

MFM Project

FIELD TRIP REPORT VLADIVOSTOK

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Municipal Finance and Management
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**Municipal Financial Management
City of Vladivostok
USAID/RTI**

DRAFT

**Field Trip Report
April 1995**

Mahesh Reddy
May 19, 1995

Introduction

As an on-going effort for democratic initiatives, USAID is funding the Municipal Finance & Management Program in Russia. The City of Vladivostok is one of the assistance sites, in Russia, and work began in March 1994 to provide technical assistance to the City. A major part of the program is to computerize the Finance Department and provide an automated environment to have accurate and timely access to financial information.

Several field trips are scheduled to supervise the development of an enhanced Budget/Accounting Financial Management software for the City of Vladivostok. The purpose of the trips are to monitor the work being performed by the contract programmers in Vladivostok and to verify and test the software in order to make progress payments.

This report is a formalized version of the Annexes. The Annexes give a little more detail on the work done in the field and the recommendations at various levels. Annex 4

Purpose of Visit

As per the work plan, a Technical Draft was due by the End of March 1995, the draft was completed by April 10, 1995. The consultant visited Vladivostok between April 21, 1995 and April 29, 1995 to review and approve the Technical Draft. The successful completion of this document would authorize payment of a 10% advance to the programmers to commence programming work.

Work Completed

Several meetings were held with City officials. The following is a list of meetings:

	<u>Meeting</u>	<u>No. of Meetings</u>	<u>Purpose</u>
1	Finance Director	- 2	Orientation and discussion of a Obligation Accounting System (OAS)
2	Finance Department division heads	- 1	Discuss OAS
3	Programming Company Director	- 1	Contract and summary of changes
4.	Chief Programmer	- 4	Technical Draft

Observations

The principal observation was an unwillingness on the programmers to program the OAS. They had swayed the finance department staff into thinking that the OAS system would hamper the working of the entire system. Resistance was due to the lack of knowledge of modern programming techniques.

A lot of discussion centered on the operational aspects of obligation accounting being linked to the implementation of a central purchasing system. They were advised that the central purchasing system was not their individual concern, however this would be a policy decision to be made by the Mayor and Finance Director.

Explanation of the technical requirements for programming the OAS was provided in two meeting sessions to the Chief Programmer. The Programming Company Director indicated that in order to program the additional work it would cost 1.5 times more. This seems to be a "base-less" amount without any justification.

The Finance Director was in favor of having a control system programmed into the software and finally decided, through a consensus with her department staff, to have a vendor payment history system programmed. The meeting was concluded with a plan to have the programmers devise a "system" to record direct payments to the vendors (suppliers of goods and services). Once this system is designed, the City may proceed to gather data on purchasing patterns, vendor payments, and recording contracts (to track order and order fulfillment history), etc. It is the start of a purchasing system which will lead to OAS.

Some of the discussions centered around the problem of having a central purchasing department in Russia due to the potential for corruption. The consultant to be hired, if the City of Vladivostok agrees to this TA, should be aware of how to develop a transparent system.

Recommendations

Having spent considerable time in reviewing municipal financial data and meeting with finance directors in over 25 different municipalities and two oblast, I am convinced that the principal reason for budget overruns is directly attributed to reprogramming expenditures without prior approval. This is a result of the absence of a record of commitments (obligations, contracts, etc.).

The most important change that can be made at the current moment is to control spending before an expenditure is made. An ICMA document, *Purchasing Manual of Arlington County*, is being translated into Russian and will be available to the Finance Director for review.

Next Steps

The completion of the software package is yet scheduled for September 1995. Though no official confirmation is available we believe that the development and programming work is progressing despite the delay in signing a formal contract. The consultant will schedule a trip in June/July 1995 to review progress on system development and be available to answer questions.

ANNEX 1**Financial Control System for Russian Municipalities**Background:

The existing system in Russia is as follows:

Budget/Expenditure Control

Regional government sets the budget for Cities. In turn cities receive financing for the deficit amount from the Region. The amount received is less than budget if there is a revenue shortfall for the Region. The Cities do the same to their organizations and their districts. Providing financing is the main function of Finance Department, not budgetary control.

After budgets are set, funds are transferred to rayon bank accounts or departmental bank accounts in portions based upon availability of funds. These funds are redirected for other purposes, by the bank account manager (department manager or rayon manager) without the approval of the finance department.

Purchasing System

The current practice, as reported by officials, is pay cash first and then get delivery of goods. So the system of committing (or recording "intended" budgetary expenses) funds is reported as unworkable.

The city or city agency must enter into a contract with an inflation index for purchases and this contract must be recorded to calculate available budget resources.

Suggestions for a Financial Control System:

1. Legislation for Contracting for purchases
2. No prepayment for purchases to negate any argument that suppliers will not supply, do an analysis of annual purchases of supplies and see if suppliers can survive not doing business with the city or districts.
3. Record "intended" purchases and transfer money to vendor bank account directly. This can be done by rayons and departments. As a compromise, if rayons or departments are not responsible the city can take control of their bank accounts.
4. Budgetary control over certain line items (utilities, salaries, benefits etc.), and disallowance of transfers from these accounts.
5. Departments **must not have** autonomy in expenditures without approval from the Finance Department (either rayon or central city). Requests for purchases must be provided once a week,

and preplanning for purchases must be done. If there are too many emergency purchases, the department manager must be contacted about the lack of preplanning.

Mechanics for Computer Program

The budget database must be duplicated and called "commitment" database. The program must have the following:

- 1 A menu item to add and delete commitments
- 2 An automatic entry to deduct commitments when a pay order is referenced to a commitment. The payment must be made against the same account and the commitment reference number
- 3 A temporary file of commitment activity by Ref. # and Budget Account #.
4. A budget review screen as follows:

a.	Adopted Budget	25,000
b.	Modified Budget	26,000
c.	Commitment	13,000
d.	Expended	5,000
e.	Available	6,000

When an commitment is canceled, an entry must be made to commitment journal to reverse expense, the program must recalculate the balance based on the account number and bring it into item 4c and item 4 e should be modified. This can be done by "calculated field" function in the screen table.

Reports should include Date of commitment, Ref. #, Budget Account, Amount of Commitment, Date(s) liquidated(partial), Payment voucher(s) (Pay order(s) #) #, Amount(s), Outstanding amount of commitment.

Voiding commitments should require signatures of Budget department and Accounting department and statement from vendor that no goods/services were provided that is not recorded.

Mechanics for enforcement:

Legislation

Prepare legislation in the form of a Mayor's Directive which recognizes the **need for financial control**. This legislation must provide the necessary resolutions to:

- the budget division to provide pre approval of expenditures and record commitment
- require departments to enter into contracts for purchases
- section on penalties for by-passing financial controls
- Monthly budget reports to include commitment balance

Policy Directives to Departments

- Require approval for purchases over certain amount
- Require approval for purchases of fuel, supplies & materials, capital equipment, capital construction, and other restricted items.
- Establish a department of purchasing
- take control of bank account of department or rayon if they are redirecting funds.

Conclusion:

A meeting was held on April 27, 1995 at 1 p.m. with the division heads of the Finance Department and the contracted programmers. The discussion centered around obligation accounting (or encumbrance accounting). There was general resistance from the staff and programmers (who did not understand the concept fully). Some of the more experienced finance staff clearly understood the concept of financial control that would be available if the city moved towards commitment accounting.

Some of the arguments against the obligation accounting was that:

- the finance department does not have the legal power to pay vendors directly
- the finance department does not have the legal power to control department budgets
- the finance department does not have the staff to perform a central purchasing function
- central purchasing will increase the number of documents to be processed
- the programmers specifically objected to the obligation accounting system (Annex 2) saying that it does not provide financial control and that if programmed, it will hamper the entire budget/accounting system. They also claimed that this system will require 150% more time to redesign and program the software

The Finance Director, the Public Economy division chief, the Non-budget funds division chief agreed that the OAS system would provide more financial control. It was surprising that the deputy director/budget division chief disagreed with this concept.

The Finance Director also recognized that the system does not have to be applied to all purchases but only to major areas of the budget and for capital expenditures. She discussed these issues thoroughly, with a full understanding and convinced her staff that a system of financial control is required. She concluded that if the her departmenet rejects the proposed system the department must develop its own system to provide adequate control.

The programmers proposed to design a system which will allow for payments directly to the vendors. They also suggested that they should be in charge of the technical development of this system.

While this is not an ideal situation, I viewed this effort as a first step towards the development of a purchasing system. The finance director discussed and suggested that a reserve fund would be created for the major purchases. Requests would be considered from departments and contracts concluded with vendors with payments made directly to the vendors. A lot of details were to be

discussed at a later date to deal with the purchasing system. I recommended to the Resident Representative that the *Purchasing Manual, Arlington, Virginia*, published by ICMA be translated and provided to the Finance Director.

Recommended specifications for the Direct Vendor Payment system:

Ability to record a contract amount (with the vendor) after approval of the expenditure
Ability to pay a partial amount of the contract and record this information
Ability to automatically look-up the budget availability prior to recording a contract amount
Ability to automatically look-up the payment history for each individual contract.
Ability to maintain contract history by vendor, budget account number, date, purpose of purchase, etc.

ANNEX 2PRESENTATION

EXISTING SITUATION

PROBLEM: BUDGET DEFICITS - DUE TO NON-BUDGETED AND/OR UNPLANNED EXPENDITURES

SOME REASONS

- FUNDS TRANSFERRED DIRECTLY TO DEPARTMENTS - TARGETED FUNDS BEING REDIRECTED WITHOUT APPROVAL

SUGGESTED SOLUTION

PRE-APPROVAL OF EXPENDITURES AND TRANSFERS BETWEEN BUDGET LINE ITEMS

- NON-BUDGETED EXPENSES FUNDED BY MAYOR'S DIRECTIVES

SUGGESTED SOLUTION

FINANCIAL IMPACT AND JUSTIFICATION TO BE PREPARED PRIOR TO APPROVAL

- RISING PRICES, SHORTAGE OF GOODS, NO LONG TERM CONTRACTS WITH SUPPLIERS

SUGGESTED SOLUTION

CONSIDER FUTURE CONTRACTS FOR ECONOMIES OF SCALE

- DEPARTMENT PURCHASES UNCOORDINATED -NO CENTRALIZED PURCHASING DEPARTMENT

SUGGESTED SOLUTION

CONSIDER A CENTRAL UNIT FOR MORE PURCHASING EFFICIENCY FOR THE CITY

Prepared by:
Mahesh Reddy

April 25, 1995

for:
Finance Department of the City of Vladivostok

ANNEX 3**Presentation
for
Obligation Accounting System (OAS)***OAS anticipates:*

- Reserving funds for specific purchases
- restricting use of obligated funds for other purchases until higher approval is received
- preventing disbursement of funds for unknown purposes
- requiring contracts between the supplier (vendor) and City
- canceling of obligated contracts to commit additional budget funds
- serving as a memory for existing obligations, obligated funds and their purposes
- not all purchases come under this system, smaller purchases will be direct

Benefits to departments:

- reduce detail oriented responsibilities, reduced functions
- purchasing efficiencies in a market economy
- more focus on operational activities and less focus on administrative activities
- more accurate account expenditure information, needed for budget department review

Disadvantages to departments:

- regulation of spending authority through finance department
- purchasing delays due to lack of prior planning
- need for planning expenditures more efficiently

Prepared by:
Mahesh Reddy

Date:
April 27, 1995

Prepared for a meeting at 1 p.m. with:
Department of Finance, City of Vladivostok, Russia

ANNEX 4**Proposal for Programmer Training
in the United States**

This proposal is prepared to provide **advanced programming concepts** for two programmers involved in the municipal finance application in Vladivostok, Russia.

The need for this assistance is based on a recent assessment that the concepts and experience in application development is very basic and needs to be enhanced through exposure to western techniques.

Travel specifics:

The trip will be for fourteen days (14)

The trip will be to learn programming concepts and tips at a financial software company specializing in **municipal financial software**.

The trip will be for two programmers:

one a network programmer

one a database programmer

Rationale:

In developing the enhanced software for the City of Vladivostok it was planned that an advanced database system would be developed. The Technical Draft reviewed suggests that the techniques and methods being considered can be significantly enhanced.

For example, most of the information input is directly into the database, not first through temporary database files to allow for an edit process. The database structure being developed is flat and with more overhead than necessary. The file structure contains four sets of fields that will contain the same information. The reason, explained by the programmers was to replicate an existing paper document on the screen. While this is a sound programming technique it is not very efficient in database management design.

Required:

A software company that will consent to designate a deputy chief programmer for 14 days uninterrupted.

Prepare a schedule of study/technology transfer activities which include some programming exercises and discussion of database development/management concepts.

Two suggested companies are American Management Systems (AMS) and American Fundware (out of Colorado, Tel. # 1-303-756-3030 [I recommend this company])

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Costs:

For two individuals:

Description	Cost per	Amount
Airfare	\$2,000	\$4,000
Hotel (14 days x persons x \$100)	\$1,400	\$2,800
Per diem (50 x 2 persons x \$50)	\$700	\$1,400
Software Company (500 x 14 days)	\$500	<u>\$7,000</u>
		\$15,200

prepared by:
Mahesh Reddyprepared for:
RTI/ Washington
RTI/Vladivostokdate:
April 26, 1995

ANNEX 5**Summary of Actions & Follow-up**

April 28, 1995

Work accomplished on this field trip:

1. Reviewed in detail the technical draft and approved it.
2. Authorized the 10% payment
3. Discussed Obligation Accounting system and changed the Technical Draft to include a Direct Vendor Payment system
4. Reviewed budget data collection for City of Vladivostok from 1991 to 1993 (City claims 1994 is not compiled yet)
5. Provided a summary chart of growth of "real" revenues and expenditures from 1991-1993
6. Prepared a proposal for programmer training in the US to Jim Alloway and Eric Chetwynd

Next steps for office staff:

1. Natasha to translate the *Purchasing Manual of Arlington County* by May 30, 1995
2. Jane to prepare charts for revenues and expenditures in "real" rubles for 1991-93 and compile 1994 financial information.
3. Jane to present these charts to Mrs. Vishnyakova and to do a more in-depth analysis of expenditure trends as requested by Mrs. Vishnyakova.

Next Steps for City Finance Department:

1. Request weekly reports from programmers, by "name" and "date" and "activity involved" on a weekly basis after 10 % advance is completed. You must be certain that all seven programmers are working on the programming and in what area. If needed fax the reports to me and I will comment on them.
2. Do an in-depth analysis of spending trends, this information should be valuable for formulating the centralised purchasing function. (When expenditures, in real terms, are increasing 700-900% there should be good reason, find out the reason).
3. Conclude a contract with TITAVC by Friday May 5, 1995 so the money can be paid, this commits the programmers to begin work and adhere to the schedule.
4. Require the Network to be operational in the Frunzinsky Rayon so programming and testing can begin.

Next steps for consultant:

1. If proposal for programmer training is approved, coordinate training session with American Fundware
2. Supervise the programming effort as required.

Prepared by:
Mahesh Reddy
1995

Date: April 28,

for: Jim Alloway Project Manager RTI/Vladivostok
