



Financial Management and Control in Public Administration as One of the Essential Factors of Good Governance

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Abstract: *Financial management and control in the public sector represent a comprehensive system of established processes and controls. They contribute to greater accountability in public administration, rational and accountable management and spending of budget funds, building a culture of integrity, promoting trust between citizens and public administration, and striving to prevent corruption and fraud. The paper aims to highlight the importance of this system, the system of accountability in public administration, its connection with internal audits, and the direction of future reforms.*

1. INTRODUCTION

Financial management and control in the public sector constitute a structured system of processes and oversight mechanisms. This system enhances the accountability of public administration, ensures the responsible and efficient use of budget funds, fosters a culture of integrity, and strengthens public trust while aiming to prevent corruption.

In theory, the FMC system, or in foreign literature “PIFC” (Public Internal Financial Control), is considered a method for regulating administrative procedures within the organization, with a direct or indirect impact on the budget (SIGMA, 2023).

As one of the countries with the status of a candidate for EU membership, Serbia has undertaken to fulfill the obligations stipulated in specific chapters in various areas. One of them is Chapter 32, which refers to financial supervision (Ministry of Finance, 2023). One of the most essential processes in the mentioned chapter is the establishment of systems and mechanisms of internal financial control and internal audit in the public sector.

Implementing the financial management and control system brings numerous benefits for public administration, and it is also one of the conditions from the negotiation chapter for countries that are candidates for membership in the European Union, such as Serbia. One of the key benefits is the increase in transparency in the management of public finances, which strengthens citizens' trust and attracts foreign investments.

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More efficient resource management enables the optimization of budget expenditures and the improvement of the ratio between invested and received in the public sector. This contributes not only to financial stability and sustainability but also to improving the quality of services provided to citizens. In addition, better control and risk management help reduce opportunities for corruption and misuse of funds.

2. GOOD GOVERNANCE AND FINANCIAL MANAGEMENT AND CONTROL

The International Framework on Good Governance in the Public Sector, developed by the International Federation of Accountants, describes good management as the actions of public sector organizations that aim to achieve planned results while respecting the public interest (International Federation of Accountants, 2014, p. 19).

According to this document, acting in the public interest requires the following:

1. fostering ethical standards and values and acting with integrity;
2. ensuring transparency and openness;
3. defining public outcomes for sustainable development;
4. predicting measures and actions that are necessary to achieve such planned outcomes;
5. an effort to develop the capacities of all relevant subjects in the system;
6. risk management through the financial management system and control and internal audit;
7. efforts to ensure adequate accountability through reporting and auditing systems (International Federation of Accountants, 2014, p. 25).

This system should strive to recognize all possible risks in an organization or institution of public administration to manage them more efficiently (Hepworth, 2024, p. 39).

3. IMPLEMENTATION OF FINANCIAL MANAGEMENT AND CONTROL IN PUBLIC ADMINISTRATION

The initial step in implementing FMC in a specific public administration organization is for management to recognize the organization's benefits from introducing and implementing this system. After that, an important step is informing and familiarizing all employees with the importance of introducing the system and the obligation of cooperation during its introduction, especially during its implementation.

The introduction of the system (financial management and control) may have specific weaknesses or challenges, such as insufficient information of all employees about the entire process, their roles, obligations, and accountability, as well as awareness of the benefits of this system for the accountable business of the whole organization. This is the first element of the financial management and control system or the so-called control environment.

After the first stages of introducing the financial management and control system into the organization, the next important step is the detailed definition of all business processes within that organization. This step involves elaborating each process, including its procedures and flows, to ensure that it is fully compliant with applicable legislation and the organization's internal rules and procedures. After defining the process, a horizontal and vertical review of the procedure follows.

A risk management strategy is created after defining the list of business processes and reviewing the procedure horizontally and vertically; first, the probability of risk occurrence is determined, then the effect of the risk is measured, and finally, the risk is evaluated.

The probability of risks shows their likelihood of occurrence in a specific organization/institution. The measurement of the risk's effect shows the degree and assessment of the significance of the consequence if the risk is realized, that is, if a harmful event occurs that causes consequences.

Risk assessment is the determination of risk exposure and its limits of acceptability for a specific institution. Risks are divided into those that do not require a further reaction, those that require an immediate reaction, and those that need to be controlled and well-managed to reduce them to a level that does not require a further reaction (Anđelković, 2024, p. 259).

Public administration entities face numerous risks in their work, such as certain unforeseen, uncertain events, which may affect the achievement of planned goals. Some risks can have a more significant impact on achieving goals and performance and some less. In this regard, defining and ranking risks is one of the more essential steps in establishing a financial management and control system. In theory, different risk classifications can be found. One of them is related to whether they represent an opportunity or a threat for the subjects of the public sector: positive risks when they represent a chance or opportunity and negative risks when they represent a threat. Other criteria divide risks into their area of occurrence, e.g., social risks, risks for human rights, strategic ones that come from strategic documents, and operational ones that come from the organization's daily operations (International Federation of Accountants, 2014, p. 45).

Regardless of the division criteria, it is essential that they are recognized and continuously well-governed. Good risk governance means that all organization subjects, including employees and management, must be aware of them. Furthermore, they must be mindful that risk governance is a continuous process. The emphasis is always on risk prevention, but since the very definition of risk is unpredictability and uncertainty, they can occur during work, that is, business, and then they must be well governed.

Risks in public administration can be very different, depending on the field of work. When creating the risk register, it is essential to identify them as much as possible at the specific moment to determine the persons accountable for risk governance, measures to eliminate risks, and the persons in charge of their elimination, that is, reducing risks to the most minor possible extent. This should be followed by analyses, working group meetings, etc., on which risk governance would be monitored and reported.

In addition to risk governance, so-called control activities enable the level of risk to be reduced to a reasonable or acceptable level, as well as mutual communication and information, which are necessary for the functioning of this system. The last element of financial management and control is monitoring and evaluating the functioning of the FMC system. This activity is carried out by internal audit, with employees regularly inspecting and monitoring it, as well as various types of self-evaluation by employees and management (International Federation of Accountants, 2014, p. 55).

The Law on the Budget System (Art. 81) regulates the system of financial management and control in the RS's legal system; this regulation establishes the obligation of all users of public funds to introduce a system of financial management and control and internal audit (in one of the three

ways provided by the Rulebook) (“Official Gazette of RS”, No. 89/2019). This Law stipulates the manager’s obligation to report to the minister in charge of finance on the adequacy of this system’s functioning by March 31 of the current year for the previous year.

The European Commission views that the development of the internal financial control system in public administration is the result of a focus on goals and performance governance, as well as on risks and good governance as a whole, especially considering the principle of organizational accountability and the quality of services provided to citizens (European Commission, 2014).

Establishing internal financial control systems in European countries varies depending on their administrative structures and legal systems. For example, these systems are organized as centralized control institutions in Spain and Luxembourg. This means that one or more central bodies are responsible for supervising and controlling economic and financial management at the national level. In most other EU countries, such as the Netherlands, Sweden, Denmark, and the United Kingdom, internal financial control is organized to manage risks and ensure the achievement of general goals. These systems represent decentralized systems of internal financial control (European Commission, 2014).

Most countries have established coordination and networking between financial controllers and internal and external auditors within the entire public sector in the form of special harmonization units, which are usually part of the Ministry of Finance (e.g., Portugal, Slovenia, the Netherlands, Lithuania, etc.). On the other hand, Austria, Denmark, and Germany do not have separate, central harmonization units (European Commission, 2014).

4. PROCESSES AND PROCEDURES IN THE FINANCIAL MANAGEMENT AND CONTROL SYSTEM

For illustration, we present a list of individual business processes and procedures characteristic or typical for public administration institutions in the domain of legal, personnel, administrative, and public procurement affairs. Then, there is a horizontal and vertical view of the procedure.

1. The process of ensuring the implementation of the Law, Collective Agreements, Statutes, and other general acts of the institution.
 - 1.1. The procedure for ensuring the implementation of the Law, Collective Agreements, Statutes, and other general acts of the institution.
2. The process of adopting general acts of the institution.
 - 2.1. The procedure for adopting general acts of the institution.
 - 2.2. The procedure for drafting letters, decisions, confirmations, and notifications.
3. The process of establishing an employment relationship, applying for compulsory insurance, terminating the employment relationship, and deregistering from compulsory insurance.
 - 3.1. The procedure for establishing an employment relationship and applying for compulsory insurance.
 - 3.2. The procedure for exercising other employee rights.
 - 3.3. The procedure for termination of employment and deregistration from compulsory insurance.
4. The process of keeping personal records of files and personnel records of employees in the institution.
 - 4.1. The procedure for possession and permanent storage of documents and data of all employees in the institution.

5. The process of keeping personnel records, storing and protecting personal data.
 - 5.1. The procedure for keeping personnel records.
 - 5.2. The procedure for storing and protecting personal data.
 - 5.3. The procedure for exercising rights from pension insurance.
6. The process of creating individual solutions from the employment relationship (maternity leave, leave for child care/special child care, unpaid leave, suspension of the employment relationship).
 - 6.1. The procedure for creating individual solutions from the employment relationship (maternity leave, leave for child care/special child care, unpaid leave, suspension of the employment relationship).
7. The process of creating individual solutions from the employment relationship (annual vacation, paid leave).
 - 7.1. The procedure for making individual decisions from the employment relationship (annual leave, paid leave, unpaid leave, jubilee awards, solidarity aid).
8. The process of participating in drafting contracts concluded by a legal entity in business with other legal entities and natural persons.
 - 8.1. The procedure for participating in drafting contracts concluded by a legal entity in business with other legal entities and natural persons.
9. The process of office and archive business.
 - 9.1. The procedure for office and archive operations.
10. The process of creating, amending, and supplementing the procurement plan and monitoring its implementation.
 - 10.1. The procedure for creating, amending, supplementing, and monitoring the implementation of the procurement plan.
11. The process of public procurement - open procedure.
 - 11.1. The procedure for public procurement - open procedure.
12. The process of acquisitions that are exempt from the application of the law.
 - 12.1. The procedure of acquisitions that are exempt from the application of the law.
13. The process of legal protection and protection of the bidder's rights.
 - 13.1. The procedure of legal protection and protection of bidder's rights.
14. The process of keeping records of working hours and records of arrival and departure from work (carnet).
 - 14.1. The procedure for making records of working hours and records of coming to work to pay wages and expenses for coming to and leaving work.
15. The process of document filing, archiving, and documentation delivery.
 - 15.1. The procedure for document filing, archiving, and documentation delivery.

5. CONCLUSION

Systems that help discipline business processes in public administration are contributing factors to the system of accountability in public administration and are essential components of good governance. Such systems are financial management and control in the public sector and internal audit.

They represent a comprehensive system of established processes and controls, contributing to accountability through good governance and budget funds spending. This system's development resulted from focusing on goals and performance governance, which contributes mainly to good governance.

The introduction of the FMC system in public administration institutions is not just a goal; it involves adequate implementation by all employees and management, constant updating, and risk governance. For that, a tone from the top is necessary, i.e., the organization's management recognizes the importance of introducing this system. That is why it is essential to connect the concept of management accountability with the financial management and control system. On the other hand, the financial management and control system should be closely associated with the internal audit system in the same institution; that is, the risks identified by the financial management and control system should be included in the internal audit's work.

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