

CGMA REPORT

PERFORMANCE  
MEASUREMENT AND  
MANAGEMENT CONTROL  
IN NON-PROFIT  
ORGANISATIONS

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Two of the world's most prestigious accounting bodies, AICPA and CIMA, have formed a joint venture to establish the Chartered Global Management Accountant (CGMA) designation to elevate the profession of management accounting. The designation recognises the most talented and committed management accountants with the discipline and skill to drive strong business performance.

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## KEY FINDINGS

1. Non-profit organisations (NPOs) are being confronted with the competitive nature of acquiring funds and need to demonstrate that they have particular competencies to funders, while at the same time continuing to adhere to their traditional welfare or development values.
2. The evidence shows that developing formal performance measurement and management controls can help NPOs to develop networks with government departments, funding agencies, other service providers and clients. However, formal management controls also have the potential to damage the internal bonding between employees.
3. Developing belief systems to incorporate financial concerns, along with traditional welfare goals, would seem a useful starting point in the move towards managing in a more competitive NPO sector.
4. Developing performance measurement and management controls in ways that are inclusive of different values and perspectives is critical in generating bonding social capital. Involving staff in the choice of performance measures and the design of management controls can provide a forum to debate and reaffirm core values. It also provides information to staff to see how controls relate to operational concerns. Finally, such an approach can help to ensure that the introduction of new performance measurement and management controls is consistent with the often more informal, collaborative and qualitative modes of control within NPOs.

## OVERVIEW AND OBJECTIVES

In recent years (NPOs) have become increasingly important in addressing humanitarian issues relating to welfare and developmental aid. NPOs face increasing pressure to demonstrate service delivery in cost efficient ways. This can create tension over delivering welfare services while operating within the constraints of cost management. The application of performance measurement and management control systems has the potential to help in the effective and efficient delivery of services, but for many NPOs such an approach is relatively new and is sometimes at odds with the customary informal controls that have been applied in NPOs. For NPOs to be successful, it is also important to develop close connections with other agencies and individuals involved in NPO activities, and that agencies and individuals are committed to aims that relate to welfare and development.

This report summarises research undertaken within two NPOs: the first NPO provides welfare services to the disadvantaged, the second NPO addresses poverty alleviation in developing countries through volunteering. We use the notion of social capital to describe how NPOs can be effective in developing social connections that ensure the delivery of services. Broadly speaking, social capital concerns the goodwill that is created through social relations. This goodwill is derived from developing two forms of social capital: bonding and bridging. Bonding involves developing close interpersonal relationships based on shared aims, and bridging to building networks between the NPOs and other parties. These dimensions act in combination, with bonding involving close interpersonal relationships based on common beliefs, and that action based on these values is carried out collectively through networks that connect different agencies and individuals.

There are several benefits to NPOs from developing the bridging and bonding attributes of social capital:

- Greater access to detailed, confidential and fine-grained information from more extensive networks.

- Development of solidarity based on social welfare values, both within the NPO, and between it and other individuals and agencies across the NPO network.
- Acquisition of influence, power and control by the NPO as a consequence of deciding who should join their networks.

In this way, social capital is a critical resource in enabling NPOs to deliver services in ways that involve commitment to their fundamental social values. Social capital is particularly important in NPOs as they typically have more limited access to financial resources than profit-seeking organisations.

Traditionally, the management of NPOs has relied on informal processes based on the shared norms and values of delivering humanitarian services, rather than on coercive or formalised procedures. The commitment of workers, volunteers and other organisational members has tended to be facilitated through strong reliance on a shared belief in the purpose of the organisation, and not primarily through financial control and remuneration based on profit making. While NPOs have customarily relied on informal management processes to help develop and sustain their social capital, there has increasingly been pressure from donors, government and other official agencies for NPOs to show accountability and managerial competence. This has necessitated the adoption of more formal financial controls and business-like management practices such as performance measurement. Management accounting has great potential to assist in:

- planning and control when formulating proposals for funding, often involving networks of partner agencies
- clarifying within the NPO the importance of including economic efficiency as an organisational value alongside traditional welfare values
- developing performance measures that aid in the evaluation of performance and allocation of resources in efficient ways
- linking non-financial operational performance to financial concerns.

For many NPOs it is difficult to make the transition from values-based, informal management practices

to an approach that emphasises the financial implications of decisions.

‘NPOs have traditionally been reluctant to import practices from the business sector.’

An additional challenge concerns the potential impact of more formal performance measurement and management controls on the ability of NPOs to develop social capital. Little is known about how formal controls affect the way NPOs develop and employ social capital, and how this influences their ability to deliver welfare services with increased pressure to be more financially efficient. This study examines how formal performance measurement and management controls can have both beneficial and damaging effects on building and preserving social capital in two NPOs.

Our first research site is a welfare NPO located in Melbourne, Australia, that comprises three divisions employing 120 full-time employees. The division that is the focus for this study, which we refer to as Tennant, comprises a manager, an administrative staff of four, five programme coordinators and 32 case workers. There is also a small part-time volunteer staff; however these individuals do not engage in the operational activities of Tennant. The NPO advocates for social change and promotes the health and wellbeing of disadvantaged young people, families and communities. Tennant’s service delivery model involves connecting clients with other agencies that provide housing, employment, medical and social services. Managing these connections is critical as no one agency can adequately meet all the needs identified for programme participants. Tennant often works with other agencies to submit to government joint proposals for programme funding. The organisation is interesting because it is not as financially well-endowed as larger agencies, like Oxfam or Action Aid. As such, it must carefully target its work to areas where it can demonstrate that:

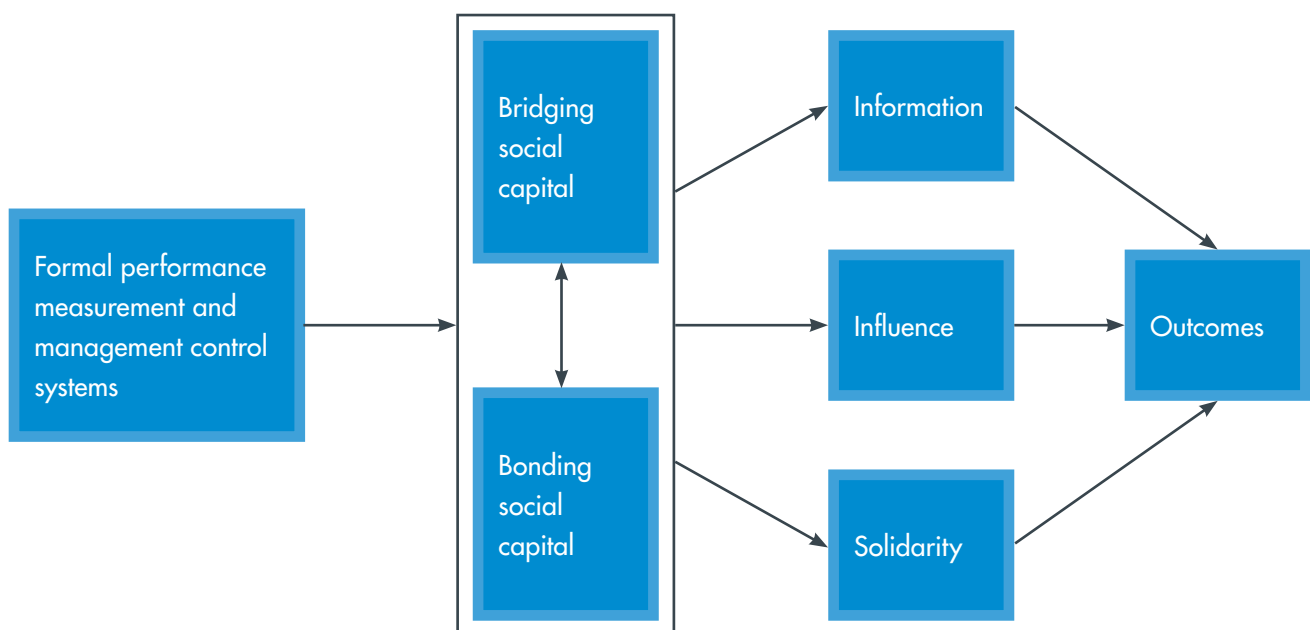
- it is well connected to relevant service providers
- it has superior capabilities and commitment in effectively delivering its services in cost effective ways
- it is able to play a leadership role in gaining collaborative projects that involve government contracts often involving several alliance partners.

Our second research site is Voluntary Service Overseas (VSO), a non-profit international development organisation that works primarily by linking volunteers with partner organisations in developing countries. VSO has over 500 staff (the majority located in the London, UK head office), and each year approximately 1,500 volunteers are recruited and take up placements in one of the over 40 developing countries in which VSO operates throughout Asia and Africa. VSO uses a ‘capacity building’ approach by partnering volunteers with local organisations that require assistance or expertise in a variety of capacities. Volunteers typically take up a specific position, often working alongside a local staff member, where partner organisations range in size from very small, local businesses, community groups and NPOs, to large

organisations and government departments and ministries. VSO receives most of its funding from the United Kingdom’s Department for International Development via three-year funding agreements. Other funding is derived from project grants and donations from philanthropists and the general public.

Social capital provides a resource that can help NPOs to build capabilities to deliver programmes. However, there is concern that in using formal performance measurement and management controls to become more efficient, NPOs may damage their social capital. Figure 1 illustrates the overall framework within which our study was positioned.

FIGURE 1: Framework relating formal performance measurement and management controls to social capital and its outcomes



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# FINDINGS

## The Tennant Centre

At Tennant, we observed the extensive use of formally articulated belief systems, such as a mission statement, promotional leaflets, statues, photographs and paintings of Tennant's patron, the use of social welfare values to select employees during recruitment, and periods of reflection on social welfare values during fortnightly senior management team meetings. Other important formal controls were financial budgets and programme management practices used in conventional ways to monitor outcomes and correct deviations from preset targets. We also observed attempts to develop a concern with efficiency and cost consciousness by using financial budgets in participative forums involving face-to-face interaction between the chief manager, programme directors and coordinators. Tennant also had a rich tradition of informal controls, such as open-door policies, impromptu meetings, 'corridor talk', sharing of information, and a tolerance for mistakes.

- We found that belief systems clearly articulated the social welfare ideals of the organisation and were used, as is common practice, to signal the values of the organisation to employees, other NPOs and government departments. This process can assist in bonding as values are clarified and confirmed. However, their role extended beyond these more symbolic purposes and the systems were actively used in day-to-day management. For example, sometimes case workers must work to rehabilitate a person with prior behaviors that are perceived as socially aberrant. Consequently, case workers may experience stress and be distracted from the values of the organisation, which preserves the dignity of all individuals, no matter what their backgrounds. This disjunction between the individual and the organisation's values can inhibit or destroy bonding. Belief systems provided a valuable way of revisiting and reaffirming values in ways that were supportive of all parties. This helped to reaffirm bonding social capital and to enhance solidarity amongst employees.
- Second, we found that well developed formal controls, including financial controls, helped to demonstrate Tennant's capabilities in service provision to other service providers and government departments. Many of these mechanisms had limited use as operational controls because they were primarily oriented towards external audiences and were not linked directly to the day-to-work of operational staff. Importantly, given the closeness of connections across the welfare sector, Tennant was seen to have a strong reputation for high quality service delivery. The use of formal controls was a way of confirming, articulating, and, in a sense, advertising these capabilities in a setting of increasing competition amongst NPOs for welfare funding. We saw close links between these processes and the development of bridging social capital, with outcomes of increased power and authority for the NPO within its network.
- Our third finding was that the use of formal controls in more participative, interactive ways can be problematic in settings where the customary mode of control is more informal and open. Formalising discussion of financial matters and their operational implications was seen to prioritise these issues ahead of a primary concern with delivering welfare services. While many organisations face difficulties in ensuring that financial matters receive due attention from managers, the jarring effects in NPOs appears to present an impasse for many employees who do not see how financial issues can help them to deliver services to clients. These tensions were manifested in damaging effects on internal bonding and a breakdown of solidarity, particularly between managers and case workers.

- Finally, we see that Tennant is at a crossroads in terms of how they are managed and the role of management control systems in this management. From informal discussions with other NPOs this appears to be a common concern. The increasing pressure to corporatise the structure and management of NPOs can be at odds with customary modes of operation, which, have helped NPOs to generate bonding and bridging forms of social capital. We see an important role for belief systems to incorporate values surrounding financial efficiency and viability, as well as traditional welfare values. Formal controls have an important legitimising role, enabling an NPO to develop networks to suit their way of delivering services. A significant challenge facing NPOs with strongly held welfare values is how to use formal controls in conjunction with the more informal, customary modes of control.

## Voluntary Service Overseas

At VSO we observed the development of a new performance measurement system entitled the 'quality framework.' The quality framework attempted to combine different indicators and narrative content into a single report that would provide a common measure of performance in each of VSO's country programmes on an annual basis. Measuring performance at VSO had become more important in recent years because of increased pressure on the allocation of resources amongst programme offices, particularly as VSO was attempting to expand its impact through more volunteer placements and the development of new programmes. In the quality framework each country programme was scored on a set of approximately 40 indicators, with the indicators grouped under 14 'elements' of quality, such as 'programme impact at beneficiary level', 'volunteer engagement and support' and 'cost effectiveness.' Figure 2 provides an example of an element and its set of indicators. Each indicator was scored on a scale of one to four, with higher scores indicating better performance. The appropriate score for each indicator was determined in two stages. The first stage involved a discussion in the country programme office, utilising relevant data sources as support, to arrive at a judgement about the appropriate score for each indicator. The second stage involved each indicator score being reviewed and agreed (with revisions if necessary) during a

consultation between the country director and his/her regional director (supervisor).

- We found that the process used to develop the quality framework was very important in assisting bonding amongst staff. The design of the quality framework was a collective endeavor involving staff from country programmes (the ultimate users of the quality framework) and head office. During an annual meeting of country directors held in the UK, a special session was devoted to discussion over the elements and indicators that would comprise the quality framework, where staff with different perspectives were able to advocate for the inclusion of particular elements and indicators. This helped bonding by enabling staff to clarify priorities and reach consensus over the most important aspects of programme work.
- Second, the quality framework signalled a shift away from measuring only inputs (eg, funding, number of programmes, volunteer numbers) to a much stronger focus on measuring outcomes and impacts. Specifically, 'programme outcomes at partner level' and 'programme impact at beneficiary level' were identified as the two most important elements in the quality framework. It was critical to the acceptance of the quality framework that indicators of outcomes and impacts were included at the outset, even though measuring these elements was inherently difficult and it would take several years to produce reliable data. This helped staff to bond around the overall purpose of VSO's work, which was to help partner organisations achieve positive changes in the lives of beneficiaries. A failure to include measures of outcomes and impacts would have created considerable tension over the purpose of VSO's work and ultimately could have led to a breakdown in bonding social capital.
- A third finding was the importance of designing the performance measurement system to reflect the diverse preferences and values of staff. This was achieved in two ways. First, as shown above, the quality framework included a wide variety of elements and indicators in order to avoid a narrow focus on only a few areas of performance. Second, the quality framework included a narrative component under each element whereby staff could provide additional written information that was not reflected in the indicator scores.

FIGURE 2: Example of an element and indicators in VSO's quality framework

Element 7: Volunteer engagement and support					
Number	Indicator	Score			
7.1	Volunteer support baselines are being met by the programme office and partners are supported to manage volunteers.	1	2	3	4
7.2	Programme office celebrates volunteer achievement, responds to volunteer problems effectively and encourages the development of effective and accountable volunteer groups.	1	2	3	4
7.3	Volunteers are engaged in programme development.	1	2	3	4

This was important to many staff who felt that indicators could not capture effectively the complexity of programme work. These two practices helped to generate a sense of inclusion amongst staff whereby aspects of performance and information that they believed were important were visible in the quality framework. Our findings reveal, however, that there are limits to this approach. The inclusion of more and more indicators and/or different types of information can make the system cumbersome and unwieldy. It can also be directed towards the appeasement of different groups, which could result in the inclusion of redundant and irrelevant information. This shows that there is an important balance to be struck between being inclusive of different perspectives but in such a way that avoids unnecessary complexity.

- Fourth, the use of performance measurement information can create considerable tension with the potential to erode bonding social capital. There were many debates at VSO about how to use the information produced by the quality framework. Some staff, particularly from head office, wanted to use spreadsheets and 'league tables' to show how the performance of one country compared to another. This practice was resisted very strongly by country programmes. They felt that the comparison was flawed because each programme operated in very different country contexts, which were not reflected in the indicator scores.

'Many staff also felt that the use of 'league tables' reflected a competitive and business-like orientation that was at odds with VSO's focus on sharing information, volunteering and helping to alleviate poverty.'

This debate generated considerable tension and had the potential to erode bonding, particularly between head office staff and country programmes. Importantly, after much discussion, the 'league table' was discontinued and replaced by a practice that highlighted only the best performing countries. This allowed staff to consult with and learn from good performers without creating a ranking. This helped to alleviate tension and share knowledge between countries that aided the development of bonding social capital.

- Finally, we see that although the quality framework was developed primarily for internal management purposes, it was also helpful in demonstrating to existing and potential funders that VSO was serious about improving quality. Importantly, the quality framework was not a tool to help VSO to 'prove' its impact, but provided the basis for discussions between VSO and existing/potential funders where its unique value and competitive position in the nonprofit community could be advanced. In this way, the development of the quality framework helped the development of bridging social capital between VSO and its funders.

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# IMPLICATIONS FOR PERFORMANCE MEASUREMENT AND MANAGEMENT CONTROL SYSTEMS IN NON-PROFIT ORGANISATIONS

Our study has several implications for the management of NPOs and how performance measurement and management controls can be used to preserve and develop social capital. NPOs foster bridging social capital to develop contacts and networks to ensure that welfare is delivered to those most in need. To assist in ensuring those within networks interact around common welfare ideals, NPOs attempt to make sure that participating individuals and agencies are bonded by sharing core NPO values.

Bridging social capital is about developing connections with other organisations while bonding involves developing close interpersonal relationships based on shared values. It is important for managers to understand this distinction. Employing performance measurement and management controls can be effective in helping managers to develop connections to suit their purposes as formal systems provide information to demonstrate why the focal NPO is more capable than others to provide services to a client group, or to be the senior partner in an alliance. They can also help to generate discussions with funders about the unique value and competence of the NPO. Here controls can include belief systems, performance measurement reports to demonstrate a sound track record and competent management, and project proposals that can be used to persuade and convince external parties of the NPO's credentials.

Conversely, the application of performance measurement and management controls to support bonding activities presents more challenges. At Tennant, bonding was best served by the pervasive use of belief systems that aligned closely to the values of the organisation. The belief systems were used actively to clarify values during recruitment, on-going operations and in times of change when external factors exerted pressure to divert Tennant from its primary aims. This case indicates that NPO managers can enhance bonding by the active use of belief systems. This should be a dynamic

process where belief systems are revisited from time to time. This can engage employees in the process of addressing the importance of the NPO to its field of operations, including contemplating the relevance of core values. In this way bonding is encouraged as the organisation engages in a process of affirming its shared values. At VSO, bonding was enhanced through the development of a performance measurement system that drew on the experience and knowledge of staff to develop indicators that were, in most part, inclusive of different perspectives and provided important signals about the strong focus on outcomes and impacts that were valuable to all concerned. As with Tennant, this process was an opportunity to debate and reaffirm core values that helped to generate bonding. It should be noted, however, that while bonding can encourage commitment to core values and solidarity, there is a danger that the organisation can become inward in its focus. This may inhibit disagreement and discussion which can challenge existing ideas and processes and potentially generate new ways of achieving effective and efficient operations.

Our research illustrates a dilemma facing NPOs. On the one hand, NPOs can promote bonding between employees by encouraging commitment to its welfare values. This occurs as the aims of the NPO are consistent with the ideals of NPO employees. On the other hand, the survival of NPOs is becoming dependent on them being able to compete for scarce welfare funds. This will require careful analysis of the benefits and costs of different programmes and discussions of possible cutbacks. Inevitably, this will result in a reduction of some services and an inability to service deserving countries, groups or individuals. To make these decisions, formal accounting is required to determine and manage the benefits and costs of different programmes.

Managers of NPOs are faced with two problems. First, how can they encourage employees to accept the inevitability of a more economically rational

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approach to their operations? Second, how can formal performance measurement and management controls be used to introduce a concern with economic matters without damaging strongly held welfare values? At Tennant, attempts to do this were unsuccessful, with damaging effects on bonding. In contrast, at VSO, although there were some difficulties, the careful involvement of staff and the inclusion of different perspectives helped to introduce the quality framework in a way that helped to develop bonding amongst staff.

From our observations at Tennant, it was clear that the customary informal controls had developed symbiotically with bonding. The informal controls encouraged open discussions and the development of trustworthy relationships which nurtured bonding. Bonding provided employees with confidence to contribute opinions and manage operational issues in ways consistent with shared aims. For managers of NPOs, more generally, this symbiotic relationship is a valuable resource that needs to be cultivated and preserved. There are real dangers to the very identity and potential survival of NPOs if this balance between the mode of control and bonding around values is lost. At VSO, this tension was most evident with the use of the 'league table' to compare countries, which had the potential to erode bonding between head office staff and country programmes and limit solidarity and the sharing of information. Importantly, the league table was discontinued, which reinstated a focus on knowledge sharing between countries that ultimately aided the development of bonding social capital.

There remains the issue of how to encourage a concern with financial matters without damaging the internal bonding aspect of an NPO's social capital. Our investigation at Tennant suggests that the use of financial controls would appear to require, as a precursor, a change in attitudes and values concerning financial responsibility and efficiency. It seems that financial responsibility could be encouraged by developing an efficiency focus before employing financial controls, and then using these controls in a participative way to manage financial matters. While this may seem to be common sense, it does highlight a potentially critical, but overlooked, role for belief systems in shaping values and attitudes towards other elements of formal controls. Given that belief systems could flag the importance of financial efficiency as a way to deliver more and/or

better welfare services, financial controls could then be employed within an approach where much of the resistance to financial controls had been addressed. In addition to the use of belief systems, our findings at VSO reveal another avenue to overcoming resistance. This involved explicit recognition of the value of different perspectives by making them visible in the design of performance measurement systems. For example, the quality framework included a narrative section to complement the indicators. This helped to alleviate concerns that the complexity of programme work would be lost within a purely quantitative approach.

A final observation relates to the importance of transparency and participation in the design and operation of formal systems in NPOs. Tennant faced difficulties employing formal financial controls due to a lack of disclosure on the connections between financial information and operational matters. This inhibited attempts to develop more interactive and participative budgetary processes that were more in line with the customary open and informal controls that suited Tennant's culture. That is, while budgetary processes involved face-to-face interactions, the budgets did not have sufficient transparency to highlight ways that budget constraints could be managed, in terms of their effects on operations. The local implications of budget cuts on programmes or of the role of organisation-wide overheads were not disclosed. In addition, discussion of budgetary matters was restricted to formal, scheduled meetings. These formal approaches were inconsistent with the more informal 'open-door' management style, where emerging issues were addressed in impromptu meetings where the opinions of employees were actively sought. It is possible that more information to enable informed debate on the connections between financial and operational matters would ensure that budgets became a more active and accepted part of management. At VSO, we see the importance of developing performance measures using a participative process. This helped to ensure that the connections between performance measures and operations were very clear, and provided a forum for airing concerns and resolving conflicts from the outset. Notwithstanding the provision of more relevant information, a challenge remains in combining the inevitability of a more formal approach to performance measurement and controls with a culture of open communications and participative decision making.

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# CONCLUSIONS

NPOs are being confronted with a need to become more sensitive to the competitive nature of acquiring funds and, as a consequence, the need to demonstrate that they have particular competencies to deliver services to targeted groups in need of welfare or development aid. In responding to this need, NPOs are inevitably drawn to incorporate business-like management controls and performance measurement systems. In positioning our research around the generation and preservation of social capital, we have been able to show both the positive and negative effects from efforts to employ more formal approaches to performance measurement and management control. Our evidence shows that developing formal management controls and performance measures can help NPOs to develop networks with government departments, funding agencies, other service providers and clients. By demonstrating superior capabilities, an NPO can act as a broker between these groups, gaining power and authority to implement projects in ways that they see as desirable.

Our study also draws attention to the potential damaging effects of formal financial controls on the bonding aspect of social capital. The challenge facing NPOs is how to preserve the critical resource of a closely bonded organisation, while introducing financial controls that are typically seen by employees as being at odds with the NPO's welfare values. Accepting that concern with financial matters is critical to the survival of NPOs, managers should aim to avoid a clash in control cultures that can arise from the premature imposition of formal financial management within the customary informal controls that have operated in most NPOs. Developing belief systems to incorporate financial concerns, along with traditional welfare goals, would seem an essential starting point in the move towards managing in a more competitive NPO sector. Employing controls in participative and inclusive ways is also paramount. Given this approach, NPOs can then engage in training and experimentation to show how employees can use performance measurement and management controls to help them identify emerging concerns involving the costs and benefits of their welfare programmes. Importantly, the information

content of management controls should be adequate to enable employees to contribute to decisions on how to achieve the most effective service delivery within the financial constraints of the NPO.

## Additional information about the project

At Tennant, we gathered data over a 12 month period through 16 interviews with key employees within the NPO, as well as a selection of agencies that had been involved with Tennant and a variety of Government departments in the areas of justice and health. We also inspected the documents used within the formal management controls, such as budgets, costing reports, programme management, and performance indicators. At VSO, we gathered data over a two year period through over 30 interviews with key employees, observations of meetings, and inspection of numerous reports, particularly those related to performance measurement practices. Over the period of the study at both organisations considerable amounts of data were collected. Due to confidentiality concerns, the findings at Tennant are based mainly on interview data with records and documents used to verify information from interviewees. At VSO, we are able to report examples of performance measurement practices in more detail. At the end of the both projects, we were involved, to a limited extent, in discussions as to how formal controls and performance measurement could be used in ways that did not damage internal morale and would enable the organisation to develop its social capital.

Our report is based on two case studies and while they are representative of other NPOs, care should be taken in generalising the findings to the whole sector. Also, while we were engaged with the organisations for extended periods (12 to 24 months) and observed business over this time, it is likely that the findings may change in the future as the NPOs adapt to their circumstances and gain further experience with management control systems and performance measurement. Notwithstanding these cautions we present findings that are likely to be pertinent to many NPOs.

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## Further reading

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