gain more from the market. Furthermore, SEC launched some plans to improve its efficiency, for

example applying BSC, after the announcement about allowing competition in the sector. This research shows clearly that competition is a much more powerful driver of change than privatisation per se.

10. Once government has privatised an SOE, it should give the company full autonomy to set its objectives and budget, apply adequate accounting systems and costing systems, attracting qualified staff. This autonomy helped STC to motivate its managers to set achievable goals and to clarify their responsibilities. Moreover, it encouraged STC to apply more sophisticated costing systems and attract more qualified people. In contrast SEC still suffers from a lack of motivation on the part of its managers and employees and from unclear responsibilities.
11. Saudi universities and institutes through their academics can contribute to achieving successful reform since this is the time for them to play a key role in order to serve their country. The privatisation process would provide a good opportunity for them to benefit organisations since organisations lack qualified staff. Moreover, they lack understanding of the organisations' actual practices, which impacts negatively on their knowledge. Saudi universities and institutes can provide SOEs and privatised companies with special courses in accounting and finance and gain benefit from these universities' academic expertise and do research on these companies' problems and provide them with recommendations.

7.4 Thesis Contributions to Knowledge:

This research has made a contribution to the understanding of MACS and their relationship to privatisation. To date, little research has focused on the issues of management accounting control systems in developing countries. By investigating MACS and their relationship to privatisation in a Saudi context, this study has added to our understanding of how privatisation would change MACS bearing in mind the social, cultural, economic, and political contexts of a developing economy.

To the best of the author's knowledge, this study is the first to investigate empirically the effects of privatisation on MACS in Saudi Arabia and the factors other than

privatisation that would affect MACS. In addition, this study identifies the gap between privatisation theory and MACS in Saudi organisations and thereby will hopefully contribute to improve the level of efficiency that privatisation would bring to an organisation.

This study also fills the gap in the international literature on management accounting reform issues since it has focused on management accounting control systems and changes in its aspects as a result of privatisation and examines the effect of the three elements of organisational context on MACS. The study identifies the factors that would have an effect on MACS other than privatisation.

This study provided empirical evidence from Saudi Arabia that supports other case study researchers in management accounting (Flamholz, Das and Tsui, 1985; Jones, 1985; Espeland and Hirsch, 1990; Adam et al., 1992; Ogden, 1993; Wright et al., 1993; Karatas, 1995; Potts, 1995; Boycko et al., 1996; Wickramasinghe, 1996; Uddin, 1997; Ferreira, 2002), namely that privatisation would change the aspects of MACS by interaction with the elements of organisational contexts and social, political, and economical factors. Thus this study replicated earlier research on management accounting control systems and the impact on these of privatisation, and extended the research by providing additional material, such as the identification of factors other than privatisation that affect MACS in privatised companies.

7.5 Research Limitations

Any research effort has its own limitations which have to be frankly admitted and discussed in detail as a means of furthering the understanding of what the research has accomplished. This thesis has several limitations.

First, because this study was conducted as an exploratory case study in two organisations, the results are constrained by the unique nature of these organisations and their activities. Hence, findings obtained highlight only the changes in aspects of MACS as a result of privatisation in the two organisations being studied and, therefore, lack generalisation.

The second main limitation was the methods of data collection. The primary data collection in this research was semi-structured interviews. The various shortcomings of interviews have been admitted, discussed and dealt with in detailed in Chapter Four.

The third main limitation was the timeframe. Given the limited time available, a complete investigation of the phenomenon under consideration could not be undertaken, especially by using a case study approach. Although all possible efforts were made to interview as many people as possible in both STC and SEC, the companies allowed only a limited number of participants.

Fourth, there were limitations in access to information especially at SEC, where officials were particularly hesitant to release information due the nature of the information requested. Access to such information was sometimes impossible because of confidentiality. However, access in this study was gained through advanced permissions and arrangements, a friendly relationship and a formal contact as a representative of Umm Alqura University, where the researcher is a teaching assistant.

Fifth, the strength of the analyses presented depends on the ability of the researcher to identify, choose and analyse the empirical data considered being the most important and appropriate. Since this involved judgements, the analyses faced the risk of being biased towards values that the researcher adopted and the extent of his knowledge to make such choices. The researcher overcomes this limitation through classifying the areas of the study and choosing and grouping participants accordingly. Therefore, although the researcher was selective in terms of issues and participants due to time constraints, this selectivity, did not affect the analysis.

Despite the above limitations, the researcher believes that the study has been successfully executed and provides new understanding in the research area studied, shedding light on the under-researched area of MACS issues in Saudi Arabia.

7.6 Areas for Future Research

One of the main aims of this chapter is to highlight some areas where further research might be pursued in order to contribute to the understanding of management accounting control systems and organisational change in privatised companies.

First, data was collected for this study in early 2008, two years ago; during this time organisation might have undergone some changes, thus an updating study would be recommended to investigate the changes over the time.

Second, the Saudi government announced that it would privatise more of the public sector and in the case of electricity sector; the Saudi government announced that it would open the sector to competition and reduce its involvement in the SEC. These would suggest a study of the effect of the introduction of these factors on MACS in SEC and compare it with other new privatised sectors. This could be compared to the findings of this study.

Third, due to the lack of studies about privatisation in Saudi Arabia, a further study could be conducted to examine the impact of privatisation on the Saudi economy in general, company financial performance in particular and on public satisfaction with the new policy.

Fourth, a study could be conducted on other countries that share the same economic, cultural, and political systems as Saudi Arabia, especially countries from the Gulf Corporation Council (GCC) or Middle East Countries. The study might try to provide a framework for other countries to follow when they want to implement a privatisation policy.

7.7 Conclusion

This study has provided several important insights into issues relating to Management Accounting Control Systems. It is one of the first to investigate how privatisation affected the management accounting control systems in Saudi Arabia by investigating the changes in aspects of MACS before and after privatisation in two Saudi privatised companies. This research discovered other factors that might affect MACS other than privatisation

This research has also contributed to the management accounting literature by providing advice for governments of less developed countries, which intend to pursue privatisation policies. It has identified the key factors, which should improve management accounting control systems, in particular the importance of introducing competition and avoiding governmental interference in the affairs of privatised companies.

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Appendix A: Interviewee Questions

A. Introductory

1. How long have you worked for this organisation?
2. What positions have you held during that time? Qualifications and experience gained?
3. What do you do now?

B. External Environment

4. What did you understand to be the main objectives of privatisation at the time it was introduced? Has your understanding changed over the years?
5. What do you consider have been the main consequences of privatisation for your organisation? Any unintended consequences?
6. What did you consider was the role of the regulator at the time of privatisation? Has your understanding changed over years?
7. What do you consider have been the main consequences of regulation for the industry? Any unintended consequences?
8. Are you personally accountable to (a) the regulator or (b) any other external bodies as a result of regulatory requirements?
9. Do you feel that your accountability relationships are clear and well defined? Do you find any conflicts between accountabilities to different bodies?
10. In terms of your organisation's stakeholders, who do you think have been the winners and losers over the years since privatisation? (by stakeholders, I mean employees, directors, shareholders, customers, suppliers, government)
11. Is the current level of regulation too intrusive, about right or not strong enough?
12. What, if any, are the main changes you would like to see in the regulatory process?

C. Organisational structure

13. Could you provide me with an organisation chart? Can we discuss it?
14. Who do you report to? Who do you work with? Do you find any conflicts in being accountable to different people, e.g. because they have conflicting objectives?
15. Are unit managers responsible for revenue, profit, cost control, ROCE? Has this changed since privatisation?
16. Your organisation has undergone numerous reorganisations since privatisation. What are the main reasons? Do you believe the reorganisations have been effective in helping your organisation to meet new challenges?
17. To what extent have you experienced new reporting structures and accountabilities which are due to the company reorganising: (a) to meet regulatory requirements, or (b) reshaping the business in order to move into new areas?
18. In what ways reorganisations have directly affected the work that you do? Have they helped you to contribute more in your work towards the achievement of organisational objectives?
19. What have the main effects of changes in organisational structure on your career with your organisation?
20. Are you aware of any power shifts (i.e. greater influence exerted by some departments or divisions than other) as a result of reorganisations?

D. Organisational culture

21. Do you believe your organisation had distinctive organisational values prior to privatisation? Can you describe it? What changed?
22. Do you think the changes in the organisational values have developed in response to new challenges, or has there been a planned effort by top management to change the culture?
23. Have you experienced any ideas, which you believe were planned attempts to change the culture, e.g. attendance at courses on management techniques, financial awareness, etc.?

24. Are certain specialist skills accorded greater prestige, status and rewards than others within your organisation? Are certain skills more in demand now than they were before privatisation? Is great importance attached to professional qualifications?
25. Would you tell me about the difference between the public sector and commercial philosophy on the way they think the organisation should be operated?
26. Do you think your organisation has changed its image in the minds of the public? In what ways?
27. Do you think that any of the changes you have experienced in relation to provision of financial information have resulted in a change in organisational culture?
28. What have been the main effects on your work and career of any cultural changes?
29. Does the number of the employees changed? How? Did u change the required qualifications? Why?

E. Accounting information

30. Do you think financial information has been taken on greater significance in relation to your work since privatisation? In what ways?
31. What sort of accounting techniques do you use in your unit? And why?
32. What sort of changes have you experienced in dealing with financial information (e.g. more use of budgeting, new or increasing accountability, ABC)?
33. Do you accept that the financial control you experienced are relevant and important in your work?
34. Do you think that any of the financial controls influence your behaviour in a way that they were not intended to do?
35. What financial information do you have to produce? Do you report the information directly to an external body or to someone else within your organisation?
36. Which financial performance indicators are of most importance to the regulator, shareholders, investors, and decision-makers?
37. What is the role of the managers in achieving co-ordination between departments?

38. Do you receive accounting reports on time? Are you satisfied with the information provided in these reports?
39. Do you use non-accounting information, such as production reports, narrative reports? And to what extent do you think they are useful?
40. Can you explain to me the importance of accounting to your company in terms of its usefulness in control?
41. What is the role of the managers in the process of budget setting? (e.g. record keeper, consultant, coordinator)
42. Do you use accounting data for the purposes of problem solving and performance evaluation? Would you provide me with examples please?
43. In which area does your company make formalised plans or budgets?
44. How often each budget is revised? (e.g. annually, quarterly, monthly)
45. How often variance reports are prepared (actual vs. budget)? (e.g. weekly, monthly, quarterly)
46. Do you have an internal audit department? If yes, what are the objectives of this department?
47. Do you have an external audit department? Does it required by the regulators? And how does it function with the internal audit department?
48. Have the financial accounting requirements changed since the privatisation? If so, who ask for these changes? Why? What are the impacts of the changes on the control system?
49. Could you explain the purposes of the use of the management accounting data?(e.g. measure performance, determine the cost, evaluate the efficiency)
50. How are specific budgets or goals established? (e.g. goals and objectives are established exclusively by members of higher management without consultation with lower levels of management or it developed by higher levels of management and are presented to lower levels of management for their consideration and comment prior to final adoption)
51. Does your organisation usually establish specific non-financial budgetary targets for its managers? (e.g. Productivity, human resources development)
52. How many budgets do you use based on its purpose? (e.g. planning and co-ordination, evaluation purposes)
53. How frequently do you review your annual budget for possible revision of goals? (e.g. monthly, quarterly, semi-annually)

54. How frequently do corporate managers formally meet with lower level managers to discuss budget related matters? (e.g. weekly, monthly, quarterly)
55. How do you handle the reports, which show a significant variance? (e.g. written or oral explanation, indicate what corrective action is to be taken)
56. Does your organisation have the freedom to set their prices? How? What are the regulators' requirements for that?
57. Would you tell me about the capital investment in your organisation? And what are the techniques they use for that?
58. How does your organisation manage their cash flow/liquidity? In other words, can you tell me about your cash budgeting?
59. Would you tell me about the rewards system in your organisation? Does it conflict with accounting department?
60. What are the methods used for personal evaluation? (e.g. residual income, variance analysis, sales target to productivity). And if there is a variance, how do you handle it?