



The Implementation of FMC : SIGMA Experiences

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1. Key Features FMC

Two key features are:

1. Financial management
2. Financial control ,though is just a part of financial management.

CHU focus is usually on the application of the COSO standards. These standards can only be effective with the development of managerial accountability. Applying the COSO standards involves the application of financial management.

Financial management, and therefore financial control both depend upon the existence of managerial accountability.

In summary the establishment of managerial accountability is fundamental to FMC reform – it cannot be a later ‘add-on’.

2.1 What is financial management?

Financial management is about ensuring that the management of public financial resources is carried out to the highest levels of efficiency and effectiveness, along with integrity and transparency.

This immediately raises these questions:

1. Who is the manager?
2. Who is responsible for achieving objectives?
3. Who is responsible for efficiency and effectiveness?
4. Who is the financial manager?

The reality is that there is a hierarchy of management – the top manager has overall responsibility and each manager below the top manager has his/her own responsibilities.

Each manager is responsible for:

- achieving the objectives for the relevant area ;
- efficiency and effectiveness;
- the quality of financial management within his/her area of responsibility.

2.2 What is financial management?

There are two key messages in establishing financial management:

First managerial authority has to be delegated from the top manager (there has to be a management structure).

Secondly, the manager is responsible for financial management or efficiency and effectiveness and not the finance officer.

This then requires, for example, that:

- Managerial structures and budgets within public organisations are aligned with programmes;
- Budgetary control by the MoF exists but at no lower than the second level of classification of expenses, because managers require discretion;
- Budgets are delegated **in whole** to managers within organisations;
- Managers understand what they are to achieve – they have objectives and are made accountable.

Treasury control should be primarily concerned with cash management. Expenditure control should lie with each public organisation.

3. What is financial control?

Financial control is usually interpreted as the COSO elements i.e. the control environment, risk assessment , control activities , information and communication, monitoring and CHUs require appropriate procedures to be implemented.

COSO presumes that managerial accountability exists, that is, that:

- Objectives and performance standards exist;
- Operations are being carried out efficiently and effectively;
- Financial reporting is reliable;
- Compliance with applicable laws and regulations is achieved

Each of these are essential for financial management

COSO exists to reinforce these to provide confidence to 3rd parties.

A single manager is responsible for overall performance but to achieve that he needs a quality organisation to help him. A single manager cannot make all decisions.

So managerial accountability is a pre-requisite for all FMC reform.

4.1 Pre-requisites for successful FMC reform

The emphasis upon the relationship between FMC reform and management means that **FMC reform should be treated as another aspect of public administration reform (PAR)**

This assumes that PAR

- Works on the same managerial principles as FMC, that is, delegated managerial authority for operational decisions and the management of budgets with accountability for decisions that are made;
- Establishes managerial structures with delegation arrangements at all levels within organisations;
- Allows for the exercise of discretion and the taking of controlled risks;
- Addresses the main problems that prevent managerial accountability from developing, namely a lack of trust and loyalty;
- Recognises that FMC totally changes the role of the financial officer from that of controller by adding financial policy and adviser;
- Operates to a timetable that is co-ordinated with FMC reform.

4.2 Pre-requisites for successful FMC reform

Managers recognise that they are primarily responsible for:

- financial management and not the finance officer;
- achieving objectives in an efficient and effective way ; and
- therefore must have the tools available to enable them to fulfil these responsibilities.

With traditional administrative systems the administrator has one financial variable i.e. that spending does not exceed the budget.

With FMC the manager has three variables:

- The budget limit;
- The objective;
- Efficiency and effectiveness.

As the manager under FMC is responsible for managing three variables the manager requires far more sophisticated financial information than is available from the treasury system.

At the same time the manager is also responsible for identifying and managing risk, so he also requires financial assessments associated with risk.

4.3 Pre-requisites for successful FMC reform

The role and position of the chief financial officer (CFO) also changes with FMC and must be clearly defined: the CFO is:

- a financial adviser to the manager including about fiscal and other risks being undertaken or considered;
- a provider and analyser of financial information including whatever cost and management information is required by the manager;
- preparing strategic financial plans to generate awareness of the long run consequences of policy decisions along with current activities;
- ensuring that the internal financial control standards are maintained and remain relevant throughout the organisation;
- assessing the financial viability and if necessary challenging inappropriate decisions.
- Ensuring that the financial control standards specified by the MoF are being properly applied.

(The financial officer may have other responsibilities as well.)

This is much more than a financial controller role and is a high status policy role.

4.4 Pre-requisites for successful FMC reform

Ensuring that FMC reform is treated as another aspect of public expenditure management reform; that means that budgetary and treasury reforms are compatible with FMC reform and that the timing of those reforms is compatible with the FMC reforms. (FMC is about budget execution!)

But very often budgetary, treasury and FMC reforms are treated in isolation, yet budgetary and treasury reforms can have a significant impact upon FMC.

This may also mean that the accounting information available from the treasury system is inadequate for their requirements and that specific accounting information systems, including cost and management accounting systems also need to be developed.

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5. Pre-requisites are not fulfilled. Why?

1. **No linkages between PAR/PFM reform and FMC reform.** FMC is an essential complement to PAR and to budgetary and treasury reform. However, in practice FMC reform is often just seen as a bureaucratic reform of interest only to finance officials and then is about financial control procedures. The 'vision' about the need for FMC is lost.
2. **Limited powers CHU.** The CHU is not responsible for PAR/PFM reform and is unable to enforce such reforms or to require that such reforms are compatible with FMC reform. Therefore it needs to develop partnerships and influence, which involves extensive 'networking'.
3. **Legal constraints.** Introducing FMC requires considerable legal change in most countries. Experience shows that changing the law or issuing regulations does not necessarily cause change in actions, for example, because other laws or regulations may prevent the delegation of authority or may separately define how managerial structures should be organised.

6. What can the CHU do within its powers?

1. The CHU should recognise that it cannot drive, but only facilitate, managerial reform from the platform of FMC reform; this should affect how it operates;
2. Before issuing laws and regulations ensure that all other laws and regulations are compatible with the requirements of FMC: this will involve negotiations with other ministries such as those responsible for public administration and the civil service.
3. Prepare a realistic timetable for reform recognising that major areas requiring reform are not within the control of the CHU or of the MoF.
4. The head of CHU has to fully appreciate the full effects of FMC- it is not just a technical financial reform; the strength of the CHU depends upon the strength of the MoF, but the head of the CHU must persuade the Minister of the full impact of FMC.
5. The CHU staff should include experts with knowledge of management, budget and treasury activity

7. How to achieve change?

The normal practice is to provide seminars, conferences and training. But this is a limited form of change management and in practice appears to be rarely effective especially where individuals are highly sceptical or adopt 'this is not how we do it here' approaches.

A more sophisticated 'change management' policy is required and ideally part of the PAR strategy. This should focus on:

- How commitment can be achieved and may require incentives and penalties;
- Training and seminars may have a role but delegates take away different messages because their backgrounds differ.

Overall diktats usually do not work and approval of a law on its own is not enough.

8.1 Lessons from SIGMA experiences: linkage of FMC reform with other reforms

FMC < - > PAR linkage

- The legal reforms that are needed to implement FMC are often not properly coordinated with all other relevant laws;
- FMC cannot drive managerial reform: that has to come from public administration reform (PAR);
- PAR ideally should come before FMC reform but usually doesn't and often the two reform policies are not integrated;

FMC < - > PFM linkage

- A lack of connection between FMC reform and public expenditure reform generally means that FMC reform is regarded as an independent activity;
- Equally budgetary and treasury reforms are often carried out independently of the impact upon FMC;
- As a result demonstrating the 'vision' about the purpose of FMC reform is frequently either lost or not appreciated with the result that much FMC reform becomes only a matter for the finance officer and then a concern for bureaucratic processes.

8.2 Lessons from SIGMA experiences: deficiencies in FMC reform

- The reasons for FMC reform (the ‘vision’) are not well communicated to managers.
- The existence of a FMC law or regulation does not mean that everyday actions are changed.
- Those concerned with FMC policy do not take into account the need for of ‘trust, loyalty and accountability.
- FMC policies have no regard to the ‘tools’ managers need to undertake their responsibilities and do not indicate how they are to be provided.

8.3 Lessons from SIGMA experiences: consequences of lack of coordination PAR/PFM reform FMC reform (1)

Financial management

- Objectives where they exist are vague and performance information rudimentary, with no timetable.
- Budgets themselves are too detailed to facilitate managerial accountability and have no regard to managerial needs.

Delegation of Authority

- Delegated responsibility is often limited to procurement, not the management of the relevant budget as a whole.
- Managerial hierarchies do not exist in reality.

8.4 Lessons from SIGMA experiences: consequences of lack of coordination PAR/PFM reform FMC reform (2)

Control

- Financial control and financial management are assumed to be the same when financial control is part of financial management.
- Accounting is understood only as recording spending against the budget.

Monitoring by CHU

- The arrangements for the review of FMC performance tend to focus on the existence of bureaucratic processes: self assessment reports in turn are only based upon measures of bureaucratic processes.

8.5 Lessons from SIGMA experiences: fundamental needs

- Linkage of FMC reform with other reforms.
- There should be a hierarchy in the development of FMC – not every aspect at once.
- More effort is required on change management - change does not come about because of the issue of regulations and laws, or the promotion of a few seminars.
- Raising profile of CHUs and developing partnerships and networking.

9. Conclusion

Overall, ministries of finance should recognise that the CHU has only limited control over the quality and timetable for the introduction of FMC because so many key decisions lie outside its competence.

As a result a greater emphasis should be put on cooperative partnerships with other organisations and the ministry of finance should encourage and support the CHU in this.