Municipal Auditing in Germany and Italy: Explosion, Change, or Recalcitrance?

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Abstract: By analysing two countries that have recently undergone NPM reform at the municipal level (Germany and Italy), our investigation challenges two popular notions: (1) that an audit explosion occurs as a result of reform, and (2) that reform causes change, i.e., that actors within a changing institutional context automatically adapt. Our empirically-derived observations are of (1) an audit implosion, and (2) institutional, cultural, and political conditions that trump any automatic adaptation to change. Indeed, these conditions – not audit reform per se – can shape the process and determine the direction of change. Recalcitrance, the stubborn resistance to and defiance of authority or guidance, is an interesting characteristic of some institutions. German auditors illustrate this nicely; our Italian case study demonstrates a mandatory dismantling of institutional inertia. By analysing the causal relationship between public management reforms and auditing, our research highlights the factors that prevent auditors from adapting to contextual change and factors that render obedience. We test Power’s audit explosion theory by operationalising it into five key components which are then evaluated within the landscapes of recent German and Italian municipal reform.

Keywords: municipal audit, audit explosion, New Public Management, Germany, Italy

INTRODUCTION

Balancing independence with control is a classic topic in the field of public sector research and the New Public Management-hype sparked a new interest in (performance) auditing (see Pollitt and Summa, 2002; and Hoggett, 1996).
primarily understood as assessment of performance goals and indicators of success, and a corresponding system of controlling and reporting (Gendron et al., 2007). In the last two decades almost every local government in an OECD-country has implemented some kind of New Public Management (NPM) reform (e.g., Kettl, 2005; and Pollitt and Bouckaert, 2004). This ‘wave of modernisation’ has in many cases changed the way governments and local authorities operate, and eventually also the audit regime. Although the NPM doctrine does not prescribe a well-defined list of reform steps, the stereotypical tool box includes privatisation, deregulation, outsourcing, service delivery competition, semi-autonomous service centers and – particularly in central and federal government reform – executive agencies, performance standards and measures, increased consumer power, and employment of professional managers and non-career personnel (see Hood, 1995 and 1998; Gruening, 2001; and Lapsley, 2008).

Auditing bodies, it is claimed, respond to NPM-type reforms by institutional, procedural, and cultural acclimation (see OECD, 1996; Pollitt, 2003; and English and Skærbæk, 2007). Increasing co-production of public goods and services by public, private and non-profit organisations seems to pose additional challenges to systems of public auditing that are supposed to counter centrifugal tendencies of decentralised agencies and public enterprises (Kettl, 2005; Wollmann, 2004; Hood, 1995; Pollitt and Bouckaert 2004; and van Wart and Cayer 1990, among others). The introduction of performance audits has been seen as one consequence of administrative reform (Pollitt and Summa, 2002; Power, 1997; Barzelay, 1996; and OECD, 1996). Some authors have even observed an explosion of auditing, which is not to be confused with quality of auditing (Power, 1994 and 1997; and Lapsley, 2008). However, scholars and evidence from countries such as the United Kingdom, the United States and Australia have mainly fuelled this discussion.

Insights from other countries, such as European ones, have not so prominently featured yet in the discussion. We therefore propose to turn the spotlight on two European countries in order to investigate to what extent public management reform has affected local government auditing in Italy and Germany. We explore whether the concept of ‘audit explosion’ appropriately describes and explains the changes that have occurred in Italian and German municipalities in the last ten years. By investigating pivotal theoretical assumptions of the audit explosion argument (e.g., Power, 1994, 1997 and 2005), this paper discusses the descriptive and the explanatory strengths of the audit explosion concept against the development in two countries outside the well-studied, early-reform Anglo-Saxon group, in order to draw a more nuanced picture of the reform-audit relationship.

We find, contrary to usual findings of an audit explosion that Germany to some extent, even characterised by an audit implosion at the local government level; we observe a reduction of auditors’ tasks and activities.1 The Italian case exhibits features characteristic of an audit explosion, such as a shift towards

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value-for-money audits and an increase of audit institutions. And instead of focusing merely on professional elites or accountability as drivers of change, our findings suggest that in examining change, attention should also be paid to factors such as political power games, the culture and identity of auditors, legal regulations, and the respective characteristics of the political system.

The analysis of the causal relationship between public management reforms and auditing, leads us to identify factors that constrain auditors from adapting to contextual change and those that foster compliance. As will be shown, New Public Management (NPM) alone cannot explain the direction, presence, or absence of change. Public management reform as the sole driver for changes in the audit system is therefore questionable (see also Pollitt, 2003) and NPM as the cause of audit change has had too much attention, leaving other factors – institutional, cultural, political – that shape a reform process, under-represented (e.g., Schröter, 2000). One important factor which can possibly explain such differences in how the audit systems have been regulated after the reforms is the institutional embeddedness of the municipal audit systems in the unitary Italian political system and the German federal system. By shifting the explanatory focus towards the implementation process of reform doctrines and emphasising the distinct nature of institutional embeddedness of audit systems in the political and administrative institutional context, our study identifies some limitations of Power’s audit explosion assumptions. In doing so, we advance the ‘audit society’ literature by characterising distinct transformative elements of local audit systems, which deviate significantly from the often debated and sometimes questioned Anglo-Saxon model(s) (Pallot, 2003).

Our case studies reveal (1) the historical process of institutional survival of auditors through adaptation of new tasks in Italy, and (2) a relative ‘enfeeblement’ of auditors in Germany. The paper therefore illustrates the different functions local public auditors play during restructuring processes and the institutional conditions that shape the direction of change. Our analysis also demonstrates the importance of institutional recalcitrance as an organisational reality, which can help to explain why institutions do not change. Institutional recalcitrance refers to an organisation’s stubborn resistance to, and defiance of authority or guidance. In general, the term describes obstinately uncooperative behaviour. Recalcitrance has also found its way into the conceptual vocabulary of the ‘old institutionalism’. Selznick (1949), in particular, refers to it to describe organisations’ ‘resistance to complete control,’ making ‘the use of organisational instrumentalities always to some degrees precarious, for it is virtually impossible to enforce automatic response to the desires or commands of those who must employ them’ (p. 10).

In the following section a brief overview of the research design and method is presented, and some challenges associated with the collection of data during the research process are analysed. The next section briefly describes the idea of the audit explosion and distils five assumptions from the literature to operationalise
the audit explosion concept. Two of the theses are descriptive (shift and growth); three are explanatory (accountability, supply side and facilitator). The third section presents a descriptive account of public management reforms in both countries, and their consequences for the local audit regimes. We conclude by comparing empirical findings to the key audit explosion components and discuss the implications of the findings for the status of local audit systems in the two countries.

Research Design, Method, and Hypotheses

For the purpose of this study a time-series, cross-sectional case study design was chosen (see Gerring, 2001, ch. 8), which allows us to compare the link between New Public Management reforms and changes in local government auditing during the past twenty years in two countries, which on the one hand started with similar reform programmes but on the other hand are characterised by very different institutional settings. The collection of evidence turned out, especially in the case of Germany, to be rather difficult as the field of empirical public auditing research has declined over the past twenty years and the field lacks in-depth empirical studies on the role and functioning of local auditing. Five audit explosion hypotheses are deduced from Power’s work and discussed against the background of evidence from official and unofficial reform documentation, results from other local study research projects, laws, and available statistical data. This combination allows us to sketch a detailed picture of the developments in local auditing in the two countries. This research engages ‘virgin territory’ and aims to start to modify the existing conceptual framework for further empirical research.

OPERATIONALISING THE AUDIT ‘EXPLOSION’ CONCEPT

In 1994 Michael Power introduced his concept of an ‘audit explosion’; his more elaborate ‘Audit Society’ was published three years later (1997; see also Scott, 2003; and Leeuw, 2000). Power criticised the audit society because it seemed to be an ideologically-driven system to discipline actors rather than foster accountability and was therefore, in the context of NPM rhetoric, deceitful (Power, 2000a). Power then elaborated on the idea of an audit society in which the audit explosion consolidates, becoming systemic and widespread (Power, 1997). It is not sufficient, he claims, ‘to quantify the amount of auditing going on’ (Power, 2000a, p. 122). It is more the spread of an idea, of an audit mentality, very often decoupled from its real effects on public sector accountability. Therefore, this fuzzy concept of auditing must not be understood as a natural reaction to the well-defined problem of accountability; rather, the very concept creates, constitutes, and shapes the public perception for which it is a solution (Power, 1997, p. 7). Power observes a paradoxical effect as a consequence: though auditing has received more attention during the last decade and is being practised in more areas of public life with more institutions and types
of auditing, it does not lead to an increase in trust in government. Rather, the opposite seems to be the case. Consequences and causes of the explosion have been widely debated by Power and other scholars (Humphrey and Owen, 2000; and Lindeberg, 2007). Consequences, Power identifies, include the political use of auditing by state executives for legitimacy and more perverse effects like the loss of a trust culture and the tremendous effort to make things auditable at the expense of getting things done (Power, 2000a and 2003; and Lapsley, 2008).

The theoretical underpinning of this claim is not evident because, as Power himself has since recognised, he does not provide a clear definition of audit. This has been criticised by a number of scholars, since without a precise definition of the concept, everything can be labelled as audit (Humphrey and Owen, 2000; and Lindeberg, 2007). In his more recent treatments of the topic Power has not delivered a precise definition, but talks of a ‘cluster of definitions which overlap but are not identical’ (Power 1997, p. 4). This is not a problem per se but can be understood as a consequence of the empirical development where the boundaries between audit, inspection, and monitoring practices have increasingly blurred. This leads Power to argue that the fuzziness in the idea of auditing is the precondition for its success in very different organisational contexts: ‘[T]he ambiguity is not a methodological problem but a substantive fact’ (Power 1997, p. 6). Therefore, by ‘audit explosion’ Power refers to ‘the growth of audit and related monitoring practices associated with public management reform processes’ (Power 2005, p. 326). As a multifaceted concept, the explosion is not only an increment in auditing activities in quantitative terms, but also a shift in qualitative perspective; mainly toward the so-called value-for-money audit and internal control systems (Pollitt, 2003; Power, 2003a; and Lapsley, 2008). It also means an increase in the number of oversight bodies in many different fields such as healthcare and education (Power, 2003a).

In order to test these observations in relation to municipal auditing in Italy and Germany, we operationalised the audit explosion concept by differentiating two descriptive and three explanatory assumptions stemming from Power’s reasoning: the (a) growth, (b) shift, (c) facilitator, (d) accountability, and (e) supply-side theses. The first two are descriptive, the others explanatory. In the following we describe what is meant by these terms.

(a) The growth thesis claims that a quantitative increase in auditing and related monitoring practices can be observed in various areas of public life, such as universities, museums, hospitals, and public enterprise (e.g., utilities). This is understood as a consequence of the rise of the regulatory state, which ‘shrinks to the role of monitor of last resort’ (Power, 1997, p. 66).

(b) The shift thesis places greater focus on value-for-money/performance audits. ‘Public-sector auditing oversight mandates in a number of countries were redefined in term of efficiency and effectiveness’ (Power,

(c) The facilitator thesis considers auditing a tool for modernising public organisations to meet fiscal constraints and the demand for better and less expensive public services. Auditors play ‘the central role in the operationalisation of the broad discourse of the NPM’ (Gendron, et al., 2007, p. 102) because they have the sufficient resources necessary for reforming the public sector. As a consequence, ‘political processes produced a need to know and realise efficiency in public services, and this in turn led to an expansion of audit mandate’ (Power, 2003b, p. 387). According to Power, ‘consulting is being designed into the audit process itself’ and ‘the audit/consulting distinction has become operationally unclear’ (Power, 2003b, p. 384).

(d) The accountability thesis refers to the increasing demand for accountability and transparency by the citizens driven by the fact that reforms tend to insulate public sector organisations from scrutiny (Pallot, 2003). ‘The audit explosion was also driven by related political demands on behalf of citizens, taxpayers, patients, pupils and others for greater accountability and transparency of service providing organisations’ (Power, 2000a, p. 113).

(e) The supply-side thesis argues that the rise of quality assurance practices coming from standards like ISO 9000 has caused or at least stimulated the audit explosion. ‘Quality assurance ideas, such as those represented in ISO 9000 and similar blueprints for good organisational processes, have a fundamental bearing on the audit/inspection explosion because they posit the creation of management control system’ (Power, 2003a, p. 189). Strong professional auditing and accounting elites and organisations have a financial interest in audit services and therefore encourage the use of those practices. There is, indeed, ‘an important supply-side dimension of the audit explosion: the existence of professional advisory groups. Able and willing to redefine what they do in the name of new political and legal mandates’ (Power, 2003a, p. 191).

Although describing an interesting picture of public sector auditing, the audit explosion theory has been variously criticised. The suggested causes of the explosion have been considered by some authors to be more descriptive than explanatory (Humphrey and Owen, 2000). Notwithstanding Power’s argument for success resting on a fuzzy concept of auditing, the lack of a clear definition of auditing is considered a weakening factor in the theory (Lindeberg, 2007). Furthermore, critics argue that Power erroneously dismisses the role of auditing practitioners facing the expectation gap. This relates to the fact that while the
public at large expects auditing services to be able to arrest, or at least detect unethical behaviour such as fraud or corruption, they are mainly designed to provide a professional opinion on financial statements without assuring the absence of integrity violations. Similarly, the idea of a conspiracy by the same professional groups to establish an audit society is *apertis verbis* denied by Power:

while accounting practitioners and others may be opportunistic there is no grand supply side conspiracy which drives the rise of audit (1997, p. 144),

but it appears clearly in his assertions that auditing is more than a simple technical matter:

[...], audit is not just a series of (rather interesting) technical practices. It must also be understood as an *idea*. [...]. Audit has become central to ways of talking about administrative control, the extension of auditing into different settings [...], is more than a natural and self-evidently technical response to problems of governance and accountability. It has much to do with articulating values, with rationalising and reinforcing public images of control (1994, p. 5),

and in the profession’s wish to enhance its discretionary space:

the existence of professional advisory groups able and willing to redefine what they do in the name of new political and legal mandates, thus being the emergent implementers of policy and the guardians of ‘best practices’ (2003, p. 191).

Power himself, on the other hand, has called for further research and development of the theory. One possible way to gain new evidence and offer alternative theoretical views is to analyse neglected cases and test theory in different institutional spaces (Power, 2003a).

**PUBLIC MANAGEMENT REFORM AND AUDITING IN GERMANY AND ITALY**

This section describes and analyses public management reforms in both countries, and their consequences for the local audit regimes by linking developments in Italy and Germany to the five audit explosion assumptions.

The plurality of NPM reform strategies aiming to transform bureaucratic administrative systems has been characterised as ‘maintain, modernize, marketize, and minimize’ (Pollitt and Bouckaert, 2004, p.186f.). Transforming the traditional Weberian bureaucracy into flexible, economic and effective organisations more like private enterprises resulted in what some observers now term the Neo-Weberian State (Bouckaert, 2004) seen in Belgium, Finland, France, and the Netherlands. Reform is somewhat apparent in Italy and Germany but their reforms have regularly been characterised as less radical (see Pollitt and Bouckaert, 2004). The neo-Weberian reform countries have introduced performance budgets, personnel flexibility, extensive decentralisation and devolution of authority, and quality standards for service delivery (Pollitt and Bouckaert, 2004, p.97). As reforms in Italy and Germany have been characterised along this line of a neo-Weberian remodelling they can best
be described as the result of ‘maintain’ and ‘marketize’ strategies (Pollitt and Bouckaert, 2004). While the benchmarks for comparisons in audit studies are mostly located in the Anglo-Saxon countries, research on countries like Germany and Italy – which have undergone ambitious reform on the local level in the past decade – has been neglected. Rather than minimising local government as, for example, in the United Kingdom; Germany and Italy have developed their own models of reform and results must therefore be assessed separately.

The subsequent descriptions of the Italian and German case will first offer a brief description of the audit system as such and then continue with an elaboration of the five assumptions highlighted above.

**Italy**

Auditing at the municipal level in Italy has been traditionally carried out by several separate bodies with intertwining responsibilities (Mussari, 1995). Every municipality has a compulsory auditing body called *Organo di Revisione* (OdR hereafter), in charge of auditing the municipal accounts, and a compulsory internal body known as *Segretario Comunale* (SC hereafter) (Law n. 2248 issued in 1865), whose main function is to certify compliance with the law for every administrative act and procedures proposed by both the city council and the executive committee. Finally, the Supreme Audit Institution (SAI hereafter), or *Corte dei Conti*, works as a special Court. It is composed of magistrates with the same constitutional privileges as ordinary judges. They are independent of the government and the parliament and subject only to the law (Italian Constitution art. 100 and 103). The SAI has two main functions. As an auditing body it checks the accounts of public sector organisations at all government levels to safeguard public finance (Santiso, 2006). As a Court it operates as a special tribunal for judging the misuse of public resources and discharging responsibilities for managers of public funds (OECD, 1996). Regional offices carry out municipal auditing but a national central office exists for coordinating the audit activities on autonomous local governments.

All three bodies existed before the reform wave, which removed a regional committee in charge of controlling municipal activities. Audit regulation is the same for all municipalities in Italy. In order to understand the effect of the reform wave on the municipal audit realm it is necessary to briefly describe its main features.

The Italian reform process was implemented through a vast and continuous flow of new legislation (Panozzo, 2000). The main reform processes in Italian public sector organisations began in the 1990s, some decades after active Anglo-Saxon countries (Mussari, 1997a; Capano, 2003; and OECD, 2001 and 1995). As a consequence of the local level reform processes, municipalities became more autonomous with respect to performance and expenditure (Mussari, 2002). Direct election, increased fiscal autonomy, and fewer transfers of money from the central state brought municipalities closer to citizens and, as was the aim, more
accountable to them (Mussari, 1997a). The law allowed public managers to spend public resources, creating a distinction between policy creators (politicians) and policy implementers (public managers) (Borgonovi, 2002). Management control, strategic control, and top management evaluation became compulsory for all municipalities and other organisations in the public sector in 1999 (Leg. Decree n. 286/1999).

In 2001 a reform of the constitutional framework equalised all levels of government. The state was no longer hierarchically superior to local governments, namely, regions, provinces, and municipalities (Cost. Law n. 3/2001). The old pyramid with municipalities at the lowest level was replaced with a flat structure; there are now no subordinate organisations. As a consequence, formal controls on municipalities’ activities carried out by regions and the state were removed. Accrual accounting was introduced at the municipal level and public service provision was strongly outsourced to companies with separate legal status, leaving the municipalities to provide only those services without economic relevance (Borgonovi, 2002).

Table 1 summarises the main effects of the reform on the three auditing bodies’ features and tasks. A more nuanced picture will be offered afterwards adopting the five assumptions previously identified to operationalise the audit explosion concepts and providing more details when necessary.

Our analysis begins by considering an increase in quantitative terms of audit services (growth thesis). Italy’s pre-reform auditing realm was focused only on the

**Table 1**

Audit Bodies Pre- and Post-Reform in Italy

<table>
<thead>
<tr>
<th>Pre-Reform</th>
<th>Post-Reform</th>
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<tr>
<td>OdR composed of elected city council members</td>
<td>OdR composed of professional certified accountants</td>
</tr>
<tr>
<td>OdR in charge only of compliance audit on municipal accounts</td>
<td>OdR in charge of compliance audit on municipal accounts and of offering performance consulting and auditing to the city council on municipal services performance</td>
</tr>
<tr>
<td>SAI composed of independent magistrates with an education in law</td>
<td>SAI composed of independent magistrates with an education in law and/or in business economics</td>
</tr>
<tr>
<td>SAI in charge of compliance audit on municipal accounts</td>
<td>SAI in charge of compliance and performance audit on municipal accounts</td>
</tr>
<tr>
<td>SC appointed by the Prefetto, the Central Government Representative in the Municipality</td>
<td>SC appointed by the Major</td>
</tr>
<tr>
<td>SC in charge of compliance audit of all juridical acts produced by the municipality</td>
<td>SC in charge of compliance audit of all juridical acts produced by the municipality</td>
</tr>
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</table>
municipal level, which was responsible for the production and provision of most local public services since autonomous organisations providing public services were not allowed by the law. Although joint stock companies and other private legal status organisations are now available for and often even compulsory for public service delivery, all such companies have their own auditors according to commercial law. Therefore, neither the SAI nor the OdR nor the SC is now allowed to carry out performance or compliance audits on them. On the contrary, only those bodies whose financial performance is included in the municipal financial statement have to be audited by the SAI, and of course by the OdR. Italian reforms narrowed the audit area by excluding outsourced provision of services, but performance audit was introduced at the municipal level. The more externalised the service provision, the narrower the audit mandate for both the OdR and the SAI, and considering the number of municipalities in Italy (8101), this would mean more time for performance audit at the core municipal level. The reform effect could be summarised as ‘less audit area, more audit depth’. Reality, however, is proving this outcome to be partially false: many independent service-providing companies are totally owned by municipalities and therefore they are included in the municipal accounts and they are subject to compliance and performance audits. In cases where one municipality has several companies, audit work is thus multiplied. This means that an audit explosion took place at municipal level.

This conclusion is confirmed also moving to the second assumption (the shift thesis). Pre-reform the OdR was responsible only for compliance audit of municipal accounting. The 1990 law widened its role, adding the duties of (1) offering suggestions concerning efficiency, effectiveness, and economy after assessing accounting system reliability and resource spending; and (2) assisting the city council in directing and controlling municipality management (De Robertis, 1992). The SAI’s auditing of municipal financial reports began in 1982 with Law. n. 51, which mandated that all local governments with more than 8,000 inhabitants send their financial statements to the SAI. It was merely a compliance audit. Nevertheless, since 1958, the SAI has been auditing those organisations receiving state financial resources through the compliance audit of their financial statements; municipalities were therefore part of this realm.

In 1994, during the reform season, law n. 20 clarified the competences of the SAI as auditor for municipalities conducting a performance auditing of right and obligations (Manin Carabba, 1998; and Zavagnin, 2004). Since 1994 efficiency and economy-focused performance auditing has become an SAI responsibility on top of its traditional role as a special Court for criminal accounting. Together with wider responsibility related to the Stability Pact, the SAI now audits performance, task fulfilment, and internal control systems adequacy (Art 7.7 law n.131/2003). The SC’s main function is to certify compliance with the law for every administrative act and procedure proposed by the city council and the executive committee. The reform wave had no influence on SC duties and it

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remains an internal compliance auditing body. The overall picture shows a clear
tendency for a shift toward performance audit at municipal level and also the
creation of a hierarchical relationship between OdR and SAI, where SAI appears
to be the stronger player in the field with the power to impose information duties
on the OdR and call it as a witness in Court trials.

The third assumption of Power’s theoretical framework suggests a facilitator
role of auditors to modernise public sector organisations (facilitator thesis). Again,
this assumption can be confirmed by interpreting one of the main reform
effects, namely the change of the composition of the auditing bodies as a way to
foster managerialism even at local government level. In particular, before the
reform era, OdR comprised three elected city council members without executive
responsibilities (art. 309 R.D. 383/1934). Since the city council members were
ordinary citizens, there were no special prerequisites for appointment. In 1990,
however, members of the OdR were required to be professionals educated in
business and economics (law n. 142/1990 art. 57). The OdR now comprises
a private-sector certified auditor, a certified accountant, and a professional
accountant, all appointed by the city council. Each of these has special lists and
examinations to be listed in (law n. 142/1990). In other words, they are external
auditors, formally independent of the municipality executive, constituting an
extended arm of the city council to monitor executive activities. They can be
dismissed only if they do not fulfil their duties, and their suggestions have to
be taken into consideration by the city council. The Italian literature on the
topic agrees with considering auditors as a means to introduce managerialism
into municipalities traditionally rather unresponsively to managerial innovations
(Persiani, 1996; Marchi, 1997; Galeotti, 1997; Zavagnin, 2004; and Mussari,
2005).

In particular, the duty imposed by the Law on the OdR to assist the city council
in directing and controlling municipality management to reach greater levels of
efficiency and effectiveness represents a clear example of the facilitator role in
Power’s terms since auditing is used as a tool to modernise administrations. The
SAI, due to its peculiar characteristics and role in the Italian judicial framework,
remained unchanged with respect to composition but over time undertook wider
competences (Corso, 2006; and Cerulli Irelli, 2006). In recent years, the SAI
magistrate selection has been open to candidates holding business and economics
degrees together with traditional law degrees. They are completely independent
of the municipality. Although this may seem a small change at least in general
terms, to equalise degrees in business and in law as a basis of employment in the
SAI represents an important breach with the past. And this is not only a matter
of providing the Court with a stronger accounting and managerial knowledge
base, but it is also a way to enable the Court to formulate a greater number of
managerial judgements and advice to local governments.

SC composition has not changed, but the appointment process has been
modified. Up to 1997 the SC was appointed by the Prefetto, the central
government representative in every Municipality, which manages the list of
qualified people (art 102, Leg. Decree n. 267/2000). Qualifications remained nearly the same. In every municipality, the mayor appoints the SC from the list, setting up a trust-based relationship. SC members must have law degrees. At the same time, it is interesting to note that the Law allows small local governments, with less than fifteen thousand inhabitants to employ the SC also as a General Manager assigning him/her also managerial duties (art. 108.3 Leg. Decree n. 267/2000). In this case, the role as facilitator for modernisation is again clear since the main traditional duty of SC is internal consulting.

The fourth of Power’s assumptions is about a demand for accountability coming from citizens (accountability thesis). In the Italian case, no strong demand from citizens has been observed. At a formal level, the city council, which represents all citizens of the municipality, is the main recipient of information coming from the audit activities of the three bodies. In 2006 a new regulation gave the OdR the duty to report auditing results to the SAI as well as to the city council at the end of every fiscal year. Being an internal auditor, the SC provides the city council with information concerning the activity of the Executive Committee. Although a Freedom of Information Act has been issued, no audit results are currently disclosed directly to citizens. The accountability gap for citizens is currently being addressed by local governments through voluntary, social and environmental disclosure (Marcuccio and Steccolini, 2005). Again even the supply-side thesis does not seem to apply in the Italian case. Since the reform was supporting a new professionalism, professional advisory groups have not been able, at least at the beginning, to organise themselves in order to operate as a lobby. After the 1990, Italian municipalities, even the very small ones, needed professional auditors, as prescribed by the new law. Coordination and agglomeration in a representative (and able to lobby) group of the thousand newly appointed auditors was quite difficult in the beginning also because they came from different (and sometimes conflicting) professional groups (i.e., certified accountants and professional accountants were at times split into two different associations). Moreover, since financial audit in municipalities was a completely new task for most of them, their main concerns were technical in the beginning even considering that while municipalities adopt a modified cash accounting base, in private sector full accrual is used.

Finally, standards like ISO9000 are scarcely applied by Italian local governments because official guidelines for applying ISO9000 to local governments were released only in 2002 while the reform wave started several decades before. To summarise, the Italian case partially confirms Power’s theoretical framework, showing an increase in auditing at municipal level, a shift toward a greater attention to performance audit and also a political use of it to modernise administrations. The picture is nevertheless somehow different from Power’s framework since the expected strong demand for accountability by the citizens does not appear to be present and also the supply side argument seems to be weak.
Germany

The so-called New Steering Model (NSM) in German local government modified the existing bureaucratic system by adapting accounting systems to private sector standards, decentralising service delivery, and introducing purchaser-provider relationships, output standards for policy formulation, and flexible personnel management and appraisal systems (see Bogumil et al., 2007; Kuhlmann et al., 2008; and Ridder et al., 2005). One important element was to decentralise administrative departments into intermediate forms, for example, public enterprises or new accrual accounting standards on local and state levels though not (yet) on the federal level. While Italy stands for a clear, coherent, and visible link between central state reforms and changes to the audit system, Germany, despite fifteen years of public management reform on the local level (see Reichard, 2002; and Röber and Reichard, 2001), is the opposite.

In the federal German political system (Moore and Jacoby, 2009), municipalities practice local self-administration, guaranteed by Article 28.2 of the German constitution and the 16 state constitutions. This status is an integral element of vertical federalism (Knemeyer, 1997). It protects municipalities from state interference, which does not mean that each municipality chooses its own institutional setting. Quite the opposite: the structure of responsibilities and administrative, mayoral, and local auditors’ duties and rights are stated by the local government code according to Article 70 of the federal constitution subject to state law (Fiebig, 1998). Thus in a number of states, e.g., Lower Saxony or North-Rhine Westfalia, and depending on the size of local communities so-called county audit offices oversee municipalities with respect to local governments’ legal compliance with state law (Schwarting, 2006). Furthermore, the local government code is the basis of the municipal financial management and supervision of local governments by the states (Birkholz, 2008). The code is also the legal foundation for the creation of local audit offices. Though the existence of 16 different local government codes in 16 different states hinders drawing general conclusions about local auditors in Germany, there exists a relatively high uniformity in the principles and institutions among the codes (Fiebig, 1998).

Formally, it is the logical consequence and extension of the city council’s budget rights to audit the financial management of the municipal administration (Fiebig, 1998). In its democratic function as the representative organ of the municipality’s citizens, the city council controls financial management with the support of the local auditor, who is directly accountable to the city council’s audit committee (e.g., §104 (1) GO NW). State-specific differences notwithstanding, the common denominator among all local governments in Germany is the right of the city council to oversee the financial management of its administration. Their auditors enjoy a high degree of independence (Fiebig, 1998), which is supposed to guarantee objective support of the council. Certain institutional elements strengthen this position. For example, the head of the audit office
and its members are directly appointed by the council; their dismissal is not an easy process; they are independent in what they audit and subject only to law; and they report directly to the council (Fiebig, 1998). All this grants municipal auditors a special and unique status (see Schwarting, 2006). Along with this comes a high culture of independence. This is an important characteristic of local auditors and their reputation is of a *habitus* that is traditionally elitist, non-cooperative, hierarchical, and compliance-oriented (Maravic, 2007). Furthermore, most auditors have traditionally received law training, which explains their focus on compliance and recalcitrance toward NSM reforms. The new generation of auditors, however, supposedly receives more balanced training, e.g., courses in accrual accounting instead of receiving training in cash accounting for the traditional cameralistic system (Ridder et al., 2005).

As the extended arm of the council, German local auditors conduct compliance audits to ascertain administrative compliance with budget and resource spending rules (Budäus et al., 2003; Fiebig, 1998; and Schwarting, 2006). So far it has not been the local auditor’s task to consult other departments regarding questions of financial or procurement management. In this respect public auditors of municipalities differ significantly from the audit courts at the federal (*Bundesrechnungshof*) and state (*Landesrechnungshöfe*) levels (Zavelberg, 1996; and Blomeyer, 1999). The council charges the auditor with special audit requests and can control their access to the municipal civil law companies. In many states, the council *may* demand the auditor to oversee the ‘appropriate and efficient’ (*Zweckmäßigkeit und Wirtschaftlichkeit*) (Budäus et al., 2003) use of financial resources, but the task is not included in the standard operating procedures of the auditor (GO NRW §103(2)1–5), its clear growth in importance notwithstanding. The reason lies more in the area of budget constraints and financial pressure than in the implementation of a performance audit as an inherent part of a reform concept. Performance audit must be defined separately by the council and is not obligatory.

Audit competencies are laid down as an object of the contract in the partnership agreement between the municipality, a newly-founded public enterprise, and its private partners. As a matter of fact, auditors in German municipalities have either limited or no legal competences to audit public enterprises based on civil law, such as public-private partnerships, public limited companies and joint stock companies. Their legal competences to fully audit an institution, meaning unlimited access to data, are clearly restricted to the core administration and enterprises based on public law (Schwarting, 2006). Considering that municipalities experienced massive decentralisation in the last decade, substantial human and financial resources have been devolved to public enterprises (Edeling and Reichard, 2003). Recent findings show for some municipalities a de-facto shift of procurement resources from the core administration to public enterprises of up to 80% (Maravic, 2007). Ultimately, auditing is a question of political will and audit arrangements. This means that the city council can charge the auditor with auditing the municipality.
as ‘shareholder, stock owner or member in companies and other civil law consortia’ (GO NRW §103(2)5). The problem lies in the actual application of these regulations. The incentives for council members are, generally speaking, not high as they themselves often serve as representatives of the council on the board of a civil law company owned by the municipality (Machura, 2001, p. 82). Attendance at meetings of the supervisory board and shareholders are not publicly available. Members of the supervisory board, mostly politicians and public servants, are bound to secrecy, are not allowed to inform the city council of confidential matters, and auditing is restricted to limited compliance audits.

Against this background we now turn to the discussion of the five audit explosion propositions. With the increasing quantitative importance of decentralised service delivery (Reichard, 2002), local German auditors’ responsibility has decreased. In a recent survey of 38 municipal auditors (Maravic, 2007), auditors were asked about the development of their mandate to audit different public enterprises. Respondents perceived a reduction of public supervision of civil law enterprises. They complained that an increasing complexity of legal and technical questions in contracting-out public services has created a sharp contrast between real audit demand and actual municipal audit capacity. This is supported by the following figures: with respect to the legal competencies of audit departments in the past five years, 10% of the surveyed auditors had to accept a limitation of their audit rights; 29% said that their legal competences to audit public enterprises had widened; 61% reported no change, and 14% were non-responsive (Maravic, 2007, pp. 460–67). The extension of audit rights in some municipalities can be regarded as an indicator for the necessity to counter the perceived audit vacuum. Forty-two percent of the audit departments were confronted with a reduction of their personnel; none experienced an increase; 58% reported no change. The financial resources for audit tasks show a similar trend. Twenty-nine percent faced financial cutbacks; 70% saw no change, and none saw an increase. These figures document a development characterised by increasing audit complexity coupled with a decreasing audit capacity of municipal auditors (growth thesis). Reducing the public auditor’s legal, personnel, and financial resources seems to run counter to decentralising public service delivery to public enterprises. Against these findings we can conclude that quantitative growth does not seem to be likely, instead a decrease in capacity and influence must be acknowledged.

German local government reform promoters, such as the very influential Local Government Institute in Cologne (KGSt), have advocated a new role for auditors as consultants (KGSt, 1997; and Richter, 1997). Generally speaking, the general status of auditors’ independence described above has not been under attack by the reform doctrine of the New Steering Model (NSM) itself, but the function of auditors has been subject to debate among reform advocates, such as the KGSt as the inventor and firmest supporter of the NSM (KGSt, 1997) and auditors themselves. The KGSt therefore, does not plan to change the legal status of
auditors (such as independence) (ARH, 2001), but her formulated reforms with regard to the auditors’ functions within the NSM. As the public auditor of the municipality is not a formal part of the administration, auditing stands outside the bureaus envisioned by the KGSt to play an integral role in local government reform (KGSt, 1997, p. 12).

This idea rested not in a shift from compliance to value-for-money-audits (shift thesis) but in a shift from ex-post audit towards ex-ante consulting (Bekemann, 2006), where auditors advise other departments in streamlining processes for more efficient management of financial resources. This vision is similar to the ‘trojan horse’ idea we found in Italy where auditors take the role of internal consultants. An initial suggestion by the KGSt proposed reforms around three aspects: auditors (1) are part of the internal controlling system, (2) act as consultants to other bureaus, and (3) draft expert reports for the council and administration head (KGSt, 1997, p. 13). On the basis of interviews with informed experts in the field of local government auditing from the KGSt as well as with the public auditors of the municipality during the past four years, we see no implementation of this vision in local government as auditors firmly opposed the idea of becoming part of the ‘extended arm of NSM reforms’ (facilitator thesis). Auditors have been the firmest critics of the NSM from the outset, and more able to resist these reform attempts than others in most of the cases.

Their structural independence has protected them against these reform attempts. A shift towards more value-for-money audits cannot be verified for the German case. In Italy reformers succeeded to use auditors as ‘reform facilitators’, in Germany reform advocates did not succeed very often. One reason for the failure of reform in Germany must be seen in the special legal status of auditors as the ‘extended arm’ of the council, which has protected them. In addition, their culture of independence has made them resistant to become ‘reform facilitators’ (Fiebig, 1998; Bekemann, 2006; and Schwarting, 2006). However, the flipside of the coin lies in the fact that what seemed to be an asset in the first place – institutional protection of the independent status of German municipal auditors – has turned out to be a burden; a disadvantage to their institutional survival. The more auditors have resisted change, the less politicians and reform advocates consider them viable partners for decentralisation or privatisation. Inevitably, they were often outplayed in the political power game, and their audit capacities have failed to adapt to the new situation of decentralised local governance (Bogumil, 2001).

Last but not least, we consider two theses of Power’s audit explosion concept – accountability and supply-side thesis – that can account, together with the facilitator thesis, in Michael Power’s eyes for the audit explosion. As for the German case, there has been no evidence so far for either a quantitative growth in auditing nor a significant shift towards value-for-money audits or a turning of auditors into reform facilitators. In addition, both attempts to establish a causal link between the assumed explosion of audit and a growing demand for more accountability or a supply-side pressure by accounting firms, cannot be easily validated for
the German case. With regard to the supply-side pressure of accounting we observe no scientific evidence for activities of these firms lobbying for more audit in the core administration. However, considering the financial incentives of auditing public enterprises, one can only speculate that these firms are not disinclined in doing more auditing rather than doing less. A specific lobbying for more cannot be observed in the case of Germany. With regard to a growing accountability demand by the public, it must be said that a growing number of public corruption and fraud scandals in municipalities during the last decade have, of course, sensitised the public for these issues, and has raised the public’s awareness for unethical behaviour in the public sector (e.g., Behnke, 2004).

DISCUSSION OF FINDINGS

Does the concept of ‘audit explosion’ describe and explain the changes that have occurred in Italian and German municipalities in the last ten years? We now compare the theoretical assumptions of the audit explosion argument with the empirical findings in the two countries. We show if and where the descriptive and the explanatory strengths of the audit explosion concept fit. Instead of focusing merely on professional elites or accountability as drivers of change, we pay attention to factors such as political power games, the culture and identity of auditors, legal regulations, and the characteristics of the political system.

Italy and Germany both faced relatively intense reform pressures that clearly resulted in changes of their audit systems at the municipal level – but in opposite directions. As has been demonstrated, we need to be cautious about assuming causal relationships in the case of parallel developments. In our case study, Italy shows a clear, coherent, visible link between central state reforms and changes to the audit system; Germany, despite fifteen years of public management reform at the local level, exhibits a highly fragmented reform landscape with – *prima facie* – no direct links between institutional change and the adaptation of new auditing instruments. On closer inspection the German reforms do somewhat mimic the Italian reform doctrine in invoking the auditors’ new role as consultants or internal advisors to promote efficiency by restructuring other municipal departments’ processes.

The descriptive assumptions of the audit explosion theory considered (1) quantitative growth of auditing and (2) a shift from compliance to performance auditing. Power’s definition of audit explosion is so conceptually broad it can be applied in the two selected case studies, that is, in countries where changes have taken place in public auditing at the municipal level. In quantitative terms it is difficult to show an increase and even more difficult an explosion of auditing in both countries. The opposite seems to be true at least in Germany where we see rather a *reduction* of auditing in many municipalities. Though there is no collapse of auditing in either country, we observe a decrease of audit activities at least with regard to the public auditor in local government.
Italian municipalities’ audits are observed to be narrower (due to the exclusion of the companies with legal status) but deeper (due to the introduction of performance audits and the increasing number of bodies delivering audit services). The explosion in quantitative terms takes place in Italy just because many of those companies with legal status are still totally owned by the same municipalities and this allows auditors to check accounts. Nevertheless, at least on a formal juridical level, privatisation of services means a quantitative decrease of municipal audit.

The German auditors’ realm also narrowed due to decentralisation of service delivery but experienced no shift towards performance auditing. That means the shift thesis – which predicts an increase of performance auditing for efficiency (or value-for-money), only partially describes reality. Only in Italy can it be identified as a consequence of the reform. In the German case, performance audits have a long tradition, but the compliance perspective remains dominant due to the strong legal traditions (see König and Siedentopf, 2001). We therefore conclude that in the Italian case the growth and shift theses are plausible but not accurate; the German case shows neither growth nor shift (see Table 2).

Turning now to the remaining three assumptions regarded essential to the audit explosion argument, we look at auditors as reform advocates (facilitator thesis), a demand from citizens (accountability thesis), and pressure from professional elites (supply-side thesis).

Auditors in Germany have stoically resisted the imposition of a role different from the traditional one (Power, 2003a, p. 192). Since both are Roman law countries, regulation is a powerful tool to weaken or empower auditing. In Germany, pre-reform institutional protection regulation offered municipal auditors an independent status and prerogatives to defend. Institutional recalcitrance was an observable trait in German municipalities with respect to auditing. We might say that the reform wave was not strong enough to bend the will of auditors to behave as internal consultants to foster managerialism in municipalities; auditors stoically resisted the new duties, which in many municipalities led to a loss of their former power. In Italy institutional protection regulations for the OdR were a product of the reform. Regulation formally issued a

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professional and independent OdR, but immediately used the body to facilitate managerialism at the municipal level, practically curtailing its independence (Gendron et al., 2000). To retain control on municipal activities, regulation widened the auditing responsibilities of the SAI whose institutional protection is established in the Italian constitution and therefore difficult to change. The OdR was not strong enough to resist such a warped implementation, and is increasingly more of a consulting than auditing body. A stronger sense of role identity and how institutional protection regulations were put into place in Germany can explain some of the dissimilarities between the two countries.

Another reason that the audit explosion theory seems not so well designed to describe and explain changes in either country lies in the fact that it tends to overestimate the role of professional elites and underestimate some important peculiarities of Roman law countries, namely, the role of (institutional protection) regulation. With regard to the supply side thesis we may state that the two case studies do not show any particular pressure coming from professional auditing or accounting groups for more auditing services; German public auditors do not even have an association, thus supply-side pressure appears to be weak or non-existent, contrary to suggestions of the Anglo-Saxon literature.

The increase in audit institutions in Italy can be seen in what some scholars refer to as the political use of auditing by the central state. In particular Bowerman et al. (2003) suggest a political use of audit regulation carried out by politicians to avoid oversight of their activities. Even more critical is Funnel’s (2003) work claiming an ongoing battle between auditors and politicians with the latter using auditing to make questionable political decisions appear technically sound. The political use of auditing can be observed in both countries though on different government levels and with different aims. With regard to the central state perspective, audit has been used in Italy to control municipalities, which have become in the course of regionalisation and political decentralisation increasingly autonomous, and have been granted a new constitutional status. In Germany the Federal State (see, Benz, 2008; and Moore and Jacoby, 2009) apparently has neither a strategy nor the constitutional right to increase control on municipalities by means of creating new audit institutions or by granting the supreme audit institution (Bundesrechnungshof) a mandate to audit municipalities (Budäus et al., 2003, p. 290). At both countries’ municipal levels, politicians tried to resist increased oversight by auditors. In Germany they played on the object of control; in Italy politicians relied more on the ( politicised) appointment procedure of auditors.

The comparison of these two countries emphasises the primacy of contextual factors such as administrative culture and legacy political systems. Federalism plays an important role in Germany; though widely debated, it seems to be still on its way in Italy, not yet changing a fundamentally centralistic state. This explains to a certain extent why Italy has a single municipal audit model while
Germany is more difficult to characterise. Similarly, a centralist state probably tends to maintain a tighter grip on municipal activities, especially in the process of devolution; a federal state already accepts the notion of giving discretional decision-making powers to other government levels.

Finally, the picture of an audit society appears realistic in our two case-study countries. The conclusion rests first on the descriptive portion of the audit explosion argument and not its explanatory strengths, which are weaker. With respect to Power’s observation that people trust government less despite a quantitative increase in auditing, we now know the complementary and interesting fact that auditing is increasingly used to deal with mistrust between governmental institutions. In Italy, ‘control of control’ is a reality, even ‘auditing of auditing’. When the law states that SAI must audit an OdR-audited document, there appears to be no trust in OdR’s capacity; the central state is requiring that the audit of municipal accounting documents is audited. Whether citizens’ trust in public institutions is, as suggested by Power, declining despite an increase in auditing cannot be answered here. In neither country can auditing be considered a tool to increase public trust. Public audit information is limited and, generally speaking, citizens do not show much interest in such technical issues. At this moment, we therefore doubt that there is any link between audit reform and citizens’ trust in public institutions – whatever the quantity of auditing. We cannot, however, deny that zealous media coverage of corruption cases and scandals for public consumption seems to have led to an increase of discrete anti-corruption institutions and processes in both countries.

By matching the underlying theoretical assumptions of the audit explosion theory with developments in the field of auditing in our two cases, we have shown that the audit explosion argument has some descriptive strength in Italy and none in Germany, especially with respect to the growth and the shift theses. The explanatory elements of the audit explosion argument do not explain the direction of change in either country. Nor is a change in audit systems itself a stand-alone variable: political, legal, identity, and power-game factors are profound considerations in deriving a satisfactory explanation of the changes observed in Italian and German local audit systems (Ahrens and Chapman, 2000; and Robson et al., 2007).

CONCLUSION

Power’s work provides a solid ground for further comparative research; but not everywhere. One needs to carefully distinguish between different explanatory as well as descriptive elements of his audit explosion concept in order to extract the heuristic juice of its appreciation. His descriptive as well as explanatory assumptions seem to be able to capture pretty accurately the developments in Italy but fail to do so with the developments in Germany. Our research applied Power’s audit explosion concept to areas previously neglected.
in current discussion on NPM and auditing. We showed that Italy and Germany offer evidence for challenging the underlying conceptual assumptions of the audit explosion theory. The test operationalised Power’s concept with five assumptions: the quantitative increase in auditing, a shift toward performance auditing, the adoption of audit to facilitate NPM reform, a supply-side increase of audit services, and the impact of an increase in auditing on public accountability. All five were tested in the two countries with respect to modifications of municipal auditing by reform processes and their effects. As was demonstrated throughout, auditing reform may have occurred in Italy and Germany in the last decade but it cannot be explained by simply borrowing concepts developed within other contexts because they do not embrace the complexity of the phenomenon. In other words, our results only partially confirmed Power’s theory. Despite this differentiated picture we are convinced that Power’s concept can be partly applied beyond the country context of the United Kingdom and adds value to the analysis of audit reforms if applied carefully.

Our research contributes to the debate in several ways. In descriptive terms, it is one of the first contributions to reform effects of municipal-level auditing in non-Anglo-Saxon countries. It also provides a comparative view of the two countries on the basis of Power’s theoretical framework of an audit explosion. As a theoretical contribution, we countered the popular notion that actors operating within a changing institutional context automatically adapt to it. We highlighted factors which prevent auditors from adapting to contextual change and those that foster obedience. For example, the institutional configurations of the Italian unitary political system facilitate rapid and radical audit changes, whereas the horizontally as well as vertically fragmented institutional nature of the German political system seems to moderate the impact of paradigm shifts in the municipal audit system. Institutional, cultural, and political conditions contribute to shaping the process and determining the direction of change. In some contexts, recalcitrance – the stubborn resistance to and defiance of authority or guidance – can be an interesting characteristic of institutions, and merits further consideration. Institutional recalcitrance is nicely illustrated in the case of German auditors; Italy demonstrates the outcome of a mandatory dismantling of institutional inertia.

For reasons stated above we therefore suggest that future research in the field of public audit reforms turns more attention to the moderating or facilitating effects of political institutions, power games, and politics to learn more about the political nature of reforms. Furthermore, we consider it necessary to extend the empirical research on audit reform to other neglected European counties, for example, the new EU accession countries in Eastern Europe, as similar reform doctrines have been propagated in most of these countries. Last but not least, we would like to invite other researchers to draw on the conceptual advances this research offers in order to enhance comparative and theory informing research.
NOTES

1 We use here the term of ‘implosion’ in a different way from Power’s (2000) contribution. He refers to it meaning an increasing tendency of organisations to rely on internal audit systems and on self-regulatory capacities to control risks (Power, 2000b). In this paper, implosion will be used to mean a reduction of auditor’s tasks and activities.

2 By institutional embeddedness we mean the characteristics of the relationships existing between the municipal audit system and the general administrative context of the two countries.

3 The so called Anglo-Saxon model refers to a well known literature based classification of countries particularly used to distinguish variations on NPM reforms implementation. According to the literature, Anglo-Saxon countries are distinguished by European continental countries for several characteristics: the adoption of a common law system, a governance system with strong parliamentary powers (Westminster –based) and so on.

4 In some states, e.g., in the state of Thuringia or Rhineland-Palatine, the auditor is subordinate to the mayor though the auditor is independent in the way he conducts the audit (Schwarting, 2006 and 322).

5 This means that only one-fifth of all tendering activities take place in the traditional core administration.

6 The data set used in this article is built from an anonymous survey conducted in spring 2004 with the cooperation of the Local Management Institute (Kommunale Gemeinschaftsstelle für Verwaltungsvereinfachung, KGSt), Cologne. A brief description of the research project was published in the KGSt newsletter in March 2004 (KGSt Info 2004) and municipalities were asked to participate in this survey on corruption. Questionnaires were send to 40 municipal auditors. The selection-criteria are municipalities of different sizes and with a different quantity of public enterprises. In the sample there are seven municipalities with less than 50,000 inhabitants, twelve with a size of 50,000 to 100,000, seven with a size of 100,000 to 250,000 and twelve municipalities greater than 250,000 inhabitants. In total, 38 local auditors answered the questionnaire. The questionnaire contained questions with standardised as well as open answers. The open questions were chosen to allow the respondents to explain their opinion and leave room for explorative investigation of this subject. This paper cannot document all answers and explanations given by the respondents (see von Maravic, 2007, for details).

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