



# Don't expect a commercial ERP to do the **government's job**

Because the mission of state and local governments is to deliver services driven by policy and legislative mandates, they cannot operate like for-profit businesses. The level of transparency into financial, budgetary and human resource activities needed exceeds any private sector requirements. This paper discusses why these and other differences between the public and private sectors affect the type of enterprise resource planning solutions needed to support the unique business of government.

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# Should government be run like a business?



This seemingly common-sense idea permeates the 24/7 news cycle, and often is amplified in election years. Without debating the politics of the statement, one can examine the pragmatic reality that there are valid reasons why such an approach is not always feasible or appropriate. Although it makes for compelling stump speeches and news panel discussions, the reality is that fundamental differences exist between the objectives of public and private sector organizations. Not only do primary objectives differ significantly, but so do the mechanisms used to manage, monitor and report on those objectives. For businesses, the objective is to maximize profit by managing voluntary capital investment, and publicly held companies must keep shareholders informed by filing periodic reports and other materials. For government entities (including public authorities, agencies and school districts), the objective is to deliver essential services through compelled investment by means of mandated tax revenue, while providing transparency and accountability of operations to constituents.

These oversimplified differences help illustrate why enterprise resource planning (ERP) solutions used to manage an organization's financial health cannot be one-size-fits-all for business and government. Since government is not intended to generate a financial return on investment, but rather deliver services in an efficient and effective manner, supporting technology should enable execution of political mandates natively, without the need for bolt-on processes or customizations that add complexity and are costly to support and manage.

The DNA of public sector ERP solutions should be embedded with government best practices and mandated Governmental Accounting Standards Board (GASB) compliance. Yet, "commercial first" ERP solutions often overlay these attributes in an extension layer or as a customization on top of the baseline. The nuances of a wealth-generation focus as compared to a public service focus require operational distinctions that should be inherent in the ERP architecture and underlying accounting models.

A truly built-for-government ERP solution is essential to providing the most cost-effective, efficient and accurate solution to meet the needs of public sector entities.

**The five key areas of public sector operations that are distinct from private sector activities and should be addressed as part of the DNA of a government ERP solution include the following, each of which are covered in greater detail in this paper.**

## 5 unique requirements for public sector ERP

Key Area	Description
1. Modified accrual accounting	Enables visibility into the cash position of a public entity while still adhering to matching principles inherent to accrual accounting
2. Fund accounting, flexible chart of accounts and reporting	Provides dynamic capabilities to structure chart of accounts to combine and/or segment roll-up information to deliver appropriate detail for transparency and mandated reporting
3. Budgeting and budgetary controls	Includes embedded controls and real-time business edits to maintain the budgetary authority within acceptable tolerances and prevent entities from overcommitting funds in daily business transactions
4. Public sector procurement processes	Provides transparency into government procurement practices such as sealed-bids through electronic lock-boxes, public notifications of intent to award, and Disadvantaged Business Enterprise (DBE) certification and tracking
5. Public sector bargaining units	Defines position classification and compensation that represents the unique rules of a specific bargaining unit; employees hired into that position then inherit all predefined rules without individual reconfiguration at the detailed employee level

## Modified accrual accounting

The budget of a government entity provides the legal authority for it to use its resources in the delivery of public services. Such entities have an obligation to maintain budget adherence with the acquisition and use of financial resources, and to ensure that the revenues brought in are sufficient to cover short-term expenditures.

As a result, governmental reporting requires various bases of accounting. Neither the cash basis of accounting (i.e., revenues and expenses recognized when they occur)<sup>1</sup>, nor the accrual basis of accounting (i.e., revenue recognized when it is earned and expenses recognized when they occur)<sup>2</sup>, alone provides the reporting detail necessary for accurate transparency and insight into a public sector entity's financial position across all funds (e.g., governmental, proprietary and fiduciary).<sup>3</sup>

Modified accrual is required for governmental funds where revenue is recognized when it is measurable and available and expenses are recognized when goods or services are received (or a legal obligation exists to pay). Modified accrual is necessary to enable visibility into the cash position of a public entity while still adhering to matching principles inherent to accrual accounting.<sup>4</sup>

ERP solutions for the public sector must be able to track discrete transactions in a way that allows for reporting on a modified accrual basis. This includes a mechanism to track a government's ability to pay short-term liabilities, yet still sufficiently track the matching revenue-related transactions used to fund the delivery of services to their constituents. Built-for-government ERP solutions with inherent capabilities to facilitate reporting on the modified accrual method, while also supporting other bases of accounting, avoid the need for complex customizations.

## Fund accounting, flexible chart of accounts and reporting

Public sector entities require a far more transparent accounting model than do publicly traded corporations. Publicly traded companies must report performance of profit and loss (P&L) to investors, but the specific detail of expenditures and revenues remains broadly opaque to the general public. Entities within the public sector must adhere to legally adopted budgets and provide traceability to the means in which revenues are obtained and the use of those revenues to fund expenditures.<sup>5</sup>

Government activities require different degrees of accountability for specific revenue and expense transactions in support of those activities; therefore, government accounting systems must be able to support nuanced fund controls to dictate these behaviors and options. As detailed in the previous section, different funds have different reporting requirements according to their bases of account—a concept not common in the private sector—requiring public sector ERP solutions to provide the ability to support multiple accounting methods and behavioral characteristics inherent to each group of funds (e.g., governmental, proprietary and fiduciary) as well as the subsets of funds within each group.

Beyond the controls and treatment of funds themselves, it also is important for public sector ERP solutions to provide the capability to control the consolidation and aggregation of fund detail via configurable “roll-ups” to present the appropriate level of visibility through reporting.

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<sup>1</sup> “Cash Basis of Accounting.” *Government Reporting Overview*. Fiscal Management Division, Texas Comptroller of Public Accountants.

<sup>2</sup> “Modified Accrual Basis of Accounting.” *Government Reporting Overview*. Fiscal Management Division, Texas Comptroller of Public Accountants.

<sup>3</sup> “Touring the Financial Statements, Part III: The Governmental Funds.” *The User's Perspective*. Governmental Accounting Standards Board. November, 2007.

<sup>4</sup> “Contrasts between Modified and Full Accrual.” *Government Reporting Overview*. Fiscal Management Division, Texas Comptroller of Public Accountants.

<sup>5</sup> “Why Governmental Accounting and Financial Reporting Is—and should be Different.” Massachusetts Municipal Association.

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Consolidation elements like roll-ups allow entities to perform summary and detail level reporting with the same data by simply changing reporting parameters. Furthermore, as organizations restructure over time, configurable roll-ups can be easily modified to facilitate reporting on different fund consolidation structures, without the need for customizing the chart of accounts.

The Government Finance Officers Association’s (GFOA’s) *Best Practice Advisories for Using Fund Accounting More Effectively* notes the following: “Sometimes governments inappropriately combine funds in their financial statements that ought not to be combined, thus denying financial statement users valuable information on legal compliance. More commonly, governments report more funds than are truly necessary to achieve the goals of general purpose external financial reporting, thereby needlessly adding to the length and complexity of their financial reports and potentially increasing audit fees.”<sup>6</sup>

While not enough detail is problematic for transparency, too much detail can be a costly and unnecessary burden on governmental entities. Therefore, it is equally as important for roll-ups to not just exist, but to also be flexible enough to adapt to the changes in mandates and administrative directives.

Looking a layer deeper, simply tracking revenue sources and objects of expenditure within a fund is rarely sufficient to tie appropriations and revenue to spending within a public sector entity. Complexities of administering public sector-specific constructs, such as grant funding for programs and projects, require far more granular management of transactions—often managing to the activity or even task level is necessary. To achieve this, government ERP solutions need the ability to define chart of account structures that deliver flexible reporting capabilities depending on the nature of the transactional activity.

While certain expenditure types require relatively straightforward allocation to the funding source, other project-based activities require additional reportable elements and tracking beyond simple object of expenditure. The Comprehensive Annual Financial Reports (CAFR) must be generated in accordance with the Governmental Accounting Standards Board’s (GASB) required reporting standards.

Government ERP solutions should allow for dynamic structuring and architecting of not just the organizational structure, chart of accounts and roll-ups, but also of the CAFR report elements themselves.

Each required statement within CAFR serves a purpose, and not all entities are structured the same way. Public sector ERP solutions need to provide necessary functionality that is both powerful and adaptable to deliver the reports and statistical data for CAFR reporting.

Forcing these government-specific complexities into a solution not designed for such variation can create an inefficient structure of reporting elements and data resulting in overly complex and potentially non-compliant reporting.

## **Budgeting and budgetary controls**

A public sector budget defines how a government will raise revenue and incur expenses to fulfill its mission. Beyond establishing a budget, the entity must also manage the publication, amendments and updates, and transactional control of the budget. Most businesses do not face the legal constraints of the governmental budgeting process, and rarely, if ever, release budgets publicly due to the sensitive nature of their contents. Furthermore, while private sector managers must comply with the budget controls established by their firms, specific revenue and expense allocations are rarely required by legal mandate or public policy.

For ERP solutions to meet the unique budgeting constraints of government, they need to generate a publish-ready version of approved budgets for constituent consumption.

<sup>6</sup> “Using Fund Accounting Effectively.” *Best Practices/Advisories*. Government Finance Officers Association, October 2012.

They should provide the ability not only to generate reports on current and prior year budgets, but also be able to easily aggregate this quantitative content with narrative text, tables, graphics and images to help fully convey the budget details to engage citizens and enable a transparent view into operations.

Government ERP solutions should also provide mechanisms to enact budgetary control in accordance with the legally adopted budget. Embedded controls at the system or fund level are important to maintain the budgetary authority within acceptable tolerances and prevent entities from overcommitting funds in daily business transactions. Financial solutions that include out-of-the-box, real-time edits and budget posting engines allow government entities to operate on current information and do not require an offline batch or posting cycle to check for available budgetary authority.

Lastly, entrenched with budgetary controls is the encumbrance accounting model that is unique to the public sector. As noted by the California Department of Finance, “By recording the estimated cost of purchase orders and contracts as encumbrances, managers are aware of the future impacts of previous financial decisions.”<sup>7</sup>

ERP solutions for government should deliver out-of-the-box pre-encumbrance and encumbrance capabilities, reserving funds within the approved budget to enable judicious spending, to help government entities maintain adherence to the revenue and spending guidance defined by the jurisdiction’s political process.

## Public sector procurement processes

In private enterprises, purchasing decisions are an internal operation. Firms often can create competitive advantage against their peers from their procurement and sourcing practices. Public disclosure of purchasing decisions in the private sector could negatively impact a firm’s success by disclosing sensitive “what,” “from whom” and “how much” data about buying decisions.

Conversely, the Institute for Public Procurement states that, “Transparency in public procurement is critical. The manner in which government conducts itself in its business transactions immediately affects public opinion and the public’s trust in good government. In addition to encouraging the public’s good will and strengthened trust, the more practical business benefits of transparency are increased competition and better value for goods, services, and construction.”<sup>8</sup>

Government ERP should function as a marketplace platform, facilitating public bidding rather than hand-selecting specific vendors from which to solicit bids. This is essential to providing transparency into government procurement practices. Interwoven with a public bidding or solicitation processes is a multi-step sourcing lifecycle, differentiated from the private sector by mechanisms, often mandated, to ensure lawful and fair bid evaluation and award. Capabilities to handle sealed-bids through electronic lock-boxes and public notifications of intent to award provide governmental constituents assurances that procurement processes remain fair in accordance with the entity’s governing laws.

Additionally, unlike private sector businesses, public entities must often seek opportunities to leverage Disadvantaged Business Enterprise (DBE) certified vendors in public contracts. A built-for-government ERP solution should provide the capability to track and easily report on DBE activity within the jurisdiction.

The ability to easily track multi-year or complex funding allocations across fiscal years when a contract activity spans multiple years is native functionality expected of an ERP solution intended for public sector entities. Roll or lapse functionality eliminates the need for manual conversion of contracts at the end of the fiscal year.



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<sup>7</sup> “Encumbrance Accounting.” *CALSTARS Procedure Manual*. California Department of Finance, March 2004.

<sup>8</sup> “Transparency in Public Procurement.” *Principles and Practices of Public Procurement*. The Institute for Public Procurement, 2012.

**A key differentiator of government ERP solutions is the ability to center all HRM information down to the employee bargaining unit.**

## Public sector bargaining units

The management of human capital within the public sector also varies greatly between governments and businesses. While union representation and collective bargaining are prevalent in both sectors, collective bargaining within the government space impacts the public interest (or electorate) as a whole by dictating the level of services provided to the public and the resulting tax implications.

By contrast, private sector collective bargaining limits the impact to only the parties involved in the agreement (labor, management and the consumers of private goods and services), and does not impact the greater public welfare.<sup>9</sup> Furthermore, public sector employees have a union membership rate more than five-times that of private sector workers (35.2% as compared to 6.7%) according to the U.S. Department of Labor—Bureau of Labor Statistics.<sup>10</sup> Because the tax-paying public is a key stakeholder in the public sector human resource management (HRM) process, it is important that salary and benefits of employees within the public sector are accurately and efficiently managed to only the negotiated positions established by their bargaining units.

Government ERP solutions must be able to center all HRM information down to the employee bargaining unit. As such, HRM for government is often defined by the unique needs and requirements of individual bargaining units and employee unions within the organization. When a position is created, HRM should be able to define that position to a classification and compensation that represents the unique rules of a specific bargaining unit. Once an employee is hired into a position, and classification and compensation rules are either inherited for that position, all predefined rules for that bargaining unit are then inherited for the employee.

**These predefined HRM rules can include:**

- **The ability to pay overtime at one rate for one union contract while other union contracts and unrepresented employees may receive overtime at another rate**
- **The ability for one group of employees to be eligible for a different set of benefits than another**
- **The ability to maintain different leave accrual, usage and balance rules for the same leave type (e.g., vacation or sick leave) for employees in different bargaining units**
- **The ability to maintain complex Fair Labor Standards Act cycles and related rules for employees within different bargaining units**
- **The ability to define performance management goals for individual employees, or a group of employees, and rate each employee against those goals during any review cycles**
- **The ability to manage employee detail at unique levels associated to bargaining units, which are fundamental to addressing the complexities of government HRM. ERP solutions should inherently address these capabilities without the need for site-specific customizations.**

<sup>9</sup> “Public Sector Bargaining: A Different Animal” Clyde Summers, University of Pennsylvania Journal of Business Law. Volume 5, Issue 3, p. 441, 2003.

<sup>10</sup> “Union Members Summary,” Economic News Release. United States Department of Labor—Bureau of Labor Statistics. USDL-16-0158. January 28, 2016

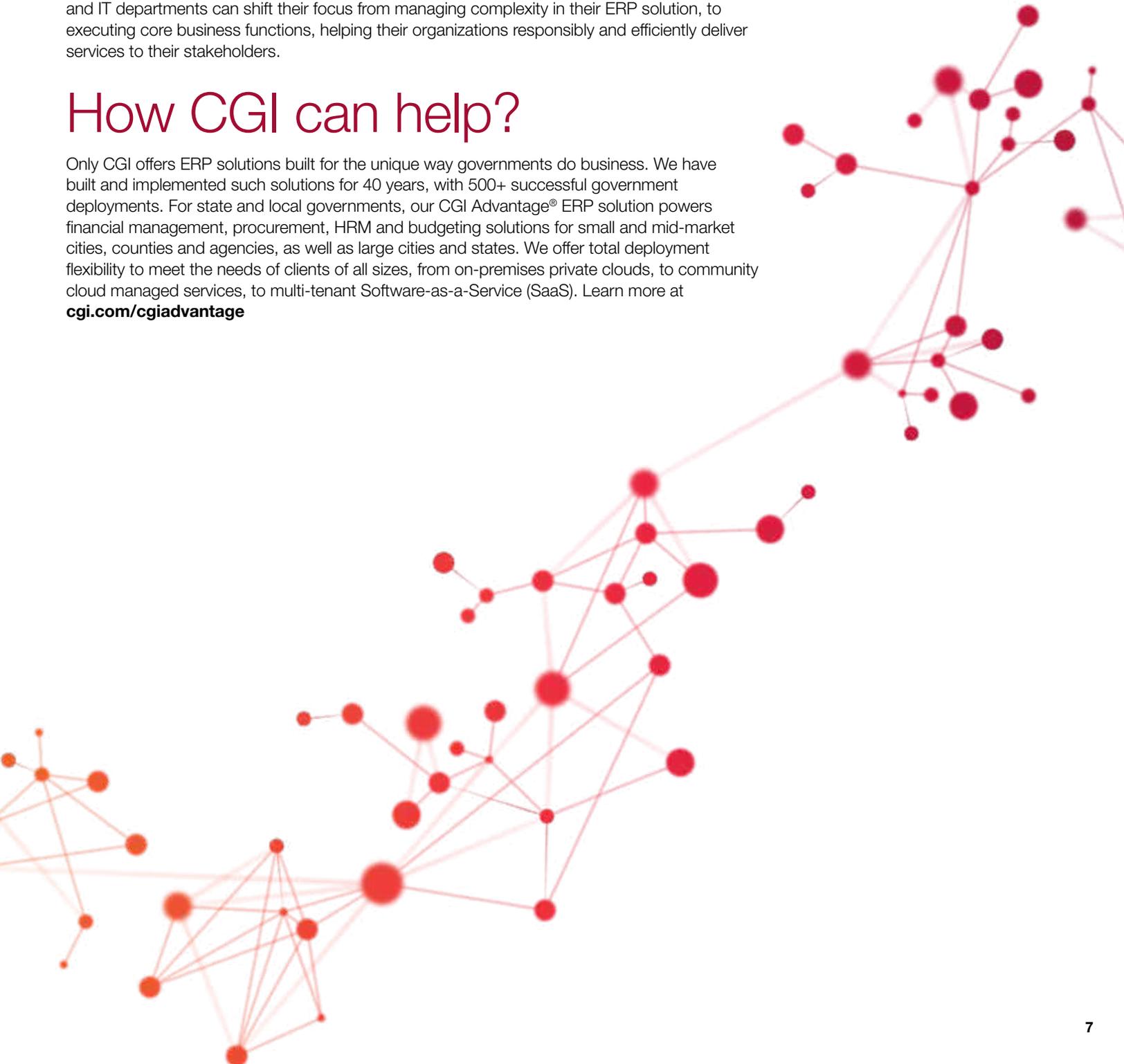
# Conclusion

Because the underlying mission of governments is to deliver services as a result of the policy of elected officials, they cannot operate like businesses when it comes to financial management. The level of transparency into the financial, HRM and budgetary activities of public sector entities is not applicable in the private sector. For-profit businesses must protect the financial position of the firm beyond what is legally mandated to be released in accordance with private sector regulations. But more is demanded in the public sector, where increased visibility into the inner workings of government operations is not only expected but is growing more significant each year.

Government entities should seek ERP solutions that can accommodate the unique accounting models, budgeting, reporting, procurement and HRM requirements of the public sector without the need for costly customizations. In doing so, valuable and scarce resources across business and IT departments can shift their focus from managing complexity in their ERP solution, to executing core business functions, helping their organizations responsibly and efficiently deliver services to their stakeholders.

## How CGI can help?

Only CGI offers ERP solutions built for the unique way governments do business. We have built and implemented such solutions for 40 years, with 500+ successful government deployments. For state and local governments, our CGI Advantage® ERP solution powers financial management, procurement, HRM and budgeting solutions for small and mid-market cities, counties and agencies, as well as large cities and states. We offer total deployment flexibility to meet the needs of clients of all sizes, from on-premises private clouds, to community cloud managed services, to multi-tenant Software-as-a-Service (SaaS). Learn more at [cgi.com/cgiadvantage](http://cgi.com/cgiadvantage)





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