



Course: Financing and economic management

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## Contents

### **Financing the budget chapter of the Ministry of Defence**

#### **1 MoD - the issue of implementation of economic management**

How many soldiers have or how many actually finance is appropriate for financing the defence, was always in question, which was not immediately clear answer. It is quite clear that in times past, these answers unfold example from the area of the country or empire, population, but also by geographical location or momentary relations with its neighbours. The rulers had to think about it and how it can be threatened his country. If, for example, was one of the major producer of minerals, certainly on this area were interested in others. Often thus conclude a peace treaty that guaranteed the safety of a given country for example, such a fee. Parts of mineral extracted. It is clear that the ruler had to compare the costs to prepare for possible war and the cost of paying a fee. From this example, we see that even a country's policy definitely affects how the state or country will be provided defence. As reported Peková et al.:

*"Every state based on its geopolitical position analyses its demographic and economic potential and creating a national defence strategy."*<sup>1</sup>

In the last few years, facing the MoD gradual reduction of financial resources earmarked state budget chapter 307 - Ministry of Defence. On this condition was to respond to the introduction of new management tools and methods by which the stated objectives will be achieved in the required quality. MoD faces the task as efficiently as efficiently as possible and effective use of allocated resources.

On the security of national defence are used three basic sources. These are: human resources, physical resources and financial resources (funds). Economical, efficient and effective use of funds is done through a system of economic management. This system is a financial management and financial security. In the current period, the MoD is in a transitional period - uses a system of financial security and financial management.

The current system of economic management of the MoD is already outdated and in view of the increasing intensity of the need for economic management of all resources and their mutual balance is necessary to introduce a full-fledged system of economic management.

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<sup>1</sup> PEKOVÁ, Jitka. *Veřejná správa a finance veřejného sektoru. 2., přeprac. vyd.* Praha: ASPI, 2005, 555 s. ISBN 80-735-7052-1, s. 435

The success of the transition to economic management is subject to changes in other management systems (command and control, defence planning, construction and transformation of organizational structures, personnel management, training and education of personnel, system management by objectives). One of the basic conditions for the successful introduction of the system of economic management into practice is to determine the responsibilities and activities of individual entities, including the creation of support required.

Managerial summary "The concept of economic management defines the so-called carrying points of transition from financial management to managing economic:<sup>2</sup>

- Economic management is based on a clear definition of the scope and activities of the major actors in the process: the user (manager targets), support manager goals (economic and professional bodies) subsystems and of economic management - financial management, management of current assets, assets reproduction management, monitoring and controlling costs;
- The aim of this document is to define changes in the planning process. However, it was necessary to identify trouble spots that have an impact in of economic management. Therefore, the concept of economic management proposes to implement changes in the planning process so that it is possible to plan all the resources in the sector, and to output documents provide consistent and stable over time basis for follow-up processes - budgeting, acquisition process, material inventory management and asset reproduction;
- In the area of budgeting compliance with the rules target- oriented budgeting is impassable limits by setting individual goals for their wearers (managers goals);
- It will be introduced perennial change management based on the resulting documents from the multi-material-based planning and medium-term outlook MoD;
- It will be introduced a system of applying the requirements of material needs of managers goals and formulating a plan of material needs and balancing the available cash resources as a basis to build an acquisition plan;
- It will be introduced a system of tracking expenses and controlling system for monitoring the behaviour of economic organization based on benchmarking inputs and outputs;

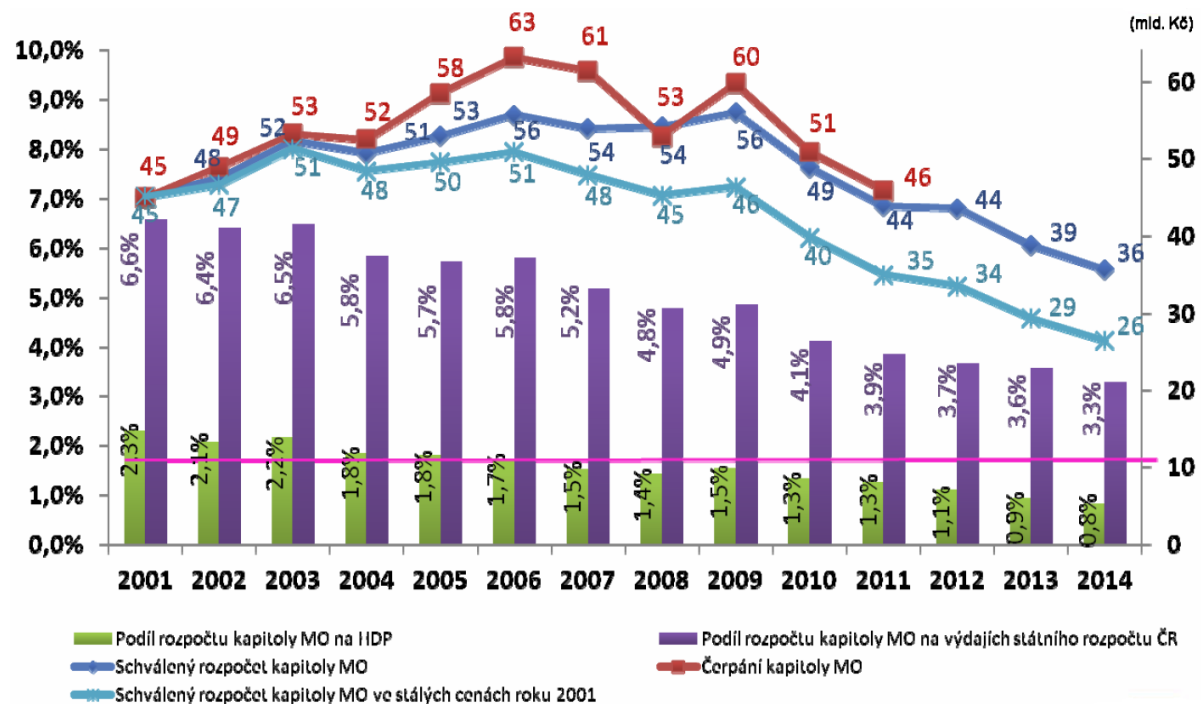
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<sup>2</sup> *Manažerské shrnutí Koncepce ekonomického řízení v rezortu Ministerstva obrany.* Praha: Ministerstvo obrany České republiky. 2013, 47 s. Čj. 121/2013-2013.

- It will be created the necessary communication links between the different elements of economic management department to ensure the efficient functioning of the system as a whole, without unnecessary information and loss of time;
- Adjustments will be implemented in the information systems used to ensure the interconnection of all information necessary for economic management and decision making. It is primarily a system of FIS, ISL, and TENDERMARKET IISSP.

Figure 1 shows the development budget expenditures of the defence sector in the years 2001 -2014.

Figure 1 **Development department of defence spending in the years 2001-2014**



Source: Ministry of Defence of the Czech Republic: Ministry of Defence: Finance and Contracts: Departmental Budget: MO 2012 - presentation. [online]. Prague: Ministry of Defence, 2012 [cit. 28.07.2014]. Available from: <http://www.mocr.army.cz/finance-a-zakazky/resortni-rozpocet/resortni-rozpocet-5146/>

Problem areas in economic management in the defence sector: <sup>3</sup>

- A. Preparation of the budget, despite the introduction of goal-oriented budgeting was implemented using incremental budgeting and primarily based on the existence of the organizational structure,
- B. The current structure needed for managing the economy no longer correspond to the needs and requirements of the MoD. It provides financial security and financial management of individual organizational units, but the structure, competence of economic services does not allow effective economic management by objectives,
- C. The outputs are provided from accounts in the MoD used for decision support various levels of command and control,
- D. In the system of management of the property is not created one entity for integrating the unified management of the acquisition, cataloguing, management and disposal of assets with exactly defined roles in the planning process and meeting the needs of property,
- E. Almost all organizational units are within its organizational structure of the body that takes property or services for the benefit of objective, which is justified by the existence of this organizational element,
- F. The MoD is not created body that would straddle the top positions of the individual processes in response to the method of management by objectives and Defence Minister guarantee the correctness of the processes and system solutions for use of various resources, i.e., It is necessary to use project management.

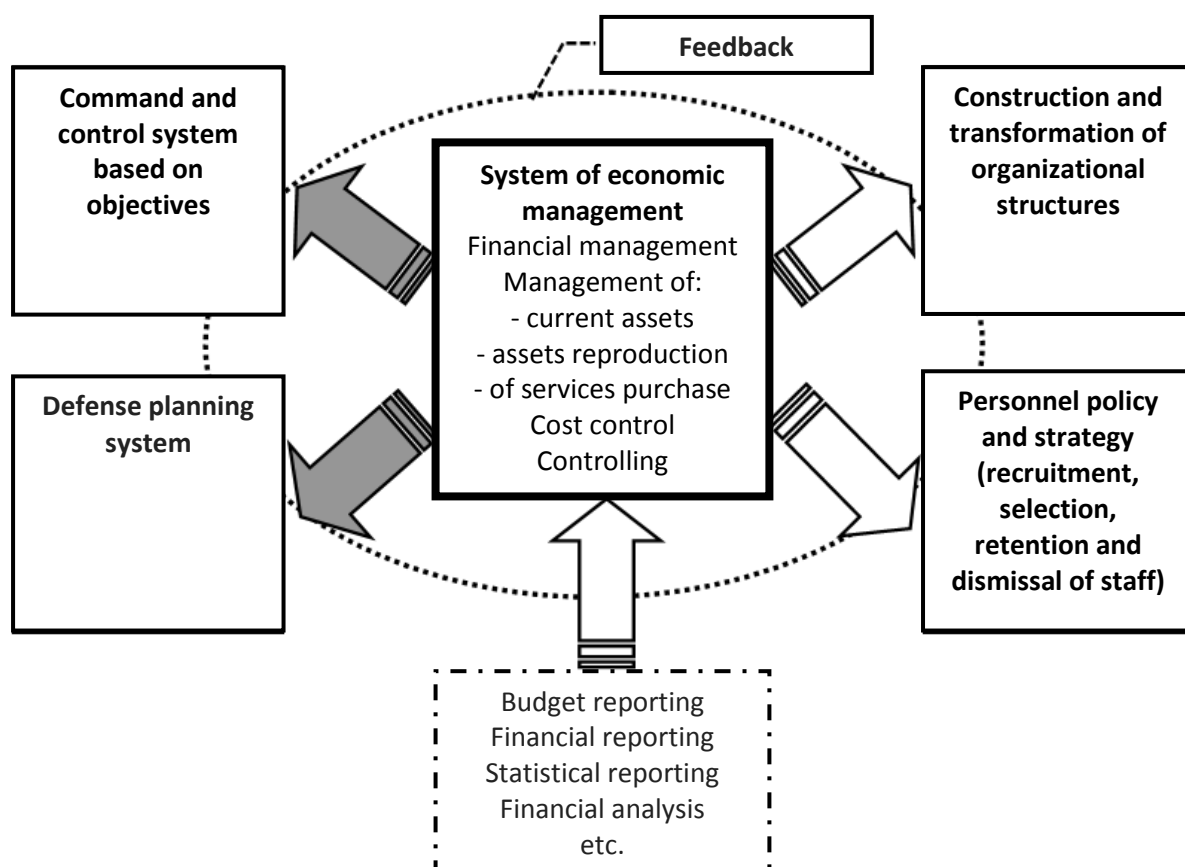
## 2 Economic resource management in defence

**Economic management** should be seen as an integrated system elements - **resource planning, budgeting, financial management, management of current assets, management of assets reproduction, cost control, cost accounting, financial analysis, controlling** - whose information is then **evaluated using economic methods and provide crucial information to management organization**. The system of economic management in the defence sector is shown in Figure 2.

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<sup>3</sup> BALVÍN, Pavel. *Koncepce ekonomického řízení v rezortu Ministerstva obrany*. Praha: Ministerstvo obrany České republiky. 2013. PPT.

Figure 2 **System of economic management in the defence sector**



Source: *The concept of economic management in the Ministry of Defence. Prague: Czech Ministry of Defence. 2013 47 s. Ref. 121 / 2013-2013.*

Subsystem **Financial management** is the main part of the system of economic management. Within this subsystem is implemented budgeting, decision making and organizing financial security department.

Subsystem **Management of current assets**<sup>4</sup> provides an analysis, establish and maintain an optimal level, structure and usage of material stocks corresponding to the needs, abilities and goals of the resort.

Subsystem **Control reproduction property**<sup>5</sup> (program funding) provides acquisition, technical evaluation, maintenance and repair of fixed assets MoD eventually other expenditures and activities designed to achieve specific goals. The main task of this subsystem is an overall economic effectiveness of programs measured in terms of financial analysis tools in the form of net present value, profitability and return.

<sup>4</sup> Oběžná (krátkodobá) aktiva jsou zejména: materiál, nedokončené výrobky, zboží, peněžní prostředky na účtech nebo v hotovosti, pohledávky, ceniny (např. stravenky) – jejich nejdůležitější charakteristikou je, že se **spotřebovávají** – spotřebou tento majetek zaniká, v podniku (organizaci zůstávají dobu kratší než jeden rok).

<sup>5</sup> Česká republika. Zákon č. 218/2000 Sb., o rozpočtových pravidlech a o změně některých souvisejících zákonů, ve znění pozdějších předpisů. In: Praha: PS PČR, 2000. §12 a § 13.

Subsystem **Costs management**<sup>6</sup> through cost calculations will transform accounts cost breakdown capabilities through costs will be allocated to individual departmental goals, which will give rise to these costs. All costs must be linked to the objectives set.

Subsystem **Controlling** will ensure in particular continuous comparison of actual and planned values of economic indicators, identifying their variations as during that period, and after its completion and removing the negative impact of these deviations, or adopting measures to eliminate their future occurrence.

Controlling as a tool used to monitor the behaviour of economic organization based on benchmarking of inputs and outputs. The management system is focused on the result, which coordinates the planning, control and information flows. It leads to every process in the organization made repeated at least as well or better compared with the previous period. The introduction of controlling management system allows managers aims to increase the effectiveness of using a continuous and systematic comparison of facts and desirable (pre-planned) state in the economic process, evaluation of anomalies observed, finding their causes, proposing measures to correct them, or to update the set objectives. Making full use of the potential of the control is only possible after creating a calculation of the planned costs, which will be determined by an impassable limit costs associated purpose (causality) to targets (performance). A prerequisite for successful implementation is controlling **an information base based monitoring costs**.

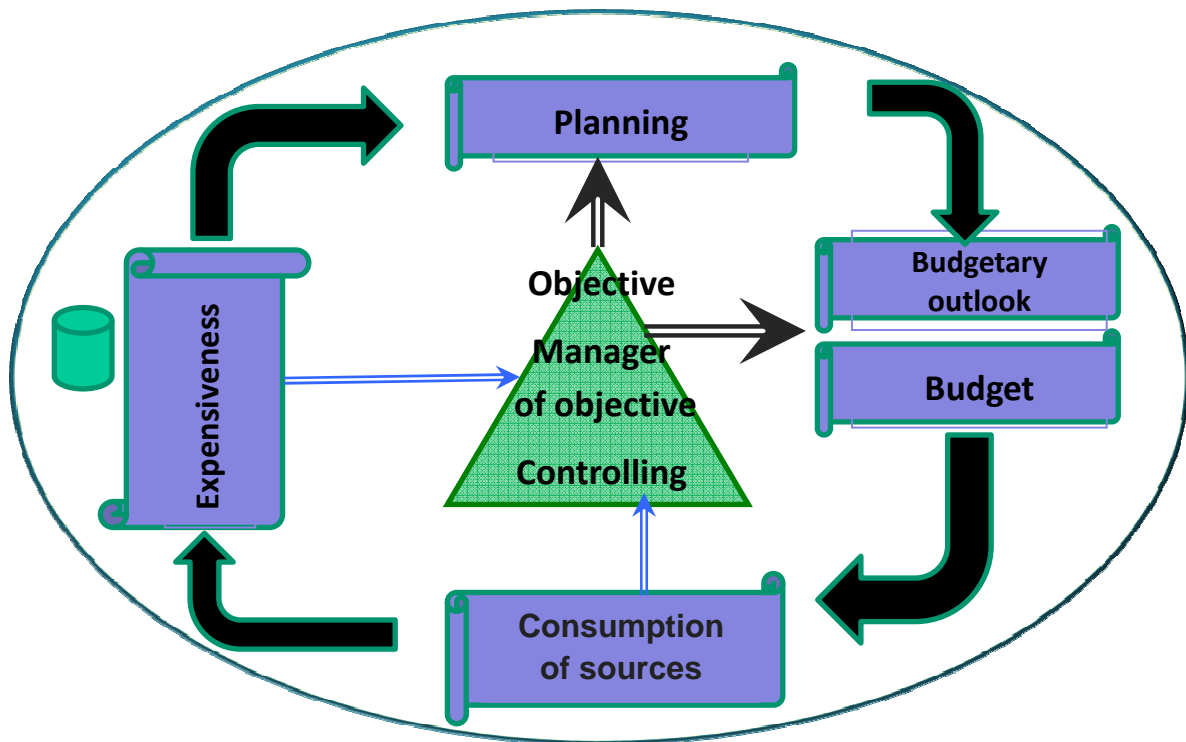
The condition of the economic management of any organizational element is **to know and understand how what target (output) worth of cash resources**, i.e., must be expressed in value all the partial performances in quantifiable variables - relational variables (time, person, piece kilometre etc.). It is a fulfilment of the principle "What I want to drive, you must be able to measure".

Along with the implementation of economic management implements a new system of resource management, which shows in Figure 3.

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<sup>6</sup> Náklady představují spotřebovávání (u dlouhodobého majetku opotřebovávání) ekonomického zdroje, které je spjato se současným nebo budoucím výdejem peněz.

Figure 3 **System resource management in the defence sector**



Source: BALVÍN, Pavel. The concept of economic management in the Ministry of Defence. Prague: Czech Ministry of Defence. 2013. PPT.

### 3 The financial management system in the defence sector

Subsystem of Financial management is the main part of the system of economic management. Within this subsystem is implemented budgeting, decision making and organizing financial security of the Ministry of Defence.<sup>7</sup>

In the defence sector, particularly at the tactical level brigade - battalion, it is important how can executives, professionals and officials planning authorities correctly formulate the goals of the Nomenclature of concrete actions - tasks as part of measures aimed at achieving set objectives.

That objective must comply with conditions such as:

- **Availability** - setting objective should be realistic with regard to the initial conditions for performance and resources that are available;

<sup>7</sup> RYCHEL, Jozef a Jozef STRNÁDEK. Financování vojenských schopností a vojenské strategie počátku 21. století. *Vojenské rozhledy*. Praha: 2002, č. 4, s. 62. ISSN: 1210-3292.



- **Simplicity, brevity and clarity** - objective must be clearly formulated;
- **Concreteness** - the objective must be clear and definite.

The role of financial management is to find ways to streamline the various activities and use of funds, which the Ministry of Defence for the calendar year, and so fulfil the assigned tasks.

The main task for tactical brigade - battalion (regiment) securing sufficient amount of financial resources and their optimal structure and use in terms of the tasks to be given organizational unit in the organizational structure to meet at a certain period in compliance with the principles of economy, efficiency and effectiveness.

Order of Minister of Defence no. 72/2012 *Financial management and financial security* than previously valid warrant specifically defines financial management "as a tool for managers goals as an integral part of economic management, ensuring economical, efficient and effective allocation and use of funds in due time and in accordance with the objectives Ministry of Defence."<sup>8</sup>

Financial management is the management of money flow from the center towards the cost centers in their implementation. This definition does not answer to any of the definitions of financial management, but these are created and applied particularly in the civilian business sector.

Financial management is carried out in the budgeting process, the realization of personal expenses, financing, accounting<sup>9</sup>, financial control<sup>10</sup> and controlling:

- Determining the desired state funds (state approved budget, budget changes after a final budget) and their structure (state funds for budget sentences, Art. 10) depending on the utilization of personnel and property and their correction within a specified time;
- Recording and monitoring in cash, receivables, payables and property;
- Organizing employee activities economic services.

For creating the concept and methodology of financial management and financial security in the Ministry of Defence is responsible Deputy Defence Minister for Economy and Deputy Assistant Secretary of Defence for the economy - Director of

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<sup>8</sup> R MO č. 72/2012. *Finanční řízení a finanční zabezpečení*. Praha: MO, 2012, čl. 3.

<sup>9</sup> NVMO Fin-1-2 *Vedení účetnictví v působnosti resortu Ministerstva obrany*. Praha: MO, 1993.

<sup>10</sup> R MO č. 5/2003. *Finanční kontrola v působnosti MO ČR*. Praha: MO, 2003 a Česká republika. Normativní výnos MO ČR č. 16/2003 Věstníku. Výkon finanční kontroly v působnosti Ministerstva obrany. In: 16/2003. Praha: MO ČR, 2003. Dostupné z: <http://www.mocr.army.cz>

the Economics Department of Defence by the scope specified in the Rules of Organization of the Ministry of Defence. Responsibility deputy assistant secretary for economy - Director of the Economic Department of Defence determines the particular Article 56, Order of Minister of Defence no. 72/2012.

The administrator of this chapter is the senior employee is designed to perform the scope of the chapter administrator Organizational Regulations of the Ministry of Defence.<sup>11</sup>

The chapter administrator also sets a target-oriented budget structure based on target- oriented budgeting in accordance with the applicable dial objective MoD. It is presented in the income and expenditure budget structure, which defines specific indicators chapter (objective Level 1 match expenditure blocks<sup>12</sup>), approved by the Ministry of Finance. Goal-oriented structure of the budget chapter administrator submits for approval to the Ministry of Finance in the structure prescribed by the law.<sup>13</sup>

#### **4 Economic management, financial management and financial support to various levels of command and control by the authorities, economic services**

The aim of economic management in the Ministry of Defence (Czech Army) is clearly define the scope of authority of economic services at individual levels of command and control so that it is clear what activities are to be carried out and secured in favour of the goals of the manager level (in relation to established budgetary competencies linked to structure objectives), and in the realization of expenditure in favour of leading organizational unit as the principal operations by type:

- **A** - Support Manager of objective Level 1 - economic management;
- **B** - Level of middle management - financial management;
- **C** - Level lower management - financial security.

##### **A. Support for of economic management at the manager level 1**

Manager Support objective - general part

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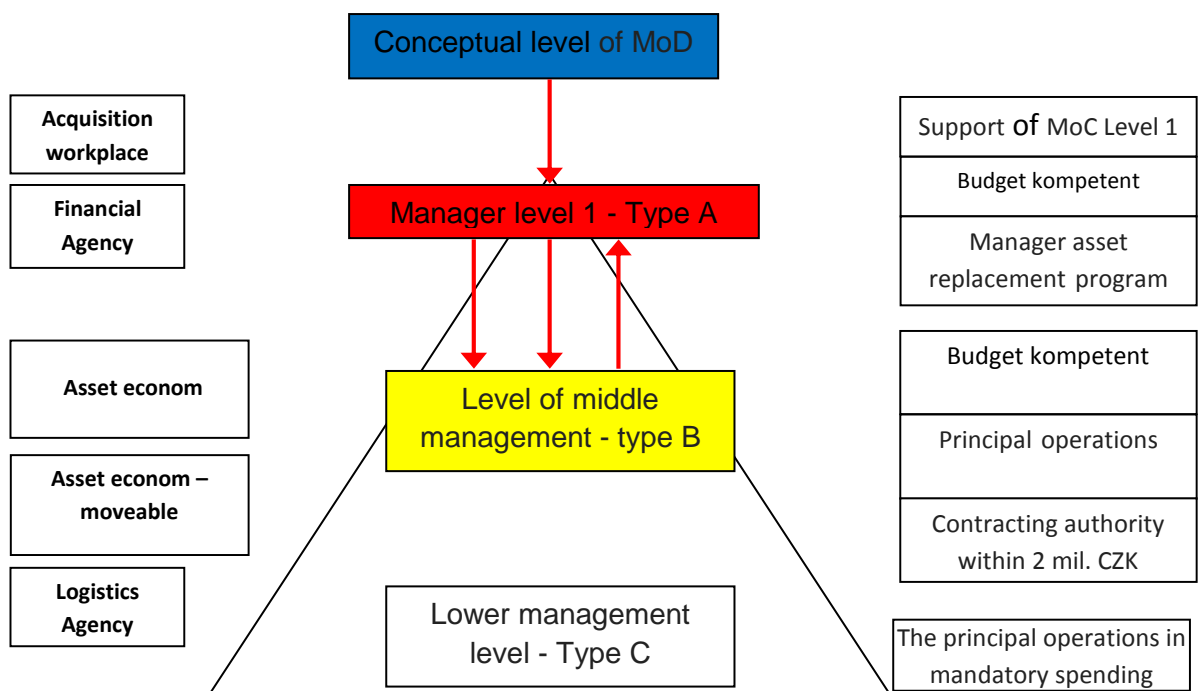
<sup>11</sup> čl. 256, příloha č. 1, Organizačního řádu Ministerstva obrany.

<sup>12</sup> R MO č. 66/2012. *Plánování činností rozvoje v resortu Ministerstva obrany*. Praha: MO, 2012.

<sup>13</sup> Česká republika. Vyhláška Ministerstva financí ČR č. 415/2008. In: 415. Praha: 2008. [cit: 2013-05-24], Dostupné z: <http://www.sbcr.cz>, příloha č. 6. Vyhláška byla ke dni 1. 6. 2013 zrušena, pro resort MO nebyla vydána nová norma, platí jen R MO 66/2012.

Responsibility for the preparation and implementation of the objectives first level is the Ministry of Defence divided among several managers of objectives. Within MoD (civilian part) perform this job, first deputy defence minister and the secretary general MO (Secretary of State), at MoD (military section) is the Deputy Chief of the General Staff - Chief of State and at Czech Army has the role of Chief of Staff of the Army. Within the military intelligence is a director of military intelligence. Another element is the commander of the castle guard, Deputy Minister of Defence (area under the care of the national sport teams). Structure of economic governance is shown in Figure 4 below.

Figure 4 Structure of economic management



Source: *The concept of economic management in the Ministry of Defence. Prague: Czech Ministry of Defence. 2013 47 s. Ref. 121 / 2013-2013.*

Supporting of managers of objective Level 1 is (will be) implemented in the framework:

- Substantive planning of objectives (documentation of objectives) and their implementation at a lower level in the creation of the SDP;
- Manage the processing of documentation asset replacement program and deciding on the implementation of requirements in program funding;

- Determining the needs of personnel and property resources linked to the allocation of funds, including their mutual balancing;
- approval of proposals to create or change organizational structures;
- Financial Management - documents in the medium-term budget outlook, budget, implementing the multiannual budget, change management and change management budget for the current year;
- Professional management of subordinate economic structures in economic management;
- Financial control of their management competence;
- Management of current assets - establishing and maintaining an optimal level, structure and usage of material stock meeting the needs, possibilities and objectives of the relevant the manager;
- Cost management;
- Controlling.

## **B. Elements of economic management at middle management level**

At middle management level, it is about creating economic decision support brigade commander (bases) or other organizational units, who will be based on this concept included structure units (device) type B. Their scope is very broad, because in the real state will manage and influence the economic behaviour of subordinate units (type B1) or provided departments (type B2). The basic change is that in the process of financial planning and budgeting will play a unique role towards the manager and objective from subordinates or provided units (devices) will require cooperation. In terms of the budget process will be the **lowest budget competent (implementation of change management budget - the current period and even multi-year period)**.

Their scope can be divided into the following areas:

- Security NS Business Type B - supporting the principal operations;
- Management of financial resources and ownership of resources - support the manager objective;
- Management of economic services units subordinate (provided) bodies (devices) - Type C.

The area of CC type B will include in particular activities to the financial security of persons and financing of their own CC or for intended CS, in the areas of salary requirements and other personal compensation, addressing FCSN, evidence of damages and claims.

**To ensure the application possibilities of economic management structure professionally prepared for implementation documents for leading organizational unit to the economic management of all resources (personnel, property and cash) were organs of economic services included in the direct subordination of the head of the organizational unit, i.e. removed from the organizational structure of Deputy Minister of Defence.**

In order to more clearly separate organizational units MoD we distinguish elements supporting economic management at middle management level in two groups:

- **B1** - organizational units MO at the brigade level or foundations;
- **B2** - are other organizational units MO, which does not have the organizational structure of the same level as the organizational units included in group B1, but due to a functional system of economic management settings will be set scope and responsibility within the group of elements supporting economic management B

### **C. Elements of economic management to lower management level**

Lowest organizational element in the system of economic management is organizational units at a lower level of management - type C. Their main task will be to implement their own financial security in areas CC salary requirements and other personal compensation, addressing FCSN, evidence of damages and claims. Furthermore, the acquisition process will be decentralized supply plan, which will be submitted to the superior degree of control and approval. Based on this approved plan will be able to acquire the assets and services needed to carry out certain tasks

The following events occurred:

- Remove the powers and duties of the financial competent;
- Increased control procurement of goods and services before the emergence of a legal commitment or. after the acquisition of property or services by a superior organizational element;

- Data acquisition usable to control the cost of senior level organizational unit.

In the event that a given organizational unit will not have the organizational structure of economic institutions will not be able to acquire assets and services. This activity will be implemented for the benefit of the designated organizational entity - type B, where the assignment of this element will only be possible after approval by the chapter administrator.

In order to more clearly separate organizational units MO distinguish **elements supporting economic management to lower management level** into three groups:

- **C1** - Organizational units MoD battalion level;
- **C2** - Other organizational units MoD, which does not have the organizational structure of the same level as the organizational units included in the group C1, but due to a functional system of economic management settings will be set scope and responsibility within the group of elements Economic Management Assistance C and at the same time they have in their organizational structures systemized positions for economic and other professional bodies to promote economic management;
- **C3** - Organizational units of the MoD, which have in their organizational structures created, systemized positions organs economic services. Financial security and economic management of this type of NS will provide designated, or in the organizational structure of the parent unit.

## 5 Resources Defence funding

The basic resources for defence include:

- State population,
- Material resources and related services,
- Funds.

The **population** is an important source of human capital used for national defence. An interesting indicator is obviously manpower professional army on 1 inhabitant of the country. Countries have also given many members of the army should have, if

there was an imminent military conflict in the Czech Republic this figure makes about 50 000 people.<sup>14</sup>

Material resources stem mainly from industrial and agricultural production. However, this is also the technical, technological and capital equipment that may get in other sectors and which serve to further various activities of the Army (e.g. clothing, vehicles, etc.). Regarding services, defence used particular services such as repairs, cleaning, security, security, etc. These services can provide either internally or externally.<sup>15</sup>

The most important source of funding for defence, however are **financial resources**. These funds stem from the state budget, which is earmarked directly chapter for the Ministry of Defence and that chapter 307.

Resources can earn market and non-market way (command). Which method is chosen depends on the kind of the economy of the country. Democratic states often use a combination of both ways, the market-based approach prevails in peacetime.

#### **List of tasks for students:**

1. Explain the implementation of the system of economic management in the defence sector.
2. Explain the economic system resource management.
3. Explain the financial management system.
4. Characterize the economic management by the economic authorities in the defence sector.
5. Try to define and characterize the basic elements of financing the defence sector.

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<sup>14</sup> PEKOVÁ, Jitka. *Veřejná správa a finance veřejného sektoru*. 3., aktualiz. a rozš. vyd. Praha: ASPI, 2008, 712 s. ISBN 978-80-7357-351-5, s. 576

<sup>15</sup> Tamtéž.