NATIONAL TREASURY

Normative Measures for Financial Management

(Phase I: Perfecting the Basics)

NORMATIVE MEASURES FOR FINANCIAL MANAGEMENT
(PHASE I: PERFECTING THE BASICS)

1. Introduction

1.1 Purpose

The purpose of this document is to establish a framework for the development of acceptable normative measures for financial management. These normative measures, which should be regarded as a management tool to perfect the basics, are aimed at:

- providing a benchmark to accounting officers to assist them with the continuous evaluation of the quality of financial management within their departments and to report meaningfully thereon in their annual reports;
- contributing towards the improvement of financial management within Government departments;
- enabling the relevant treasuries to report bi-annually to Cabinet and the Executive Councils on specific aspects of financial management within a specific department or for national and provincial departments as a whole; and
- enabling the Auditor-General to improve his reports to legislatures on financial management in national and provincial departments.

1.2 Scope

The framework focuses on financial management within national and provincial departments and more specifically on the successful implementation of the Public Finance Management Act (PFMA), 1999, and its related Treasury Regulations. The focus is therefore not on service delivery standards (outputs and outcomes) of specific programmes within national and provincial departments. These issues and more advanced norms and standards for financial management in the public sector as a whole will be addressed in Phase II of the Normative Measures for Financial Management.

1.3 Coverage

The framework covers requirements as set out in the Public Finance Management Act, (PFMA), 1999, annual Division of Revenue Act (DORA), Treasury Regulations, 2002, Public Service Regulations, 2001, principles contained in the King Report on Corporate Governance for South Africa, 2002 as well as principles contained in various guideline documents issued by the National Treasury.

1.4 Implementation

1.4.1 Accounting officers should use the Framework to establish to what extent his or her department is functioning towards required and predetermined standards. Chief Financial Officers must design supplementary measurement standards to support the normative measures to be evaluated by the accounting officer. These supplementary standards would obviously differ per department and level of application.

1.4.2 The relevant treasuries will utilise the Framework to conduct bi-annually surveys within departments for purposes of reporting to Cabinet, Executive Councils and the Standing Committees of Public Accounts (SCOPA's). These reports will cover progress with PFMA implementation as well as improvement of financial management in general.

1.4.3 The Office of the Auditor-General will utilise the Framework as a basis to evaluate the level of financial management in individual departments and report thereon in the General Report of the Auditor-General after year-end. Information submitted to the relevant treasuries during a financial year for purposes of the bi-annual surveys will therefore be subject to auditing.

2. The need for proper standards of financial management in the public sector

Financial management is not an end in itself. It is, however, crucial to the successful functioning of any organisation since it relates to how resources available to the organisation are used.

Considering that the public sector is service delivery driven, the analysis and evaluation of management performance is somewhat different and more complex than that of industries that are driven by profit incentives. In the public sector, economy is measured by the relationship between quantity and quality of resource inputs and its related cost. Efficiency is measured by the relationship between resource inputs and outputs whilst effectiveness is measured by the extent to which outputs accomplish set outcomes. Appropriateness is measured by the extent to which programme outcomes meet the real needs of the community, which also form part of Government’s priorities.

It is recognized that the dynamics of public sector organizations sometime make it difficult to measure effectiveness and efficiency since these concepts are not always quantifiable. This, however, does not justify any argument in favour of less vigorous financial management for public sector organisations.

3. Financial management and an approach to managing for results

Sound principles of corporate governance and international best practices provide a sound basis for effective financial management in the public sector. To this end, the PFMA and its subordinate Treasury Regulations introduce an approach of management for results instead of managing for compliance. Some characteristics of this approach include, amongst others,:

- accounting officers entering into employment contracts with executive authorities supported by performance agreements that include performance standards;
- clearly defined responsibilities of the accounting officer and other role players for resources committed and outputs produced;
- greater alignment of planning and budgeting processes;
- the introduction of strategic planning;
- central regulations being reduced to the minimum and replaced with guidelines;
- accounting officers being allowed flexibility in the use of resources;
- management accounting and reporting;
- appropriate internal control and risk management principles ; and
- the introduction of accounting practices to facilitate the transition from a cash based system of accounting to that of an accrual base.

It is recognised that the quality of financial management in departments are directly related to the ability of accounting officers to recruit and retain adequately qualified chief financial officers, financial and management accountants, supply chain management practitioners and programme managers. The approach of management for results, with its associated flexibility in the use of resources with a greater emphasis on accountability, enables accounting officers to compete for the best personnel to achieve the agreed outputs of each department with an acceptable standard of financial management.

4. The aim and goals of financial management in the public sector

Given that Government intends to maximise service delivery to the community, financial management from a public sector perspective can be defined as:

"all decisions and activities of management, as guided by a chief financial officer, that impact on the control and utilisation of limited financial resources entrusted to achieve specified and agreed strategic outputs."

The aim of financial management in the public sector is:

"to manage limited financial resources with the purpose to ensure economy and efficiency in the delivery of outputs required to achieve desired outcomes (effectiveness), that will serve the needs of the community (appropriateness)".

Financial management ranges from daily cash management through to the formulation of long term financial objectives, policies and strategies in support of the strategic and operational plans of the department. It includes the planning and control of capital expenditure, working capital management, interaction with the relevant Treasury, funding and performance decisions. It supervises the supporting financial and management accounting functions, which are predominantly concerned with the collection, processing and provision of financial information and the planning, operation and control of the supporting financial information systems.

5. General principles for financial management in the public sector

- Financial management must be performed by or under supervision of personnel with the necessary technical training and proficiency.
- In all decisions affecting departmental outputs, financial impact must objectively be considered with the aim to provide the public with economical, efficient, effective and appropriate services or products.
- Due professional care must be exercised during all financial decisions affecting departmental outputs.

6. Performance requirements for financial management in the public sector

- Financial resources must be optimally planned and allocated between required outputs.

- The optimal investment in total assets required to support specified departmental outputs must be quantified and economically funded.

- The use of financial resources to achieve specified outputs must be monitored and controlled against the strategic and operational plans of the department by means of quantitative and qualitative data.

- Internal controls must be designed, implemented and maintained to ensure that:

  - Transactions are executed in accordance with management's general or specific authorisation;
  - All transactions are promptly recorded at the correct amount, in the appropriate account, in the correct accounting period to which it relates and in accordance with the departments' accounting policies;
  - Access to assets is permitted only in accordance with management's authorisation;
  - Recorded assets are compared with existing assets and vice versa at reasonable intervals and appropriate action is taken with regard to any variances.
  - Accountability must be established for performance associated with the freedom to consume scarce financial resources in the delivery of specified outputs.

7. Reporting requirements for financial management in the public sector

- Financial management information must be supplied on a regular basis to management to facilitate objective corrective decisions where activities are not in line with the budget of the department.

- Financial management information must be useful, reliable and timeous in support of the evaluation of performance.

- Financial reports must conform to the standards of reporting identified by appropriate legislation.

8. Critical areas for financial management performance

To achieve the aim of financial management as described above, requires involvement by the chief financial officer in the planning, design and control processes of the department. The following are recognised as critical areas for financial management performance in the public sector:

Critical Area for Performance	**Typical core tasks**
Management arrangements	The efficient, effective, economical and transparent use of resources; delegation of powers to other officials; proper risk management; design and implementation of internal controls, including internal audit, proper systems, processes and procedures; segregation of duties and financial management training.
Planning and budgeting	Provision of timely, accurate and adequate financial and other operational information for strategic decision making purposes; preparation of strategic plans, including advice on new strategies for achieving Government's objectives; costing and pricing of the department's products and services; programme performance measurement.
Revenue and expenditure management	Examine the department's operations to identify sources or potential sources of revenue; regular evaluation of the effectiveness of sources of revenue; timeous collection of revenue; ensure that sound systems and procedures for expenditure management and control are in place; deliver programmes with levels of efficiency, effectiveness and economy that seek to emulate the forces of market competition; effective management of transfer payments and conditional grants in terms of the annual Division of Revenue Act; implementation of processes to track expenditure and commitments against the vote and the identification, recovery and reporting of unauthorised, irregular and fruitless and wasteful expenditure.

Critical Area for Performance	Typical core tasks
Asset and liability management	Proper planning for the acquisition of assets, including the need to consider alternative strategies for the achievement of Government objectives; design and implement measures to protect and maintain assets, including the establishment of a comprehensive asset register; preparation of monthly age analysis of debtors and creditors reports.
Accounting and reporting requirements	Design, implement and maintain accounting systems to ensure complete, valid, accurate and timeous financial/non-financial information; maintenance of appropriate and consistent financial/non-financial reports that satisfy the needs of the users of financial/non-financial information; guidance on regular performance reporting to management.

9. Relationship between the chief financial officer and his or her clients

The chief financial officer neither operates on his or her own nor is he or she divorced from management. Successful financial management is the result of a collective and conscientious effort from everybody in the department, as guided by a technically trained and proficient chief financial officer who is objective and performs his duties with due professional care.

In this regard, the chief financial officer must establish effective service delivery relationships with his or her clients on a basis of integrity, reliability, objectivity and usefulness. These core values must be evident in the relationship with the following clients:

- Accounting officer
- Programme managers
- Internal audit and the audit committee
- Budget committee
- Treasury
- Auditor General
- Portfolio Committee
- Standing Committee on Public Accounts

Achieving these core values requires adequate education and training and maintaining the highest possible degree of professionalism in the delivery of financial services.

10. Core competencies and skills required for financial management in the public sector

Against the background of the definition, aim and scope of financial management in the public sector, it is recognised that chief financial officers must be technically trained and proficient in at least the following subject areas:

- Strategic management
- Business planning and design
- Performance measurement
- Financial accounting (including principles of GAAP/GRAP)
- Management accounting
- Internal control
- Internal and external audit
- Information systems
- Economy
- Negotiation skills
- Communication skills
- Analytical skills

11. Recommended structure of the Office of the Chief Financial Officer and related duties

In terms of Treasury Regulation 2.1.2, the chief financial officer is directly accountable to the accounting officer. The chief financial officer should have an appropriate support structure that allows him/her sufficient opportunity to provide analysis, interpretations and appraisals that will assist and improve decision making in the institution.

The following diagrammatic representation recommends the reporting lines and structure of a chief financial officer's component:

FINANCIAL MANAGEMENT

- **DEPARTMENTAL HEAD** (Accounting Officer)
  - **PROGRAMME MANAGER**
  - **FINANCIAL MANAGEMENT (CFO)**
    - **MANAGEMENT ACCOUNTING**
      Financial business support and risk management (including strategic planning, budgeting and performance measurement)
    - **FINANCIAL ACCOUNTING**
      Transactional processing and internal/external financial reporting
    - **SUPPLY CHAIN MANAGEMENT**
      Demand Management
      Acquisition Management
      Logistics Management
      Disposal Management
  - **PROGRAMME MANAGER**

12. Conclusion

The normative measures and its accompanying user manual, as contained in the enclosed Annexures A and B respectively, must be seen as a management tool to achieve sound financial management. By continuously evaluating the state of financial management in his or her department with the help of performance indicators/measures or requirements, the accounting officer should be able to ensure that pro-active rather than re-active steps are taken to address financial management problems. These measures must, however, not be seen as definitive but rather as a basis for the development of further measures that are unique to a department and its hierarchy.