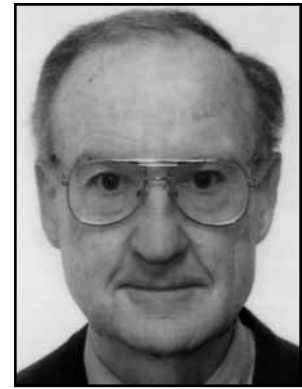

A Framework for Financial Management and Control

James Q. McCrindell



James McCrindell

James McCrindell is a Canadian and International consultant specializing in financial and performance management. During his career with the federal public service he was actively involved in the improvement and modernization of financial management and control, particularly during his time with the Office of the Comptroller General and the Treasury Board Secretariat (TBS), where he held the posts of Deputy Comptroller General and Assistant Secretary. Since leaving the government in 1995 he has continued to be an active proponent of improved government management, having been among other things a CCMD Fellow at the University of Waterloo's School of Accountancy (1995-96) where he did research on strategic performance measurement in government, and the principal author of a major research study by the Canadian Institute of Chartered Accountants on 'Costing Government Services for Improved Performance and Accountability' (published in 1999). As well as lectures and other speaking engagements, he accepts requests to write about key government management issues. In addition to over 30 articles he has had published in other professional journals, this will be his 8th publication with FMI.

Financial management and control is the bedrock of government management and its framework should provide the principal source of reference for guiding managers and their financial advisers in the efficient, effective and proper use of public resources.

It is the premise of this article that the status of financial management and control has diminished in recent years because of unclear communications and a lack of accountability by those responsible for exercising it. The article provides examples of how this situation has come about.

The commendable objectives of recent management reforms, such as improved stewardship and accountability, will be much more difficult to achieve without clear, comprehensive and coherent financial management and control frameworks in government departments and agencies.

A model framework for financial management and control is outlined in this article that is consistent with the objectives of the most recent management reforms, notably those related to modern comptrollership and the management accountability framework.

The accountability and communication challenges

1. Accountability

Significant advances have been made in government financial management and control (FM & C) since the Financial Administration Act came into being in 1951. Despite this, the Auditor General and other critics of government management continue to express disappointment with the state of government FM & C¹.

I believe the most significant cause of FM & C not getting the respect it deserves is a lack of real accountability for exercising it properly. FM & C problems are almost always caused by managers not feeling any

sense of accountability for this responsibility, rather than because of inadequate policies and guidelines.

Many of the management reforms in government have promoted the concept of empowerment and risk taking², and departments and their managers have often avidly accepted these. However, the accountability *quid pro quo* has usually been performance targets that do not have a stringent resources-results relationship³. Also, performance targets tend to give short shrift to the proper use of authorities. The focus has been on program or service results, even if their achievement may require liberal interpretations of some essential controls, or even by-passing them completely.

Avoiding control is not part of a sound risk management strategy. If controls appear to impair achievement of planned objectives and performance targets, then they should be discussed with the control authority to see if there are legitimate ways to use them more effectively or obtain some form of exemption. In the government, as well as private sector organizations, controls, whether they be in the form of laws, regulations or policies, may not always be in harmony with operational goals. But this is something that most sensible people accept, just like they accept that they must not travel over the speed limit in order to reach their destination sooner. They may believe that they can drive just as safely at a higher speed, but this is not an option.

Unfortunately, when embarrassing scandals occur with respect to the mismanagement or misappropriation of public funds, rather than addressing the real problem – a lack of accountability – the government tends to push the control pendulum so that it swings from the sound concept of 'empowerment and risk management in exchange for equivalent accountability' to more stringent controls; and this, of course, induces a more risk averse culture across government.

The government, on many occasions in the past, has specifically addressed FM & C accountability, most notably perhaps in the 1979 Report of the Royal Commission on Financial Management and Accountability (Lambert). Regrettably though, one can almost apply the old truism to this subject: when all is said and done, a lot more has been said than done. Or to paraphrase what I recollect the permanent secretary in the British television series 'Yes Minister' saying: 'the more we talk about something, the less we actually do about it'. This situation applies to accountability in general. For example, on page 3 of the Introduction to her 2004 Annual Report, the Auditor General expresses concern about the fact that while many documents have been published recently about accountability⁴, the government needs to describe more fully how it intends to turn into action the principles that its documents set out.

2. Communications

I believe progress on improved FM & C has also been thwarted by a lack of clear and

consistent communication of its meaning and purpose. This has led to both specialists (financial officers) and their clients (operational and non-financial staff) not being sure of their respective roles, responsibilities and authorities and, consequently, not developing the critical synergy necessary to make FM & C work effectively.

Improvements in some of the key elements of government management, such as FM & C, tend to become lost in a host of other management reforms, to the extent that managers and specialists are no longer sure of the depth and scope of their responsibilities and accountabilities. Years ago, a respected senior public servant, Herbert Laframboise talked about an ‘alphabet soup of management acronyms’⁵ and ‘saturation psychosis’⁶ with respect to managers being so overwhelmed with management reforms that they were no longer able to cope with their core jobs. Yet, Leonard Lee, a former public servant and one of Canada’s most successful entrepreneurs, is apparently fond of saying – good management is not rocket science; it is about applying common sense. But more importantly, it is about doing it rigorously and consistently: day in and day out.⁷ This is certainly true as far as FM & C is concerned.

The problem with the meaning and scope of financial management probably dates back to confusion about how it differed from financial administration⁸. For some people financial management is considered broader than financial administration, and for others it represents a managerial responsibility vis-à-vis a specialist’s responsibility. Yet we have a Financial Administration Act (FAA) that encompasses financial management, as well as many much broader areas, such as the Minister of Finance’s responsibility for the financial affairs of the country.

Financial Management is described in Part I, section 7 (1) (c) of the FAA under Responsibilities of the Treasury Board as:

..., including estimates, expenditures, financial commitments, accounts, fees or charges for the provision of services or the use of facilities, rentals, licences, leases, revenues from the disposition of property, and procedures by which departments manage, record and account for revenues received or receivable from any source whatever;

It excludes expenditure management by having a separate responsibility under section 7 (1) (d) that reads as follows:

the review of annual and longer term expenditure plans and programs of the various departments of Government, and the determination of priorities with respect thereto;

Various financial controls are described in other parts of the FAA, such as Part II, Public Money, Part III, Public Disbursements, and Part VI, Public Accounts.

A subject that often puzzled many observers of government management was why expenditure management would be separate from financial management. What self-respecting controller in the private sector would agree to have nothing to do with the corporation’s financial plans? This was addressed by the Secretary of the Treasury Board and Comptroller General of Canada in an August 3, 1994 memo to Deputy Ministers and Heads of Agencies on ‘A Vision of Comptrollership’. In this memo, the Secretary/CG stated that with the integration of the Office of the Comptroller General (OCG) into the Secretariat, the comptrollership function had been strengthened by blending financial and expenditure management, and that his vision of comptrollership was ‘an essential and effective tool to facilitate the best decisions within the bounds of acceptable risk’.

Comptrollership, as described in the 1997 Independent Review Panel Report on the Modernization of Comptrollership, does not, in my view, help clarify the purpose of FM & C. Rather than making it the same, it appears to suggest that FM & C is one of a number of disciplines. For example, on page 47 of the report, it illustrates required competencies of Senior Financial Officers (SFOs) as follows:

- *management accounting*
- *risk management*
- *budgeting*
- *financial management, planning and analysis*
- *financial accounting*
- *non-financial performance reporting*
- *business planning*

In the latest guidance to Deputy Ministers on their accountability for the overall management capacity and performance of their departments, FM & C is not mentioned specifically in the TBS Management Accountability Framework (MAF), which is used to summarize the Deputy Minister’s accountabilities⁹. Yet in the British Government, under the Accounting Officer

concept, the head of a department is accountable to parliament for ensuring that standards of financial management are high, that financial systems promote efficient and economical conduct of business and safeguard financial propriety and regularity, and that decisions on policy fully take into account financial considerations¹⁰.

It is reasonable to state that FM & C should be woven into the fabric of a department’s management framework. It is also very true that FM & C should not be the specialized domain of those with financial qualifications. Sound FM & C is a shared responsibility of specialists and their clients. Nevertheless, I am concerned that the only indicator of performance for financial or other specialists in the MAF is ‘as partners’. This could be misinterpreted. Specialist support must always be within the bounds of rules (laws, regulations and policies), ethics, departmental and public service values and objectives, and professional integrity. As long as both sides agree on these kinds of common rules and values, then partnership is great. In this sense, good financial specialist partners will not only want to help their partners achieve their objectives, but also make sure they understand and follow the straight and narrow of FM & C.

Purpose of a Financial Management and Control Framework

In my view, it is possible to extract a financial management and control framework from the management reforms and expert commentaries of the last few years, and this is the subject of the rest of this article.

Let’s start with the definition of comptrollership submitted by the Society of Management Accountants to the Independent Review Panel on Modern Comptrollership:

“...the process of acquiring resources and using them effectively and efficiently in the accomplishment of an organization’s purposes and objectives”¹¹

I like this definition because it focuses on what preoccupies most government managers, namely, getting the resources they need to get the job done, and being able to account to stakeholders on how well they used approved resources in accordance with stakeholders’ expectations. I say this because in my view ‘accomplishment of an organization’s purposes and objectives’ includes staying within the bounds of a

legal mandate and meeting the stated values of the organization with respect to ethics, and applicable rules.

Given the above interpretation, I suggest that the purpose of a governmental or departmental/agency FM & C framework is:

To facilitate and set the boundary lines for the planning, use and accounting of resources.

The phrase ‘and set the boundary lines’ establishes that an FM & C framework facilitates the resource management cycle (from planning to external reporting) within the rules, values, and performance expectations of the organization’s stakeholders¹².

Facilitating the planning, use and accounting or resources

An FM & C framework must respond to the business process of an organization, which in the federal government context is the management accountability framework (MAF). As shown in Figure 1, FM & C is where the MAF rubber hits the road, i.e., when resources become part of the process.

The facilitation of resource management through financial management is illustrated in Figure 2.

Attributes of a Successful FM & C Framework

Boiled down to bare essentials, a successful FM & C framework is present when an organization has the capacity to:

- conduct the resource management cycle well;
- establish boundary lines that clearly delineate the limits within which all decisions and transactions must be made; and
- establish and exercise clear accountabilitys for:
 - managing resources and staying within the boundary lines, and
 - demonstrating integrity vis-à-vis the shared values and beliefs of the organization.

While the accountability in the last sub-bullet may stem from the organization’s board of management or equivalent, it is nevertheless an integral part of the FM & C and all other frameworks within the organization.

Using the attributes to assess FM & C capacity:

Figure 3 shows how an organization might examine the gap between a successful FM & C framework and what it has in place.

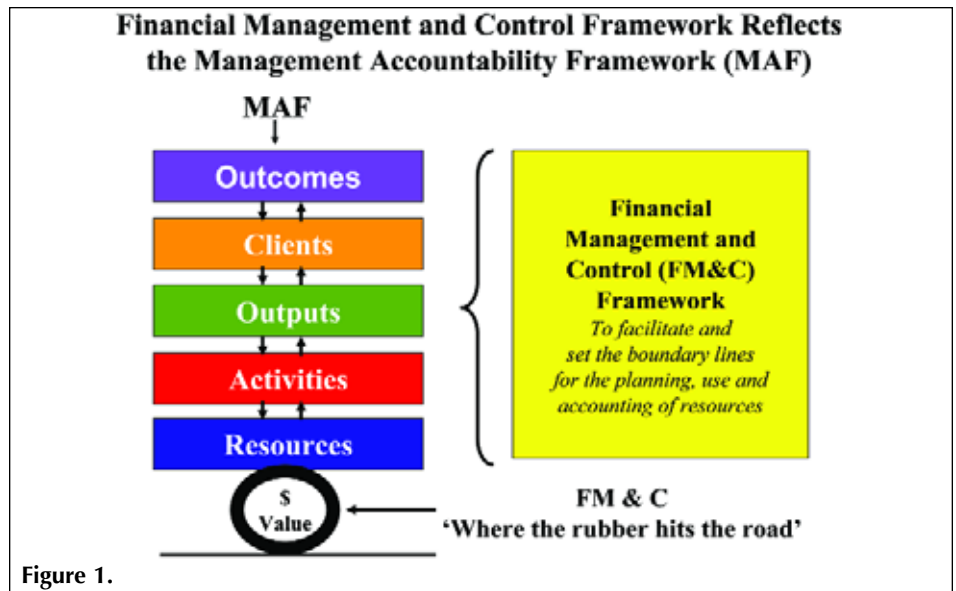


Figure 1.

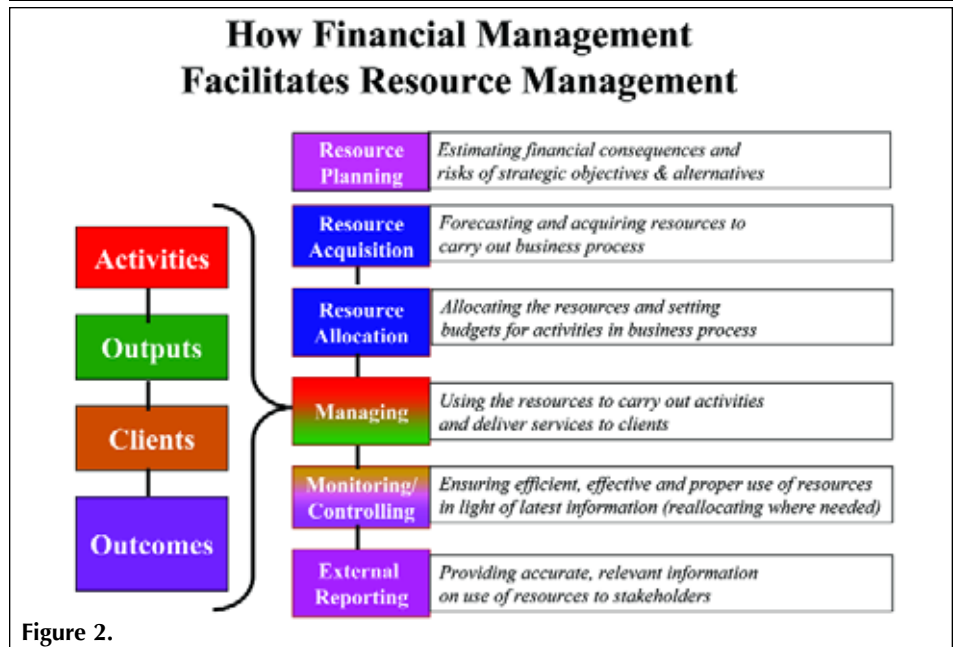


Figure 2.

Who is accountable for FM & C?

While the Deputy Head has overall accountability, all managers and employees are accountable for exercising FM & C, and financial management specialists¹³ have the additional accountability for ensuring that a sound framework, on behalf of the Deputy Head, is in place to foster the exercise of FM & C. These specialists must also have the capacity to provide sound advice on the interpretation and use of the framework, and to monitor its application so that its purposes are achieved.

The Pillars of a Financial Management and Control Framework

The four pillars of comptrollership advocated by the Independent Review Panel¹⁴

and later by the Modern Comptrollership team at the Treasury Board Secretariat can be summarized as follows:

1. Performance Information – financial and non-financial information
2. Risk Management
3. Control Systems
4. Ethics, ethical practices and values (beyond a focus on legal compliance)

Each of these pillars fit well with the FM & C Framework:

Linking financial and non-financial information

- The key objective of this pillar is to link resources to results. In my view, the reason why this objective has been so hard

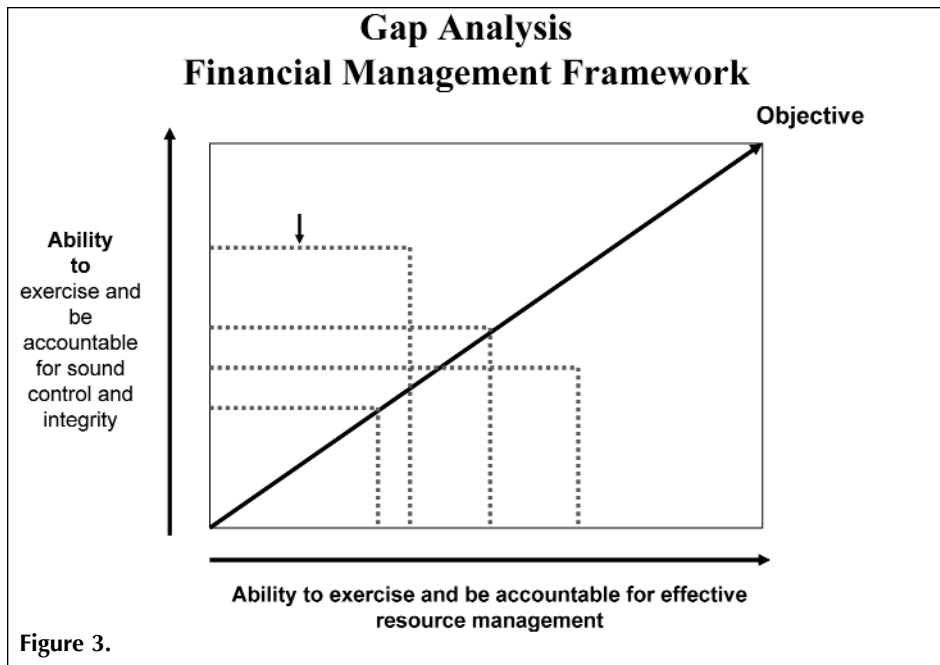


Figure 3.

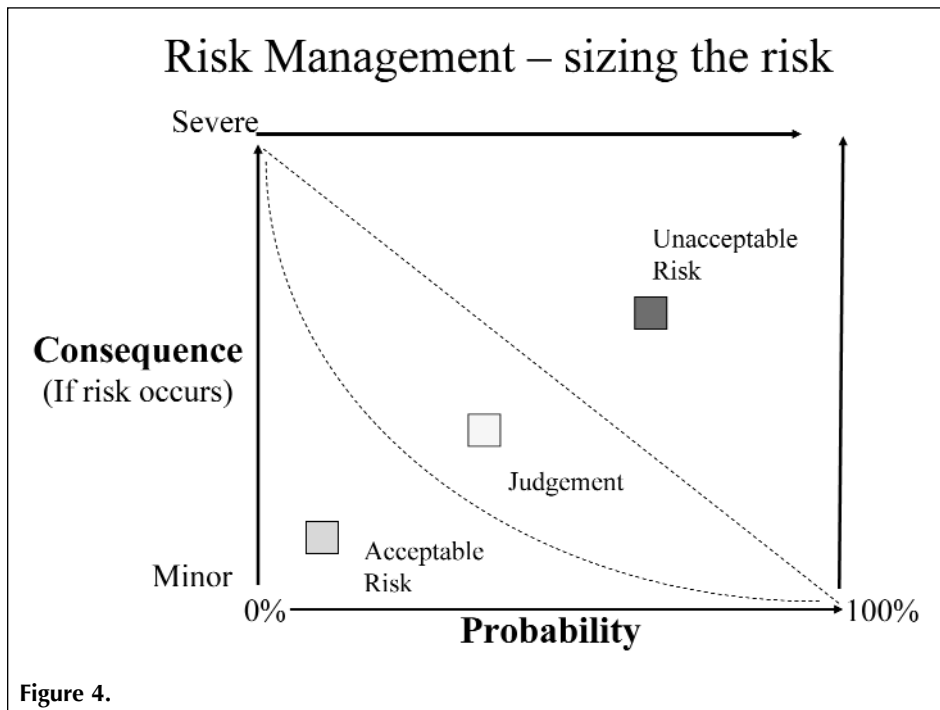


Figure 4.

to achieve is because of a lack of cost management, a critical element of financial management. Expressed in simplest terms, cost management is a responsibility for managing the factors that cause costs; specifically what causes the work (the activities in the MAF) that consumes resources. When the factors that cause costs are understood and managed, it is much easier to achieve sound resource management.

- Factors that cause the costs of activities

(resources consumed) may include many things, such as: the volume of client demand; service standards (e.g., accuracy and timeliness); the type of clients; and the complexity of governing rules and systems. This is the non-financial information that needs to be linked to the financial information in order to link resources to results. A good cost management structure within the FM & C framework will provide clear cost policies and principles, costing methodologies,

and an activity dictionary that truly reflects the actual work that is done to achieve results. It will also have a costing module in its FM & C system to enable expenditures to be linked to activities, and the resulting activity costs to be assigned on a causal basis to performance targets (outputs and outcomes in the MAF) and to other cost objects, such as clients and services.

- While the concepts in cost management are fairly straight forward, they appear to be extremely hard to apply in the public sector. I believe one of the main reasons for this is that an expenditure culture still exists. The primary interest appears to be in how much has been spent by a department or program, rather than what it costs to deliver its services and outputs. In the federal government this culture will be difficult to change as long as appropriations continue to be authorized and managed on an expenditure rather than an accrual basis.
- A good cost management framework not only enables the linking of resources to results for accountability purposes, but also provides better information for planning, alternative service delivery analysis, pricing of services, and other critical decisions.

Risk Management

- This second pillar is clearly related to FM & C, particularly to control. This is because control is a function of risk. The only reason for having controls is to guard against unacceptable things happening. Thus, we have the FAA and TB policies and regulations. These only exist to help alleviate the possibility of Ministers and public servants doing the wrong things, such as misappropriating or overspending funds.
- FM Controls are costly, and this is why they should be subjected to risk management techniques before being implemented. A key requirement is to size the risk, as illustrated in Figure 4.
- FM & C also uses risk management to help in the analysis of decisions, such as how to minimize the risk of unfavourable downstream financial consequences. A good example of this would be where the financial specialist, using life-cycle costing methods, is able to show that the best

acquisition price for a major capital acquisition may not in fact be the least costly option over the long term.

- It is important to remember that risk management is also to alleviate the risk of opportunities being missed. This involves anticipating new technologies or new pieces of legislation to ensure that the organization will be ready to take advantage of them as soon as they are available or take effect.

Control Systems

- FM & C control systems reflect mandatory controls such as those required for expenditures and revenues under the FAA and TB policies, and those that stem from risk management techniques where there is discretion by the senior executive or a board of management to decide what areas of management and accountability need protective or facilitative control measures.
- Protective controls are meant to protect public funds from being spent improperly or imprudently and public assets from loss, theft and damage. Facilitative controls are controls that enable the achievement of program objectives. Expressed another way, protective controls are input-oriented and facilitative controls are output oriented.
- Protective control systems are exemplified by financial, appropriation and commitment accounting systems as well as inventory and asset systems. Because they are costly, these systems should be as efficient as possible, for example, through the use of expert systems. These systems can make the work associated with protective controls user-friendly. They prompt the user to make selections from a menu on the computer screen so that no essential control steps are missed. They also advise the user of the authority to consult with in the event that difficulties are encountered.
- Facilitative control systems are exemplified by financial planning and forecasting systems, and integrated financial and non-financial performance systems. They alert managers of the need to revise plans and take actions to correct identified problems, or to take advantage of newly identified opportunities.

Ethics, ethical practices and values (beyond a focus on legal compliance)

- The purpose of this pillar is to extend the traditional prudence and probity principles of the public service, with a number of stated ethics and values that can be boiled down to what any public servant 'ought' to do in the best interests of the government and its stakeholders. In other words, it means doing what is right rather than what is expedient or personally beneficial.
- It is unfortunate that ethics and values have to be codified, communicated and even taught, given that the vast majority of public servants instinctively do the right thing. The only exception to this would be where an organization has some unique responsibilities and accountabilities and the right course of action for certain transactions or dealings might not be in accordance with the natural instinct of an average public servant. Instances of this would be rare in my opinion.
- This pillar is probably the most important from the perspective of control because a lack of ethics and values can seriously weaken most control frameworks, whereas strong shared values and ethics
...see *Financial Management and Control*, page 39

"BUD" JOHNSON, BUTCHER

HE CAN ADVISE WHAT YOU SHOULD STEW, WHAT

YOU SHOULD GRILL,

AND WHICH KIND OF WINE TO DRINK WITH

YOUR ROAST. EVEN WHERE TO FIND A

BAKER AND CANDLESTICK MAKER.



BUT WHEN IT COMES TO AUDIT ADVISORS, BUD

SHRUGS HIS SHOULDERS AND RECOMMENDS

THE ONLY EXPERTS HE KNOWS,

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ble force Mother Nature has to remind us of both our basic mortality and humanity. There were some up-sides as we saw a world that asked tough questions in the face of 'Might is Right' proponents, saw a widespread mobilization in defence of democracy and the right for people to chose and support for our fellow human beings that nearly eclipsed amazing survival stories and the insurmountable nature of the human spirit. We watched it all on our 40-inch TVs and felt lucky to be safe at home or anywhere the action was not unfolding.

So 2004 turns to 2005 and we fill ourselves with turkey and fixin's and promise to do better next year. But what does "do better mean" for we mere mortals in the financial community and what does this have to do with keeping our eye on the bottom line?

Absolutely nothing.

And that's as it should be. Maybe this time of year is really about reflecting on how we can be better people versus better professionals. About how we can contribute to something greater than the bottom line. About not wasting our mental energy trying to calculate how much water it will take to fill the backyard skating rink (*mea culpa*) but wondering instead how much care and attention it takes to fill your kids' eyes with true wonder and amazement at simple miracles and that being a kid doesn't compute on a balance sheet. About its not how much we or our organizations make but how we make a difference. Talk about a real balanced scorecard!

Yes, it's been an interesting and even wondrous year. How did you stack up?

More importantly how will you stack up next year?

Before I get all preachy (a big trap I often fall into, I am told) let me close out uncharacteristically short of my 1500 words, with the following advice that should be our community's credo:

- Live every day like it was your last
- Dance like nobody's watching
- Let the child you were be proud of the adult you are now
- Be good to one another
- Smile more, think less

May 2005 be a happy, healthy and thought-provoking year for all. Yes, I know I didn't say prosperous...but that's how I see it from behind my green eyeshade. ■

Financial Management and Control, from page 15...

make controls not only stronger but unnecessary in many cases; thus creating the opportunity to reduce costs and increase innovation.

Conclusion

The financial management controls established to protect the taxpayers of Canada are generally of a very high standard. Control breakdowns mostly result from a lack of accountability for the exercising of controls.

Financial management controls established to help managers and organizations achieve their objectives could be improved. Greater progress will result from:

- clearer communication on the meaning and purpose of FM & C and where it fits within the overall management framework of the government;
- clearer communication and guidance on the respective responsibilities and accountabilities for FM & C of financial experts and managers at all levels; and
- more emphasis on how to link resources to results, such as by introducing sound cost management policies and practices across government.

An FM & C framework should be built on the premise that the government wants a sound process in place in its departments and agencies for planning and acquiring the resources needed to achieve stakeholders' expectations and for rendering accountability to their respective stakeholders for the cost effective and proper use of these resources. Based on this premise, this article suggests that the purpose of an FM & C framework is to facilitate and set the boundary lines for the planning, use and accounting of resources. ■

References

1. AG Report, Chapter 5, December 2002, and various issues that have received public attention, such as the allegations of poor financial control of transfer payments by HRDC, and the breakdown of controls in the Office of the Privacy Commissioner.

2. An early example was the government's response to the recommendation of the Royal Commission on Government Organization (Glassco) in 1962 to delegate substantial responsibility and authority to departments and agencies for financial management in exchange for a corresponding increase in accountability of deputy ministers.
3. This is problem that has been raised by a succession of Auditors General over the years, and is a subject that has not been given sufficient attention in financial and expenditure management reforms.
4. She refers to the Guide for Ministers and Secretaries of State; Guidance for Deputy Ministers; the Management Accountability Framework; and the Values and Ethics Code for the Public Service
5. Unfortunately, I could find no reference document on this so this quote is based on my personal memory of what Mr. Lamframboise said.
6. H.L. Laframboise, *Administrative Reform in the Public Service: Signs of a Saturation Psychosis*, Canadian Public Administration Journal, Vol 14, No. 3
7. Quote from *Why is government so difficult (reluctant) to change?*, Sheldon Ehrenworth, Optimum on Line, Vol. 34, Issue No. 3, October 2004.
8. Similar confusion has occurred over the difference between public administration and public management.
9. Guidance for Deputy Ministers, figure 2, page 30, Privy Council Office, 2003.
10. Her Majesty's Treasury, *The Responsibilities of an Accounting Officer* (London (UK): HMSO, 1991, Annex # 4.1. (s. 5)), p. 2.
11. Page 19 of the Report of the Independent Review Panel on Modernization of Comptrollership in the Government of Canada
12. Stakeholders include the people within the organization, as well as external bodies.
13. FM & C Specialists range from junior financial officers all the way up to the Comptroller General of Canada.
14. Page 4.

Shared Services, from page 28...

It would also approve service level agreements to ensure fair and equitable treatment of its constituents. Finally, it would also act as a final dispute settlement mechanism between the clients and the service providers, as required.

The shared services initiatives sets the relationship such that the interest of the various stakeholders are counter-balancing without being counter-productive. The relationships will ensure long-term sustainability by encouraging a creative tension throughout the system. Continuous improvement and client responsiveness, which are built in, will ensure success.

Now that theory has been brought to life, the next and last article, to be published in the next edition of the FMI Journal, will present the implementation strategy developed to establish the new Shared Service Office. ■