COURSE GUIDE

PAD 407
PUBLIC FINANCIAL MANAGEMENT

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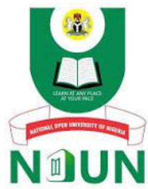

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CONTENTS

Introduction ………………………………………………………. iv
Course Contents …………………………………………………… iv
Course Aims ……………………………………………………… iv
Course Objectives ………………………………………………… iv
Course Materials ……………………………………………….. v
Study Units…………………………………………………………. v
Main Course… …………………………………………………. vi

INTRODUCTION

Public Financial Management (PAD 407) is a first semester course work of 3 credit units taken by undergraduate students of the National Open University of Nigeria (NOUN) in the Faculty of Management Sciences. The importance of public financial management to students of public administration cannot be overemphasized as the course would help develop deeper understanding of how government secure and administer financial resources in order to embark on policies, programs and projects that will grow the economy and promote the general well-being of the citizenry.

This course acquaints you with the fundamentals of public financial management, as well as methods and processes of how government secure funds to meet its obligations. It also aims at encouraging you to acquaint yourself with the budgetary processes and control as well as planning in the public sector.

COURSE CONTENTS

The course has 4 modules and 18 units. Contents of the modules dwell on fundamentals of public financial management; government accounting with specific focus on public revenue and expenditure; budgetary process and control in the public sector; Nigeria's public debt and planning in the planning in the public sector.

COURSE AIMS

The aim of the course is to acquaint you with the fundamentals of public financial management with specific reference to meaning, nature and scope of public finance; monetary and fiscal policies of government; government revenue and expenditure; government budgetary process; accountability and control in the public sector; as well as planning in the public sector.

COURSE OBJECTIVES

By the end of this course, you will be able to:

i. define public finance and public financial management
ii. discuss the nature, scope and objectives of public finance
iii. trace the origin and evolution of public financial management
iv. define public revenue and explain the various ways by which government generate and allocate revenue
v. define public expenditure and explain factors responsible for Nigeria's growing debt profile

vi. define budget and explain the budgetary process
vii. Explain control and accountability measures in the public sector
viii. Discuss planning in the public sector and various types of planning
ix. Discuss the role of multi-national financial institutions in public debt management

COURSE MATERIALS

The major components of this course are:
i. Course Guide
ii. Study Units
iii. Self-Assessment Exercises
iv. References /Further Readings/Web Resources
v. Possible Answers to Self-Assessment Exercises

STUDY UNITS

MODULE 1 FUNDAMENTALS OF PUBLIC FINANCIAL MANAGEMENT

Unit 1 Meaning, Nature, Scope and Objectives of Public Finance
Unit 2 Principles of Public Financial Management
Unit 3 Monetary Policy
Unit 4 Fiscal Policy

MODULE 2 GOVERNMENT ACCOUNTING: PUBLIC REVENUE

Unit 1 Meaning, Objectives and Sources of Public Revenue
Unit 2 Tax and Taxation
Unit 3 Revenue Generation and Management in Nigeria
Unit 4 Fiscal Federalism and Resource Allocation in Nigeria

MODULE 3 GOVERNMENT ACCOUNTING: PUBLIC EXPENDITURE

Unit 1 Meaning, Objectives and Types of Public Expenditure
Unit 2 Canons and Classification of Public Expenditure
Unit 3 Theories of Public Expenditure Growth
Unit 4 Public Debt
Unit 5 Nigeria's Public Debt Profile

MODULE 4 BUDGETING IN THE PUBLIC SECTOR

Unit 1 Meaning, Objectives and Types of Budget
Unit 2 Budgetary Process
Unit 3 Budgeting in the Public Sector
Unit 4 Budgetary Control in the Public Sector
Unit 5 Transparency and Accountability in the Public Sector

MODULE 5 FINANCIAL REPORTING AND AUDITING IN THE PUBLIC SECTOR

Unit 1 Regulatory Framework for Managing Public Finance
Unit 2 Financial Reporting
Unit 3 Analyzing Financial Report and Audit
Unit 4 Accounting Practice and Financial Management Cycle
Unit 5 Financial Misconduct

Everything is contained in each unit except the textbooks, which you may have to acquire. You are expected to study the materials carefully and attempt the exercises. Practice the Self-Assessment Exercises as well. You are also expected to consult the textbooks under references/further readings for additional information. However, you may contact your tutor where you encounter any problem about recommended textbooks.s

MAIN COURSE

CONTENTS

Module 1 Fundamentals of Public Financial Management………….……............... 1

Unit 1 Meaning, Nature, Scope and Objectives of Public Finance... 1
Unit 2 Principles of Public Financial Management………………..…………………..…..... 8
Unit 3 Monetary Policy …………………………….... 16
Unit 4 Fiscal Policy …………………………………..... 22

Module 2 Government Accounting: Public Revenue………………………………………….. 28

Unit 1 Meaning, Objectives and Sources of Public Revenue………………………………..……… 28
Unit 2 Tax and Taxation ………………………….…... 35
Unit 3 Revenue Generation and Management in Nigeria……………………………………………. 48
Unit 4 Fiscal Federalism and Resource Allocation in Nigeria…………………………………………..... 57

Module 3 Government Accounting: Public Expenditure…………………………..……….. 67

Unit 1 Meaning, Objectives and Types of Public Expenditure……………………………….…… 67
Unit 2 Canons and Classification of Public Expenditure……………………………….…… 73
Unit 3 Theories of Public Expenditure Growth…….……. 81
Unit 4 Public Debt…………………… ……………… 89
Unit 5 Nigeria's Public Debt Profile……………….……. 99

Module 4 Budgeting In the Public Sector….……………… 104

Unit 1 Meaning, Objectives and Types of Budget….. 104
Unit 2 Budgetary Process………………………………. 111
Unit 3 Budgeting in the Public Sector…………… ……... 117
Unit 4 Budgetary Control in the Public Sector……… …. 125
Unit 5 Transparency and Accountability in the Public Sector…………………………………………... 132
Unit 6 Concept of Transparency and Accountability…. 141

Module 5 Financial Reporting and Auditing In The Public Sector…………………………… 151

Unit 1 Regulatory Framework for Managing Public Finance……………………………………… 151
Unit 2 Financial Reporting……………………………. 161
Unit 3 Analyzing Financial Report and Audit………… 168
Unit 4 Accounting Practice and Financial Management Cycle…………………………….. 176
Unit 5 Financial Misconduct…………………….…… . 185

MODULE 1 FUNDAMENTALS OF PUBLIC FINANCIAL MANAGEMENT

Unit 1 Meaning, Nature, Scope and Objectives of Public Finance

Unit Structure

1.1 Introduction
1.2 Objectives
1.3 Public Finance
 1.3.1 Meaning of Public Finance
 1.3.2 Nature and Scope of Public Finance
 1.3.3 Objectives of Public Finance
1.4 Summary
1.5 References/Further Reading/Web Resourse
1.6 Possible Answers to Self-Assessment Exercise(s) within the content

1.1 Introduction

In this unit, you will be introduced to the concept of public finance, its meaning, nature, scope as well as its objectives. This is to give you a background knowledge of public financial management as well as the philosophy behind public financial management. The comprehension of any concept depends on analysis of its features and this is the reason you are being introduced to them firstly.

1.2 Learning Outcomes

By the end of this unit, you will be able to:

- define of public finance and public financial management
- explain the nature and scope of public financial management
- state objectives of public financial management

1.3 Public Finance

1.3.1 Meaning of Public Finance

Public finance refers to all activities of government in generating and allocating (spending) revenue towards ensuring efficiency of the state and the general well-being of the people. In other words, public finance refers to financial operation of public treasury and its implication. Dalton cited in Benjamin and Martin (2012) submitted that public finance is concerned with income and expenditure measures of public authorities and with the adjustment of one to the other. Public finance is the study of the methods employed by the government to raise revenue and the principle underlying government expenditure. For Taylor (1972), public finance deals with the finances of the public as an organised group under the institution of government such as raising and disbursement of government funds. It is concerned with the public treasury. Carl (1986) sees public finance as the study of funds raised by government to meet the needs of governance.

Ola and Offiong (2008) define public financial management as "the measures put in place to control people's money or funds." You will note that the word 'public' means the people while 'finance' connotes funds or money. The management of public funds is known as public financial management. Ekpung (2001), also defines public financial management as the management of the flow of money or financial resources through an organisation (public), whether it is a company, a school, a bank, or a government agency. The actual flow of money or financial resources as well as claims against money in a judicious way is its concern. Public financial management is a specialised, functional area found under the general classification, public administration and finance.

The traditional concept of finance (providing funds needed by an organisation) has the merit of highlighting the central core of the financial function –the treasury function- which is simply keeping the organisation supplied with enough funds to accomplish its objectives. In the present modern economy, there is increase in complexity, size, technology, inflation, recession and government control with a lot of implications to financial management in many organisations. In public financial management, every decision is based on equity and efficiency back-up by public policy so as to ensure efficient employment of resources. Thus, public financial management deals with judicious use of funds, and also ensures accountability and financial control.

Self-Assessment Exercise 1

What do you understand by public financial management?

1.3.2 Nature and Scope of Public Finance

In a modern economy, finance may be defined as the provision of money at the time it is needed. Every person responsible for finance, whether it be the finance of company (business), household (private) or government (public), is confronted with the prospect during the coming days, months or years of an inflow of receipts on the one hand and an outflow of payments on the other.

The persons in government (administrators of various ranks – mostly accountants and treasurers(Public Financial Managers) are charged with the responsibility of ensuring that the inflows and outflows are so arranged in a way that money is always available to make necessary payments as they arise. Handling of receipts and payments take place evenly and continuously at least to satisfy the constitutional requirements. Where either the receipts or the payments or both occur discontinuously and especially if they occur in relatively large amounts at relatively long intervals, much care and forethought have to be taken to ensure that at any given moment there is money available to make the necessary payments.

Scope of public finance covers all governmental activities relating to revenue generation and expenditure including fiscal and monetary policies. The scope of public finance includes but not limited to:

i. Public Revenue: this refers to the several sources from which the government might derive its income such as taxes, public debts, creation of additional currency etc. it also involves analyses of comparative advantages and disadvantages of various forms of revenue and the underlying principles governing taxation and its effect on the economy.
ii. Public Expenditure: the major tool used by government for implementing economic growth, economic stabilization, citizens' welfare and other policies. Public expenditure shows how government controls the economy and its contribution to the financial flows of the economy including the demand and supply patterns. The theory of public expenditure helps government to build school, hospitals, roads, bridges, provide social amenities to citizens, pay salaries and other remunerations to workers as well as promote stabilization of prices of goods and services in the country.

iii. Financial Management: this relates to public budget, starting from budget preparation, executive approval, legislative enactment, budget implementation, budget authorization including financial audits

iv. Fist Mortem: this relates to the examination and re-appraisal of the budget implementation in order to ascertain the performance of the budget. This would help to know if it was judiciously utilized and the objectives stated in the budget achieved accordingly.

v. Economic Stabilization: this covers all governmental efforts at stabilizing prices of goods and services, promotion of employment opportunities and economic growth in the country. Economic stabilization and growth are very important to any nation's economic policy, hence demands a separate consideration in the scope of public finance.

Self-Assessment Exercise 2

Identify the scope of public finance?

1.3.3 Objectives of Public Finance

Public finance helps the government of any nation to achieve numerous objectives, some of which include:

a. Resource allocation: this involves redistribution of resources from the private sector to the public sector. Government must encourage efficient and maximum utilization of scarce resources through effective resource allocation to the benefits of the society.

b. Economic stability: this objective involves stabilization of the economy, promotion of favourable balance of control of inflationary payments, trends and rate of unemployment including income stability and the prices of goods and services.

c. Equitable distribution of income: Public finance helps to promote egalitarian society, through equitable distribution of income and wealth among citizens and other segments of the society. This objective also include distribution of welfare programme and progressive taxation structure.

d. Economic growth: public finance also encourages increase in the rate of economic growth in the country. This include increase in Gross Domestic Production (GDP), employment opportunities and a sustainable improvement in the living standards of the inhabitants, power generation and infrastructures.

Public financial management however aims to enhance the management of the flows of money or financial resources through government and its agencies for the purpose of government in a modern economy. The

following functions summarize aims of government in a modern economy: provision of essential public services; control of certain sectors of the economy; application of social policy; and that government assumes responsibility for the overall state of the economy.

Self-Assessment Exercise 3

List four objectives of public finance?

1.3.4 Modern Governments' Instruments of Intervention in the Economy

Modern governments intervene in the market economy in other to fine tune it; this is made possible through legislation, regulation, controls and standard legislation. Government intervenes through the provision of public goods and income distribution. The government is concerned with the welfare of its citizenry. Government invests on projects, supposedly, not attractive to private investors, but beneficial to the citizens.

These projects are relatively low in profitability. Instruments for government intervention in the economy include the following.

i. Fiscal policies: these are government policies through which government revenue and expenditures are manipulated.
ii. Monetary policies- government through the Central Bank targets the quantity of money in circulation within the economy, considering the cost (interest) and general credit direction.
iii. Direct control- this comes in the form of rules and regulations involving the passing of laws or executive directives as a supporting tool to enforce implementation of policies.
iv. Income policy- this aims directly at regulating the disposable incomes accruing to earners to meet government macro-economic objectives, ensuring equitability in income and productivity level. These include minimum wage laws etc.
v. Debt management policy- government, normally, incurs internal and external loans for some important reasons. A policy as an instrument of debt management will be in place to avail the team of managers to meet current fiscal obligations.
vi. Exchange rate policy- with international trade, the exchange rate (price of foreign currency) is of value in the economy, as it affects and influences virtually all other prices for the purpose of controlling the economy.

1.4 Summary

Public finance is the study of the methods employed by the government to raise revenue and the principle underlying government expenditure, while public financial management deals with judicious use of funds, and also ensures accountability and financial control. The scope of public financial management covers a vast field of endeavour which encompasses the whole processes of formulating and implementing decisions made on government services, expenditures, taxes, public debt and other revenue which seeks to ensure judicious resource allocation, equitable distribution of income, and economic growth and stability

1.5 References/Further Reading /Web Resources

Benjamin, E. & Martin, N. (2012). *Public finance administration in Nigeria. Cases and issues*. Onitsha: Chambers Books Ltd

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Ogunjimi, S. O. (1997). *Public finance*: *For polytechnics ICAN students.* Bida Nigeria: Lekem Productions.

Ola, R.O.F. & Offiong, O.J. (2008). *Public financial management in Nigeria*. Lagos: AMFITOP Books.

1.6 Possible Answers to Self-Assessment Exercise(s) within the content

What do you understand by public financial management?

Answers to Self-Assessment Exercise 1

Public finance refers to all activities of government in generating and allocating (spending) revenue towards ensuring efficiency of the state and the general well-being of the people. In other words, public finance refers to financial operation of public treasury and its implication on the society. Furthermore, public finance is concerned with income and expenditure measures of public authorities and with the adjustment of one to the other. Public finance is also the study of the methods employed by the government to raise revenue and the principle underlying government expenditure.

Identify the scope of public finance?

Possible Answers to Self-Assessment Exercise 2

The scope of public finance covers all governmental activities relating to revenue generation and expenditure including fiscal and monetary policies. The scope of public finance includes but not limited to:

i. Public Revenue
ii. Public Expenditure
iii. Financial Management
iv. Fist Mortem
v. Economic Stabilization

List four objectives of public finance?

Possible Answers to Self-Assessment Exercise 3

Public finance helps the government to achieve numerous objectives, some of which include:

a. Resource allocation
b. Economic stability
c. Equitable distribution of income
d. Economic growth

UNIT 2 Principles of Public Financial Management

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Principles of Public Financial Management
2.3.1 Basic Functions of Government
2.3.2 Basics of Public Financial Management
2.3.3 Dynamics of Public Financial Management
2.3.4 Public Financial Management System Based on Principles
2.3.5 Normative Principles
2.3.6 Public Sector Accounting
2.3.7 Government Accounting
2.4 Summary
2.5 References/Further Reading
2..6 Possible Answers to Self-Assessment Exercise(s) within the content

2.1 Introduction

In the previous unit, you were acquainted with the meaning and objectives of public finance as well as its scope. The flow and management of funds is the life blood of public administration. No policy regardless of how it is well crafted and designed can achieve set objectives unless it is associated with adequate and effective flow of funds that will make it possible. In this unit, you will be acquainted with the fundamental principles of public finance and its management. This will give you a background knowledge on the essence of public finance in public administration.

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- list the basic functions of government
  state the fundamentals of public financial Management
- identify the dynamics of public financial management
  list the basic principles of the design of public financial management
- identify the basic characteristics of public sector accounting.

2.3 Principles of Public Financial Management

2.3.1 Basic Functions of Government

In the previous unit of this module, we identified functions of government to include among other things: The up-keep of the president, legislature, the judiciary, maintenance of law and order, provision of facilities for defense and diplomatic representation including discharge of international responsibilities. The direct or indirect involvement in enterprises example the postal services, energy, inland waterways, gas and oil etc. It could be through financial assistance or advisory services. This involves revenue and expenditure. Revenue is taxation and its distribution among the community. Expenditure is on social services like education, health etc. The maintenance of a high and stable level of employment is the encouragement of growth in the economy.

2.3.2 Basics of Public Financial Management

From the above enumerated function of government we can identify the subject of public finance to be the acquisition and disposal of resources by the government, be it Federal, State or Local Government. It is about government income and expenditure. It deals with budgets. Budgets are statements about how a government plans to obtain income (income) and the ways a government plans to spend such income during a particular financial year. A budget can be deficit, surplus or balanced.

2.3.3 Dynamics of Public Financial Management

Public Financial Management is a dynamic, living, breathing system with which citizens interact every day. Let us think of an irrigation system, one that gathers rainfall behind large dams and distributes the flow of water through large and small pipes and channels this to many disparate communities, to commercial users, to schools and hospitals, parklands and charities, to businesses and individuals, to seaside areas and deserts. Such a system must be managed and regulated throughout its length, and its consumers must be built according to politically accepted framework. If there is adequate rain falls and the dams and pipes do not leak or burst and if the supply of water is not diverted or stolen before delivery, the system will become a precondition for life growth and even abundance.

That means public administrators as well as citizens are river wardens. They all are sustained by its flow. A dynamic public financial

management strategy must be in place for the project to be executed successfully. In public administration, social factors play a great deal in decision making and one requires guts to be in-charge of public funding. The role of a public financial manager goes beyond "the measures put in place to control the people's money or funds' it requires meticulous handling of funds and follow-up. If this is not done, the funding could be stalled, owing to other interest that still requires political attention.

Lobbyist would rather want the project initiated in a different community or that the members of the committee in charge of the execution of the project will influence the diversion of the project fund to areas that will make the project to become a white elephant, hence, the fund will not follow the projections especially in a developing economy like Nigeria. Sentiments at times over-ride reasoning, hence, a professionally sound public financial manager who is trustworthy, firm and committed to humanity is expected to be able to "weather the storm" of resisting trials and temptations associated with the timely disbursement of fund/accountability and avoid connivance in order to maintain quality assurance.

Self-Assessment Exercise 1

Is public financial management a static affair?

2.3.4 Public Financial Management System based on Principles

At the heart of the design of an effective system of public financial management, are the following principles:

a. **Democratic** consent: Taxation and spending should not be done without the explicit consent of the governed.
b. **Equity**: Government should be equitable, i.e. people should be treated in similar circumstances similarly- in raising and spending taxes.
c. **Transparency**: Government activities in raising and spending funds should be open to public knowledge and scrutiny.
d. **Probity**: There must be scrupulous honesty in dealing with public funds, of which the legislators and administrators are the stewards, not the owners.
e. **Prudence**: These stewards should not take undue risks with public funds.
f. **Accountability**: Those who deal in public funds can and should be regularly called to account for their stewardship through legislative review and audit process.

Self-Assessment Exercise 2

List the principles affecting effective public financial management?

2.3.5 Normative Principles

These normative principles are "should"; but they are often breached in real life. Public financial management can be abused. Democratic consent is lacking when government is conducted in secret. Concerns for equity often yield to favouritism toward areas, or groups (favouritism by a government in the allocation of benefits or resources; legislation that favours the district of a particular legislator by providing for the funding of public works or other projects- such as post office or pipe borne water contract- that will bring economic advantage to the district and political favour for the legislator). Without transparency, probity and prudence, the inherent caution so essential to the management of public funds is thrown to the winds. Governments then may incur substantial losses through risky investments or negligence (Shafriz and Russell, 2005).

2.3.6 Public Sector Accounting

The need for greater attention in developing government accounting or public sector accounting and financial control is now globally awaken. The reason being that government is obviously the largest single business entity and broad sense; it is the pivot of the economy. The pattern of resource allocation determines the level of accountability for economy to be efficient and effective. These objectives can be realised by having a sound financial control system which depends on the status of the accounting system.

2.3.7 Government Accounting

Definition of Government Accounting

Government accounting can be defined as the process of recording, analysing, classifying, summarising, communicating and interpreting financial information about government in aggregate and in details, reflecting all transactions involving the receipt, transfer and disposition of government funds, assets/property and stores.

Objectives of Government Accounting

With the definition of government accounting in mind, you can break down the meaning into objectives as follows:

a. To determine the extent of probity and accountability in the management and disbursement of government resources.
b. To determine propriety of transactions and their conformity with established rules
c. To provide financial information useful for control and co-ordination of activities; determining and forecasting the flows; balance and requirements of short term planning and budgeting for effective allocation of resources and assessment of socio-economic, political conditions of government establishments.

Basis for Government Accounting

You can deduce from the above objective that the basic feature of public or government accounting is established on accountability and probity. It deals with the control and stewardship of receipts, payments and related activities in the public sector. The peculiar nature of social or government accounting transactions make it desirable and indeed mandatory to treat them in accordance with specific but cohesive and standardised measurement theories and rules like budgeting system and applicable procedures, fiscal accounting procedures, nature of source of revenue etc.

The need to get formal approval on estimates of revenue and expenditure before they are collected or incurred, makes budgeting to largely determine the structure of government accounting

The governments-Federal, State and Local- sometimes find it necessary to demarcate and segregate its resources into specific or special purpose compartments – receipts and payments – and the method of accounting adopted in recording and measuring each component is referred to as "fund accounting"

Another peculiarity of government accounting is that it is maintained on cash basis. This ensures stewardship accountability and cash programming. Accordingly, the Balance Sheet (known as Monthly Reconciliation of Accounts, surplus and Deficit Statement of Assets and Liabilities in Government) does not contain information on fixed assets such as buildings. In summary government accounting are based on the following: cash basis, accrual basis, group account into fund Commitment/obligation basis

Self-Assessment Exercise 3

What are the objectives of government accounting?

2.4 Summary

We have discussed the basic functions of government along with the fundamentals of public finance. The dynamics of public financial management and the principles guiding the system to work effectively were considered with a normative view in a contemporary circumstance.

2.5 References/Further Reading /Web Resources

Ogunjimi, S. O. (1997). *Public Finance: For Polytechnics ICAN Students.* Bida Nigeria: Lekem Productions.

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2.6 Possible Answers to Self-Assessment Exercise(s) within the content

Is public financial management a static affair?

Answers to Self-Assessment Exercise 1

Public Financial Management is a dynamic, living, breathing system with which citizens interact every day. A dynamic public financial management strategy must be in place for the project to be executed successfully. In public administration, social factors play a great deal in decision making and one requires guts to be in-charge of public funding. The role of a public financial manager goes beyond "the measures put in place to control the people's money or funds' it requires meticulous handling of funds and follow-up. If this is not done, the funding could be stalled, owing to other interest that still requires political attention.

List the principles affecting effective public financial management?

Answers to Self-Assessment Exercise 2

The following are principles that determine the effectiveness of public financial management:

1. Democratic consent: Taxation and spending should not be done without the explicit consent of the governed.
2. Equity: Government should be equitable, i.e. people should be treated in similar circumstances similarly- in raising and spending taxes.
3. Transparency: Government activities in raising and spending funds should be open to public knowledge and scrutiny.
4. Probity: There must be scrupulous honesty in dealing with public funds, of which the legislators and administrators are the stewards, not the owners.
5. Prudence: These stewards should not take undue risks with public funds.
6. Accountability: Those who deal in public funds can and should be regularly called to account for their stewardship through legislative review and audit process.

What are the objectives of government accounting?

Answers to Self-Assessment Exercise

The objectives of government account are:

1. To determine the extent of probity and accountability in the management and disbursement of government resources
2. To determine propriety of transactions and their conformity with established rules

3. To provide financial information useful for control and co-ordination of activities; determining and forecasting the flows; balance and requirements of short term planning and budgeting for effective allocation of resources and assessment of socio-economic, political conditions of government establishments.

Unit 3: Monetary Policy

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Monetary Policy
    3.3.1 Objectives of Monetary Policy
    3.3.2 Policy Instruments (Measures)
    3.3.3 Monetary Policy Administration in Nigeria
3.4 Summary
3.5 References/Further Reading
3.6 Possible Answers to Self-Assessment Exercise(s) within the content

3.1 Introduction

In this unit, you will be acquainted with monetary policy. Monetary policy is part of the mechanisms used by government in public financial management. It is primarily concerned with discretionary control of money supply by financial institutions (particularly the Central Bank) in other to achieve set economic goals and objectives. With this policy, governments try to control the money supply in order to stabilize the quantity of money in circulation. This helps in checking inflationary trend and position in the economy.

3.2 Learning Outcomes

By the end of this unit, you will be able to:

- define monetary policy
- discuss objectives of monetary policy
- state the instruments of monetary policy.

3.3 Monetary Policy

According to Dwivedi (2005), monetary policy is essentially a programme of action undertaken by the monetary authorities generally the central bank, to control and regulate the supply of money with the public and the flow of credit with a view to achieving predetermined macroeconomic goals.

Monetary policy consists of a government's formal efforts to manage the money in its economy in order to realise specific economic goals. Three basic kinds of monetary policy decisions can be made about:

a. the amount of money in circulation
b. the level of interest rate
c. the functions of credit markets and the banking system.

The combination of these measures is designed to regulate the value, supply and cost of money in an economy, in line with the level of economic activity. Excess supply of money will result in an excess demand for goods and services, prices will rise and balance of payments will deteriorate. On the other hand, inadequate supply of money can lead to stagnation in the economy, hence retard growth and development. Consequently, the central monetary authority would normally attempt to keep the money supply growing at an appropriate rate to ensure sustainable economic growth and to maintain internal and external stability.

Self-Assessment Exercise 1

Define monetary policy?

3.3.1 Objectives of Monetary Policy

The primary objectives of monetary policy are to:

a) Check the rate of inflation
b) Sustain exchange rate stability
c) Promote output and employment growth and
d) Enhance overall efficiency of the economy.

In pursuit of the above objectives, the stance of monetary policy will be non-accommodating and will ensure efficiency in resource allocation to support private sector. Monetary policy is used to influence these ultimate objectives because there is a belief that there is a relationship between the real variables and the monetary variables.

However, this is valid only for a highly monetary economy. If the economy is not highly monetary, then the efficacy of monetary policy is restricted. In a developing economy like Nigeria, where a large proportion of output is subsistence, the level of output would be independent of supply of money. Therefore monetary policy would not be efficacious in determining the output level of the subsistence sector.

Monetary policies are effective only when economies are characterised by well-developed money and financial markets like developed economies of the world. This is where a deliberate change in monetary variable influences the movement of many other variables in the monetary sector

Sef-Assessment Exercise 2

List three (3) objectives of monetary policy in Nigeria?

3.3.3 Policy Instruments (Measures)

The primary instrument of monetary policy is Open Market Operation (OMO), Reserve Requirements, Discount Window Operations and Moral Suasion. The techniques in use are- direct/portfolio control approach and indirect/market intervention. There is a basic difference between the mechanisms of direct and indirect monetary control.

Under the system of direct monetary control, the monetary authority uses some criteria to determine monetary and credit targets and interest rates which are the intermediate targets to attempt to achieve the ultimate objectives of policy. In direct monetary control only the operating variables related to the path of the intermediate variables. The operating variables, particularly the monetary base are managed, while the market is left to determine interest rates and credit allocation. These instruments place restrictions on a particular group of institutions – especially deposit banks – by limiting their freedom to acquire assets and liabilities. This method is employed mainly in developing economies in which the financial infrastructure necessary for operating indirect monetary control is under-developed.

On the other hand, the indirect method is used mainly in developed financial systems. It relies on the power of the monetary authority as a dealer in the financial markets to influence the availability and the rate of return on financial assets, thus affecting both the desire of the public to hold money balances and the willingness of financial agents to accept deposits and lend them to users.

Open Market Operations: This is an indirect monetary policy instrument introduced to influence the level of money supply in the economy. This involves the issuance of short-term instruments such as treasury bills and other securities to the public subscription.

Cash Reserve Requirement: These serve as prudential and liquidity management policy objectives and complement OMO. This is the least amount of reserve a bank must maintain with Central Bank of Nigeria expressed as a ratio of each individual banks total liability. Liquidity

ratio: this refers to the minimum percentage amount of reserve which shall be in form of liquid assets expressed as the banks total deposit liability, promissory notes and certificate of deposits which the banks must keep with the CBN.

Discount Window Operations: these are transactions in the form of short term, overnight loans, collateralised by the borrowing institution's holding of government debt instruments and other eligible first class securities approved by the CBN. Moral Suasion is the CBN regular dialogue with banks and other financial institutions, under the aegis of the Bankers Committee on monetary and financial issues and to encourage enhanced operational efficiency in the banking industry.

3.3.3 Monetary Policy Administration in Nigeria

The Central Bank of Nigeria proposes the monetary policy to be considered by the presidency through a memorandum with the caption-monetary, credit, foreign trade and exchange policy proposals for a particular fiscal year. The memorandum is an input of all the policy departments of the CBN. It considers the prevailing economic conditions, prospects and the policy objectives that appear most appropriate to pursue in the immediate future.

The memorandum is, initially, considered by the committee of governors, the highest management body for the daily administration of the CBN. It is deliberated upon and approved by the board of directors of the CBN and transmitted by the Governor of CBN to the presidency for consideration and approval. The Presidency after reasonable consultation with other tiers and agencies of government takes a decision on which proposals to accept and include them in the budget. The CBN conducts periodic and special examinations of the books of all licensed banks as a monitoring tool. The banks are also required to submit regular returns on their operations to the Central Bank in compliance with the monetary policy circular.

3.4 Summary

In summary, monetary policy is essentially a programme of action undertaken by the monetary authorities generally the central bank, to control and regulate the supply of money with the public and the flow of credit with a view to achieving predetermined macroeconomic goals. The primary objectives of monetary policy are to check the rate of inflation, sustain exchange rate stability, promote output and employment growth and enhance overall efficiency of the economy. The

primary instrument of monetary policy is Open Market Operation (OMO), Reserve Requirements, Discount Window Operations and Moral Suasion. The techniques in use are- direct/portfolio control approach and indirect/market intervention. The Central Bank of Nigeria proposes the monetary policy to be considered by the presidency through a memorandum with the caption- monetary, credit, foreign trade and exchange policy proposals for a particular fiscal year.

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3.6 Possible Answers to Self-Assessment Exercise(s) within the content

Define monetary policy?

Answers to Self-Assessment Exercise 1

Monetary policy is essentially a programme of action undertaken by the monetary authorities generally the central bank, to control and regulate the supply of money with the public and the flow of credit with a view to achieving predetermined macroeconomic goals.
Monetary policy consists of a government's formal efforts to manage the money in its economy in order to realise specific economic goals.

List three (3) objectives of monetary policy in Nigeria?

Answers to Self-Assessment Exercise 2

The primary objectives of monetary policy are to:

a) Check the rate of inflation
b) Sustain exchange rate stability
c) Promote output and employment growth and
d) Enhance overall efficiency of the economy.

Unit 4 Fiscal Policy

Unit Structure

4.1 Introduction
4.2 Learning Outcomes
4.3 Fiscal Policy
 4.3.1 Major Instruments of Fiscal Policy
 4.3.2 Fiscal System and Allocation of Functions in the Economy
4.4 Summary
4.5 References/Further Reading /Web Resources
4.6 Possible Answers to Self-Assessment Exercise(s) within the content

4.1 Introduction

We continue this unit with fiscal policy, the twin of monetary policy. Fiscal policy is the use of government spending and taxation policies to influence the level of economic activity, inflation and economic growth. Fiscal is the expression of taxation, public revenue or public debt. The fiscal year is a 12-month accounting period without regard to a calendar year. The fiscal year for the federal government of Nigeria is from 1st January to 31st December. In this unit, you will learn about the definition of fiscal policy, the objectives and major instruments of fiscal policy and system and allocation of functions of different tiers of government in Nigeria.

4.2 Learning Outcomes

By t the end of this unit, you will be able to:

- define fiscal policy
- state the objectives and major instruments of fiscal policy
- discuss allocation of functions of tiers of government.

4.3 Fiscal Policy

Fiscal policy is the manipulation of government finances by raising or lowering taxes or levels of spending to promote economic stability and growth (Shafritz & Russell 2005). Fiscal policy is the manipulation of

government expenditure and taxation in order to influence economic performance in a particular direction. This role of government sector in economic management is performed through the formulation and implementation of economic policy generally and fiscal policy in particular. It is designed to achieve the objective of price stability, growth, balance of payments equilibrium, full employment, mobilisation of resources and investment.

Self-Assessment Exercise 1

Define fiscal policy?

4.3.1 Objectives of Fiscal Policy

Fiscal policy enables government to obtain revenue through the follow means:

i. Taxation
ii. Price stabilisation
iii. Equity in income distribution
iv. Increase in investment in the economy
v. Maintain a favourable balance of payments
vi. Exchange rate stabilisation

i. Taxation: Fiscal policy through taxation means the reduction of taxes in certain areas of the economy in order to increase disposable income among businessmen, individuals and corporate bodies. Reduction of corporate taxes would be more available for the corporate bodies to expand their business thereby increase employment opportunities. On the other hand, individual consumers who may be affected by tax reduction would now be in a better position to make effective demand for more goods and services produced by the corporate business firms and industries.
ii. Price Stabilisation: Government may use fiscal tool i.e. contractionary fiscal policy to combat inflation and expansionary fiscal policy to combat deflation and unemployment. This approach helps to stabilise prices of goods and services in the economy. In using contractionary fiscal policy, government could increase the taxes of corporate bodies and those of individuals in order to lower the level of disposable income in the hands of these entities. Government could equally reduce its expenditure on chosen special areas of the economy in order to curb aggregate demand in the economy.
iii. Equity in Income Distribution: Fiscal policy through appropriate tax system may be used to reduce the gap between the incomes of the rich and the poor. A tax system which is highly

progressive in nature may likely reduce the consumption and accumulation of wealth of the rich.

iv. Increase in Investment: Fiscal policy can assist in generating revenue to increase investment in viable sectors of the economy if managed effectively. In the process, it helps to accelerate economic growth.

v. Maintain a favourable Balance of Payment: The government may impose taxes in order to reduce imports and encourage exports so as to minimise the balance of payment deficits. In so doing, it could engender a favourable balance of payment in its foreign trade.

Vi. Exchange Rate Stabilisation: Effective fiscal policy properly implemented could lead to exchange rate stability. A stable exchange rate is effective when there is no constant disequilibrium in the nation's balance of payment position.

All these revenue, when obtained, help government in solving socio-economic and political challenges like providing employment, reviving ailing industries and solving national security insurgents etc.

4.3.2 Major Instruments of Fiscal Policy

The major instruments of fiscal policy include:

i. Taxation
ii. Government expenditure and
iii. Borrowing from domestic and external sources to finance budget deficits.

A country may achieve growth of Gross Domestic Product (GDP) without corresponding economic development. The experience in Nigeria as in many other developing countries, have also proved the public sector intervention in an economy can result in failure just as the rationale for government intervention is based on the inherent failure of price mechanism to achieve a stable equilibrium in the market economy.

Self-Assessment Exercise 2

State the objectives of fiscal policy?

4.3.3 Fiscal System and Allocation of Functions in Nigeria's Economy

Nigeria operates a federal system of government hence this has fundamental implications for the fiscal system and economic management of the country. The economic role of the public sector in a federal system like Nigeria is the joint responsibility of the all tiers of government; that is federal, state and local governments. This joint responsibility of local, state and federal governments in performing the fundamental functions of socio-political administration and economic management introduces complications in the fiscal system which must be technically and constitutionally resolved in the light of political factors and pressures that gave birth to the union.

Theoretically, there is an optimum allocation of functions among the tiers of government in a federation such that the fiscal relations would facilitate the achievement of macroeconomic objectives of price stability, full employment, economic growth and balance of payments equilibrium. If the three tiers of government were to provide the functions of stabilisation, income redistribution and resource allocation simultaneously, inefficiency would result (Musgrave& Musgrave, 1973).

The citizens of a country, incidentally, belong to all the tiers of government in a federal system. There is, therefore, intersection of jurisdiction among the tiers of administration. Local government areas intersect the state constituencies, while the states intersect the national boundary of the federal government. State and local governments engage in the performance of the resource allocation functions along with the federal government in accordance with the provisions of the constitution. However, the stabilisation and income redistribution functions are better performed when domiciled in the central government to avoid unintended spillovers. Revenue Mobilisation and Allocation Commission is saddled with the responsibility of sharing the national revenue, in consonance with the provisions of the constitution of the Federal Republic of Nigeria

Self-Assessment Exercise 3

What are major instruments of fiscal policy of government?

4.4 Summary

Fiscal policy is the manipulation of government finances by raising or lowering taxes or levels of spending to promote economic stability and growth. It is designed to achieve the objective of price stability, growth, balance of payments equilibrium, full employment, mobilisation of resources and investment. Fiscal policy uses taxation, government expenditure and borrowings to achieve set economic goals and objectives.

4.5 References/Further Reading /Web Resources

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4.6 Possible Answers to Self-Assessment Exercise(s) within the content

Define fiscal policy?

Answers to Self-Assessment Exercise 1

Fiscal policy is the manipulation of government finances by raising or lowering taxes or levels of spending to promote economic stability and growth. It is designed to achieve the objective of price stability, growth, balance of payments equilibrium, full employment, mobilisation of resources and investment. Fiscal policy uses taxation, government expenditure and borrowings to achieve set economic goals and objectives.

State the objectives of fiscal policy?

Answers to Self-Assessment Exercise 2

Objectives of fiscal policy are:
Fiscal policy enables government to obtain revenue through the follow means:

1. Taxation
2. Price stabilisation
3. Equity in income distribution
4. Increase in investment in the economy
5. Maintain a favourable balance of payments
6. Exchange rate stabilisation

What are major instruments of fiscal policy of government?

Answers to Self-Assessment Exercise 3

The major instruments of fiscal policy include:

1. Taxation
2. Government expenditure and
3. Borrowing from domestic and external sources to finance budget deficits.

MODULE 2 GOVERNMENT ACCOUNTING: PUBLIC REVENUE

Unit 1 Meaning, Objectives and Sources of Public Revenue

Unit Structure

1.1 Introduction
1.2 Learning Outcomes
1.3 Public Revenue
   1.3.1 Meaning of Public Revenue
   1.3.2 Sources of Public Revenue
   1.3.3 Oil Revenue
   1.3.4 Non-oil Revenue
1.4 Summary
1.5 References/Further Reading/ Web Resources
1.6 Possible Answers to Self-Assessment Exercise(s) within the content

1.1 Introduction

Having been acquainted with basics of public financial management in the previous units as a background knowledge to understanding public finance, this unit will take you further by introducing you to government accounting with particular focus on public revenue. Public revenue simply refers to income generated by the public sector from various services rendered. In order words, it could mean a portion of total funds required by government for the purpose of financing activities. The various sources of public revenue are basically categorized into taxes and non-tax revenue. The Constitution of the federal government of Nigeria provides for the generation of revenue through taxation and miscellaneous receipts as the main sources of revenue. In the second part of this unit, our discussions will center on two main sources of government revenue in Nigeria classified as: oil and non-oil although governments have other means of sourcing for fund for financing their spending requirements.

1.2 Learning Outcomes

By the end of this unit, you will be able to:

- define of public revenue
- state the objectives of public revenue
- list the sources of public revenue

1.3 Public Revenue

1.3.1 Meaning of Public Revenue

Public revenue otherwise known as government revenue refers to the income of the government from different sources. It is the revenue of the government finance by means of participating in the distribution of the social products, which is the financial resource for ensuring the government to function. Dalton in his "Principles of Public Finance" mentioned two kinds of public revenue. Public revenue includes income from taxes and goods and services of public enterprises, revenue from administrative activities such as fees, fines etc. and gifts and grants. On the other hand public receipts include all the incomes of the government received from formal sources. The sources of public revenue have been broadly divided into: (A) Tax Revenue (B) Non-Tax Revenue.

1.3.2 Sources of Government Revenue

Public revenue can be defined as income generated by public sector from various services rendered. Revenue is the other arm of the public/government accounts. Income generated by the public sector from various services rendered could mean a portion of total funds required by government for the purpose of financing its activities. We know that government earns money to sustain itself and perform it duties of national building through fiscal measures. The money required by government to perform its duty must be from a source and utilised on recurrent and capital expenditure. In Nigeria, there are two main sources of government revenue-oil and non-oil. This became imperative since exploration of oil became major contributor to the national budget.

Self-Assessment Exercise 1

1. Define public revenue?
2. Mention two main sources of government revenue in Nigeria?

1.3.3 Oil Revenue

This source consists of royalties, petroleum profit, rent, earnings from direct sales of crude oil to domestic market by Nigerian National Petroleum Corporation (NNPC), gas flaring penalties, pipeline licenses etc. Now, you are to note the following salient issues.

i. Since the 1970s oil revenue became the dominant source of government revenue, contributing over 70 per cent of federally-collected revenue.
ii. For most of the 1960s, federally-collected revenue from oil sources accounted for an average of 8 percent of total receipts.
iii. The oil boom of the 1970s propelled the sector to become dominant, accounting for most of the foreign exchange earnings as well as federally-collected revenue.
iv. The contribution of the oil sector to total receipts increased from average of about 46 percent between 1970 and 1973 to about 77 percent between 1974 and 1980. Through-out the 1980s and 1990s, the contribution of the oil sector to total revenue maintained its dominant position and contributed between 70 and 76 percent of the federally-collected revenue (CBN, 2000).
v. With the constitutional powers vested on the federal government to control the exploration of mineral resources, proceeds from the sales of crude oil, petroleum profit tax, rents and royalties etc. are collected by the federal government and paid into the Federated Account for distribution among the three tiers of government. The status quo has remained till today with various legislative adjustments.

1.3.4 Non-oil Revenue

These are Direct and In-direct taxes.

Direct taxes include:

i. Personal income tax.
ii. Company gains tax that is, taxes on profits.
iii. Capital gains tax – taxes on assets held for more than one year.
iv. Death duties- taxes on the property of deceased.
v. Royalties and mining rents, stamp duties, motor vehicle duties

vi. Miscellaneous receipts of the government include loans profit from direct government investment, grants and fines.

Indirect taxes are:

i. Custom duties – imports and exports:
ii. Excise duties – domestic products
iii. Purchase tax – on certain goods at wholesale level
iv. Sales tax – levied and collected either at wholesale or retail level.
v. Value-Added-Tax- VAT. (Replaced sales tax since 1994)

Since independence, federally-collected revenue was largely revenue from non-oil sources, accounting for an average of 92 percent of the total receipts while revenue from the oil sources accounted for the balance. As can be deduced from available records, from the 1970s to this day, the non-oil sector revenue accounted for the balance of about 20 to 30 percent receipts annually, to complement the oil sector receipts which form the mainstay of the sources receipts of Federal Republic of Nigeria. Government also borrows from the public through issuance of bonds and using innovative finance techniques, public-private partnerships, franchise or licensing of private sector providers etc. are also applied where the need arises.

Representation of public revenue

Oil revenue

1. NNPC earning
2. Petroleum profit
3. Tax
4. Royalty

Non-oil revenue

1. Import duties
2. Export duties
3. Excise duties
4. Stamp duties
5. Value-added tax
6. Personal income tax
7. Corporate tax
8. Capital gains tax
9. Capital transfer tax

Independent revenue sources

1. Fines
2. Fees
3. Rates
4. License

5. Income from government investment
6. Public loans

1.3.5 Types of Revenue for each Government Level

Sources Federal Government

The major sources of revenue collected by the Federal Government are listed below.

1. Import, export, excise duties and fees
2. Direct tax- mainly company income tax and petroleum profit tax
3. Licence fees and stamp duties
4. Mining rents and royalties
5. Earnings and sales
6. Rents on government property
7. Reimbursements
8. Revenue from Armed Forces
9. Interest and repayments
10. Miscellaneous

Sources States Government

Sources of revenue for States Government are as follows.

1. Independent revenue
2. Statutory appropriations from the federation account
3. Non-statutory grants
4. Total recurrent revenue less recurrent expenditure
5. Budget surplus or deficit
6. Capital grant from federal government
7. Internal loans
8. External loans
9. Total capital receipts

Sources Federal Government

Sources of revenue for Local Government are as follows.

1. Independent revenue
2. Statutory allocation from the federal government
3. Statutory allocation from the state government
4. Budget surplus
5. Internal loans
6. Capital grants
7. Total capital receipts

Self-Assessment Exercise 2

List the sources of revenue available to the federal government?

1.4 Summary

In this unit, we have identified the sources of government revenue as Oil and Non-oil Revenue. There are other means by which government generate receipts. The introduction of Value Added Tax (VAT) was explained as a sales tax replacement and it has contributed to the growth in revenue since inception.

1.5 References/Further Reading/Web Resources

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1.6 Possible Answers to Self-Assessment Exercise(s) within the content

1. *Define public revenue?*
2. *Mention two main sources of government revenue in Nigeria?*

Answers to Self-Assessment Exercise 1

1. Public revenue otherwise known as government revenue refers to the income of the government from different sources. It is the revenue of the government finance by means of participating in the distribution of the social products, which is the financial resources for ensuring the government to function. Public revenue includes income from taxes and goods and services of public enterprises, revenue from administrative activities such as fees, fines etc. and gifts and grants. On the other hand public receipts include all the incomes of the government received from formal sources.

2. The two sources of public revenue are broadly divided into:
a. Tax Revenue
b. Non-Tax Revenue.

List the sources of revenue available to the federal government?

Answers to Self-Assessment Exercise 2

The major sources of revenue available to the federal government are:
1. Import, export, excise duties and fees
2. Direct tax- mainly company income tax and petroleum profit tax
3. License fees and stamp duties
4. Mining rents and royalties
5. Earnings and sales
6. Rents on government property
7. Reimbursements
8. Revenue from Armed Forces
9. Interest and repayments
10. Miscellaneous

Unit 2 Taxation

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Taxation
 2.3.1 Tax as Source of Revenue to Government
 2.2.2 Types of Taxes
 2.3.3 Canons or Principles of Taxation
 2.3.4 Incidence of Tax
 2.3.5 Effect of Tax on Economic Amenities-Purpose of Taxation
 2.3.6 Tax Evasion and Tax Avoidance
2.4 Summary
2.5 References/Further Reading /Web Resources
2.6 Possible Answers to Self-Assessment Exercise(s) within the content

2.1 Introduction

In the last unit, you were introduced to public revenue, this unit will take you through taxation as a source of revenue in Nigeria; it will also focus on types and the purpose, incidence and canons of taxation. Revenue generation is the base of financial management in the public sector; and tax is a reliable and legitimate means of obtaining revenue by any government. You will be shown taxation from the basic point of view.

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- define taxation
- identify types, purposes and canon of tax in Nigeria
- list the incidence and effects of taxation in economic amenities
- explain tax evasion.

2.3 Taxation

2.3.1 Tax as Source of Revenue to Government

Taxation is defined as a compulsory payment or levy imposed via legislation by the government of a country on the income of the residents. The Joint Tax Board defines taxation as "the legal demand made by the Federal Government or the State Government for its citizens to pay money on income, goods and services". Public financial management involves how funds are generated, allocated and managed by the government (Ola and Offiong, 2008). Nigerian income depends so much on the incidence of tax, and different types of taxes are imposed on individuals, businesses and corporate bodies.

Government also borrows funds from different available sources in order to meet its general responsibilities. The oil and gas sector, for sometimes now, has contributed greatly to the revenue base of the country as it has helped in the long run to solve social and political problems. It has also helped the government in addressing a lot of issues concerning the populace (despite Nigerian increasing population) the attitude of people towards payment of tax has been in the low level as discussed later in this unit under tax evasion and avoidance.

The attitude of the people has negatively affected the incidence of tax and those who find themselves in the 'corridor' of power have not helped matters because they do not pay their taxes, either. In view of these, the reliance of government on taxes for public expenditure has been relatively low hence the dependence on revenue from oil and gas sector. This has affected the numerous public projects embarked upon by different tiers of government. Sense of responsibility by citizens as tax payers has been neglected and even corporate bodies have also joined this 'wagon'. Invariably, the standard of living of the people has been affected because of shortage of revenue through taxation.

Self-Assessment Exercise 1

Define taxation?

2.3.2 Types of Taxes

Below are some major types of taxes:

Direct taxes include the following

a. Personal income tax
b. Company gains tax that is, taxes on profits
c. Capital gains tax – taxes on assets held for more than one year
d. Death duties- taxes on the property of deceased
e. Royalties and mining rents, stamp duties, motor vehicle duties
f. Miscellaneous receipts of the government include loans profit from direct government investment, grants and fines.

Direct tax- if the payer bears the burden of the tax and cannot shift the burden to any other person. These taxes are based on income or receipts and their incidences fall directly on the payer. It can be used as a fiscal instrument to adjust disposable income of the citizens and redistribute income through different forms of direct taxes. Different forms of direct taxes are progressive, regressive and neutral (proportional).

Progressive tax- the higher the tax base, the higher the rate will be. The rate of taxation graduates progressively as income increases. Its major features include the following.

a. Reduces inequality of income
b. Increases aggregate demand
c. Is non-inflationary
d. Yields more revenue to government
e. May induce disincentive as it is exorbitant in additional income of tax payers.
f. Adopted in real life situation.

Regressive tax- the tax rate diminishes as income level/tax base increases. This is the opposite of progressive tax.
Features-
a. Low rate of tax is paid at high levels of income
b. Creates incentives to efforts
c. Widens inequality of income in the economy
d. Decreases aggregate demand
e. Only rich saves extra income
f. The rest discouraged in investment in the economy
g. Not applied in real life

Neutral (progressive) tax- this takes no cognizance of the economic situation of the tax payer and the tax is proportional to the tax base/income at a constant rate.
Features-

a. Is impartial
b. Is not disincentive to efforts
c. It does not provide incentives
d. It is insensitive to economic situation
e. It is against social equity

Self-Assessment Exercise 2

Identify types of taxes in Nigeria?

Indirect tax- the payer shifts the burden to someone else. This depend on the elasticity or otherwise of the demand for the goods and services and the object of the tax.
Tax on expenditure
It is possible to shift tax incidence (partly or wholly) to someone else.

Indirect taxes are listed below.

a. Custom duties – imports and exports
b. Excise duties – domestic products
c. Purchase tax – on certain goods at wholesale level
d. Sales tax – levied and collected either at wholesale or retail level
e. Value-Added-Tax- VAT (replaced sales tax since 1994).

Tax base

Taxes are based on something. In Nigeria tax system it is based on three main bases namely- income, capital gains and consumption.

1. Income tax

This is the regime of tax levied on the financial income of individuals, companies and corporate entities. Diverse income tax regime exists in different degrees of tax incidence – progressive, regressive or proportional which had earlier been discussed above. Income tax is levied on the income or profit of the companies as corporate tax, corporate income tax or income tax. It is based on net income – the difference between gross earnings and expenses and/or any other write offs. When it involves an individual, the income tax is often assessed on the total income less deductions or exemptions statutorily permitted by the law and regulations of tax in a given country. Types of payments that are taxable include: personal earnings, capital gains and business income.

2. **Capital gains tax**

This is tax levied on the gains or profits realised from sales of assets. The most common capital gains tax around the world are charged on the sale of stocks (shares), bonds, precious metal, real estate, mutual trust shares, interest on bank deposits, etc. The capital gains take into account the cost of investment and the proceeds realised from the sales of such assets. There are exemptions like agricultural land, primary residential buildings, etc.

3. **Consumption tax**

Sales taxes are also known as consumption tax, charged at the point of purchase for certain types of goods and services. The percentage of this tax is set by the government (authorised tax authority – Federal Inland Revenue Service and backed up by their States counterpart). There are exemptions in terms of goods and services which are not subject to sales tax. This sales tax can be included in the sales price of the good or service. By its nature and application, sales tax is considered to be fair and has a high compliance rate which makes it difficult to avoid. The retail sales tax (a version of sales tax) is, usually, affected by charging the tax only on the ultimate consumer as compared to the gross receipt tax levied on the intermediate businesses in production or distribution line.

Value Added Tax (VAT)

The value added tax (VAT) is also known as goods and services tax, and is a tax on exchanges. It is levied on the added value that results from each exchange through the whole gamut of the production of goods to the final consumer. It is an indirect tax because the tax is collected from someone other than the person who actually bears the cost of the tax; the seller of the product or service pays the tax rather than the consumer who benefit the utility of the commodity. VAT is the acronym for valued added tax. This tax which is in other words called consumption tax can be defined as the amount charged by the government for every goods or services purchased from time to time. This means it can only be paid when there is consumption of goods or services (It forms part of the price paid for the good or service).

This was introduced by the federal government in 1994 to replace sales tax. Initially, the federal government received only 20 percent of the VAT proceeds to cover administrative cost of collection while state and local governments received 50 and 30 percent respectively.

VAT was designed broadly to be levied on imported goods, locally-manufactured goods, hotel service, bank transaction etc. and to be federally-collected. A uniform rate of 5 percent was fixed on all affected items while VAT proceeds are shared among the three tiers of government at an agreed proportion.

Characteristics of value added tax

These are spelt out as follows.

a. It is a consumption tax- it can be paid when there is consumption of the good or service.
b. Its incidence is borne by the final consumer.
c. It is multi-stage tax. That is, as additional value is created at each stage of production the tax is paid by the consumer of the product at that stage. The total payments make up the consumer's price of the product.

The following goods and services are exempted from VAT

1. Medical and pharmaceutical items
2. Basic food items (food stuffs etc.)
3. Books and educational materials
4. Agricultural equipments, product and veterinary medicine
5. Fertilizer/ agricultural Chemicals
6. Baby product
7. Exported goods.

Services exempted are:

a. Medical services
b. Services by development finance institutions – like Agricultural, Cooperative and rural Development, Mortgage Banking institutions.
c. Plays and entertainments by educational institutions (part of learning)
d. Religious services
e. Exported services

VAT administration

The tax authority for VAT is the Federal Inland Revenue Service (FIRS)- with head office centrally located at Abuja, and has Zonal offices and local offices throughout the federation. The VAT directorate works in close cooperation with the Nigerian Custom's Services and the State Internal Revenue Service.

VAT registration-procedure

Steps involve in VAT registration

1. identification of VAT-able person and address
2. Prepare a comprehensive list of all suppliers of goods and services
3. Form 001 is completed by each VAT-able person
4. VAT identification number is given
5. VAT certificate issued to the VAT payer
6. VAT-able person registers for VAT within six months of the business

A penalty of N10,000 is given in the first month of failure and N5000 for each subsequent month if failure continues.

Government ministries, statutory agencies have to register for VAT as FIRS agents, for the purpose of collecting VAT and paying to the appropriate VAT office.

Non-resident companies doing business in Nigeria shall register for VAT with FIRS, but the person with whom it has a subsisting contract shall act as agent of FIRS in collecting the VAT and paying over to the VAT office. This formula varied in 1996, 1998, and 1999 as shown on the table 2.1 b below. You should note that revenue from VAT recorded a substantial growth since its inception in 1994, increasing from N726.8 million in 1994 (which represented 3.6 percent of totally-collected revenue in that year), to N36,867.7 million or 8.0 per cent of the total revenue in 1998.

Table 2:1 VAT Revenue Allocation Formula (%)

S/N	Governments	1994	1995	1996	1997	1998	1999
1.	Federal	20.0	50.0	35.0	35.0	25.0	15.0
2.	State and FCT	50.0	30.0	40.0	40.0	45.0	50.0
3.	Local	30.0	20.0	25.0	25.0	30.0	35.0
	Total	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**

Source: CBN Publication (2000). Approved Budgets of the Government of the Federal Republic of Nigeria

2.3.3 Cannon or Principles of Taxation

Here, let us consider the following.

1. **Equity**- equality of sacrifice; this principle states that the subjects of every state should contribute towards the support of the government in proportion to the revenue which they respectively enjoy under the protection of the government.
2. **Certainty**- by this principle tax paid by individuals must be certain with respect to amount paid, time of payment and manner of payment.
3. **Convenience**- the principle of convenience states that the time of payment and the manner of payment should be suitable to the contributor.
4. **Economy**- the administrative cost of collecting the tax should not be higher than revenue realised, but should be less enough to leave surplus revenue.
5. **Simplicity**- the tax system should be coherent, straight forward and clear to the tax payers and accepted by the public.
6. **Flexibility**- the tax system should be such that it should respond to changes.
7. **Impartiality**- all similar income earners should pay the same amount of tax.
8. **Productivity**/fiscal adequacy- the origin of taxation is to raise revenue for the expenditure of government, hence should be able to cover government's expenditure.

2.3.4 Incidence of a Tax

The incidence of a tax is upon the person who pays it. In the case of income tax, the incidence is always on the person receiving the income because income tax cannot be shifted to someone else. A person's income is always being reduced by the full amount of the tax. In the case of an indirect tax, one cannot be sure in advance whether the incidence of the tax will be on the buyer or on the seller of the commodity or whether it will be on them. The effect will depend on the elasticity of demand.

Illustration

Suppose a specific tax of N2 is imposed on a commodity previously priced N10. If the price is immediately raised to N12, the incident of the tax is clearly on the purchaser. For now, he has to pay N2 more for it. That is, the old price plus the full amount of the tax. If the demand for the commodity is perfectly inelastic, the price will rise to N12 and the full incidence of the tax will then be on the buyer as shown graphically in figure 2.1 below

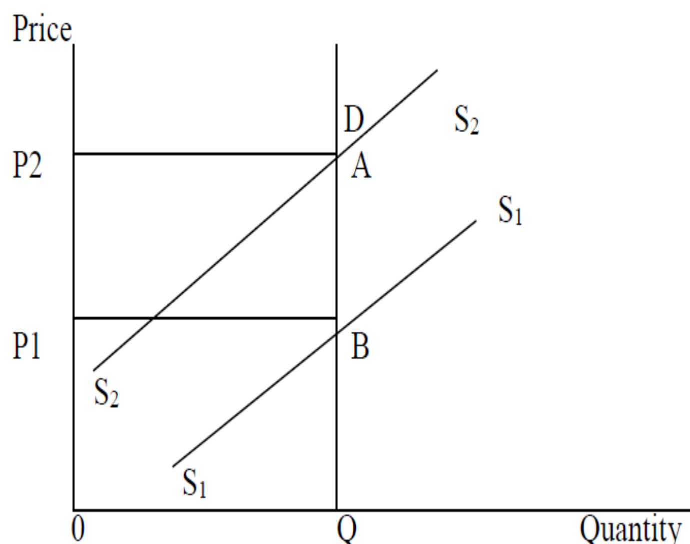

Figure 2.1: Incidence of Tax – Inelastic Demand

Tax AB increases the cost of production by that amount and so the condition of supply moved from S1 to S2. The demand curve being perfectly inelastic, the price rises from Op1 to Op2, this increase being exactly equal to the amount of the tax AB. If the demand for the commodity is perfectly elastic, the incidence of the tax will be entirely on the seller, since at any price above N10 sales drops to zero as shown in figure 2.2 b. Again tax AB increases the cost of production by the same amount, but because demand is perfectly elastic, price OP remains the same.

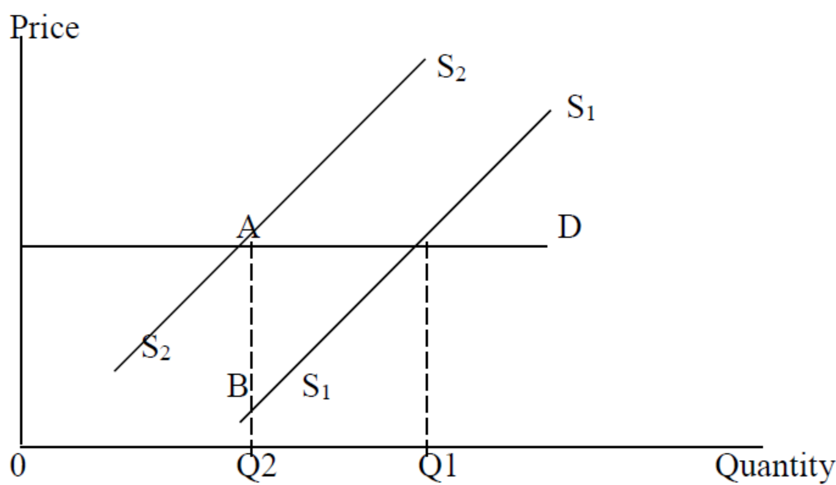

Figure 2.2: Incidence of Tax – Elastic Demand

The above are extreme cases of incidence. If demand is moderately elastic, the quantity demanded will fall off due to increase in price. To

keep sales up, the price may be reduced to may be N11. In this case, buyer and seller pay part of the tax each so that the incidence of the tax is partly on the buyer and the seller as shown in the figure 2.3

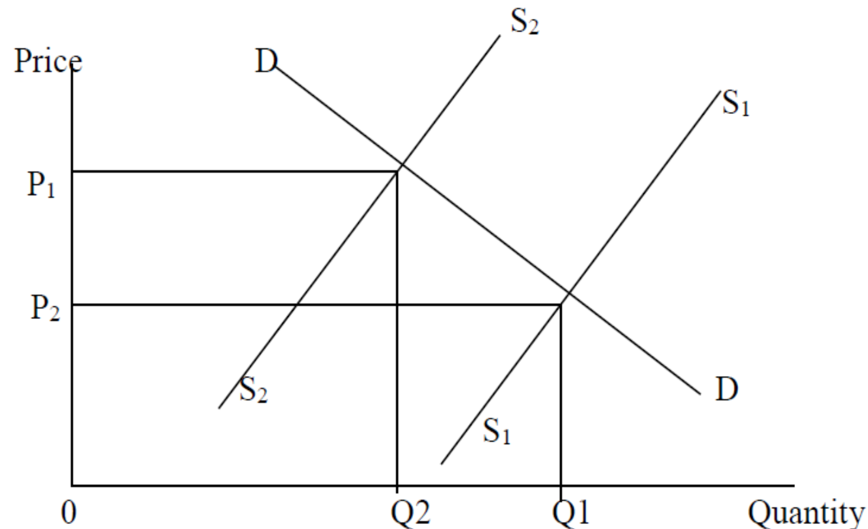

Figure 2.3: Incidence of Tax – Moderately Elastic Demand

From the foregone discussions and graphical presentation, it stands to reason that the commodities most suitable for taxation (when thinking of maximising revenue) will be those for which demand is inelastic. Unfortunately, many of the commodities for which there is a fairly inelastic demand are common necessaries of life, whereas for some luxury goods demand moves towards more elastic. Semi-luxuries like alcoholic drink have to bear an increasing burden of taxation because experience has indicated the demand for them to be fairly inelastic.

2.3.5 Effect of Tax on Economic Amenities- Purpose of Taxation

The general tax administration and practicing guide for professionals proffers the following reasons for imposition of taxes:

1. To maintain general administration, defence, law & order, and social services provided by government
2. To reduce income and wealth in order check inequality
3. To control consumption of goods and services considered non-essential and harmful
4. To check inflation by reduce the volume of purchasing power
5. To service national debt and to provide retirement benefit etc.
6. To provide subsidies in favour of preferred sectors of the economy-for example, agro-allied industries
7. To implement government policies since budget is now an adjunct to monetary policy

8. To serve as a dependable fiscal tool to plan and direct the economy, by shaping the growth and development of the country.

Self-Assessment Exercise 3

List five (5) principles of Taxation?

2.3.6 Tax Evasion and Tax avoidance

Tax evasion is the manipulation of forms when rendering returns and claims as regard the taxpayer's income status and the accompanying responsibilities. This is a direct violation of the law and it involves a fraudulent or deceitful effort by the tax payer to escape legally stated obligation. It is a criminal offence as it involves illegal means of reducing the tax payable by making false returns or by deliberate omission from the return of some source of income like declaring lower income or refusing to pay altogether.

Tax avoidance

This is where the individual takes advantage of the loopholes in tax regulation and manipulate his/her economic situation accordingly to pay low tax. It occurs when a tax payer takes a perfectly legal course to lower the amount he has to pay in taxes like the taking a life assurance policy, deductible from the total amount subjected to tax or claiming the existence of an aged mother or father- where there not which statutorily attract some deductions from the taxed sum and declaring that he has children whereas he/she has none

2.4 Summary

In summary, we have discussed the definition and historical perspective in Nigeria, highlighting types of tax, canons/incidence of tax, effect of tax on economic amenities, tax evasion and avoidance. Tax is compulsory levy on the residents of an economy by the government of that economy. In this unit, we will see tax as a compulsory payment which is enforced by law for adults within the work-force age to pay and the non-payment leads to penalties. The other fact is the only government can levy tax as a means of revenue.

2.5 References/Further Reading /Web Resources

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2.6 Possible Answers to Self-Assessment Exercise(s) within the content

Define Taxation?

Answers to Self-Assessment Exercise 1

Taxation is defined as a compulsory payment or levy imposed via legislation by the government of a country on the income of the residents. The Joint Tax Board defines taxation as “the legal demand made by the Federal Government or the State Government for its citizens to pay money on income, goods and services”.

Identify the types of taxes in Nigeria?

Answers to Self-Assessment Exercise 2

The major types of taxes in Nigeria are:
1. Direct taxes which include:
2. Personal income tax
3. Company gains tax that is, taxes on profits
4. Capital gains tax – taxes on assets held for more than one year
5. Death duties- taxes on the property of deceased
6. Royalties and mining rents, stamp duties, motor vehicle duties
7. Miscellaneous receipts of the government include loans profit from direct government investment, grants and fines.
8. Indirect taxes include:
9. Custom duties – imports and exports
10. Excise duties – domestic products
11. Purchase tax – on certain goods at wholesale level
12. Sales tax – levied and collected either at wholesale or retail level
13. Value-Added-Tax- VAT (replaced sales tax since 1994).

List five (5) principles of taxation?

Possible Answers to Self-Assessment Exercise 3

1. Equity
2. Certainty
3. Convenience
4. Economy
5. Simplicity
6. Flexibility
7. Impartiality

Unit 3 Revenue Generation and Management in Nigeria

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Revenue Generation and Management in Nigeria
    3.3.1 Federal Board of Inland Revenue
    3.3.2 State Board of Internal Revenue
    3.3.3 Joint Tax Board
3.4 Summary
3.5 References/Further Reading/Web Resources
3.6 Possible Answers to Self-Assessment Exercise(s) within the content

3.1 Introduction

Having discussed taxation as the major source of revenue for government in the last unit, this unit introduces you to the agencies and government parastatals saddled with the responsibilities of revenue generation and management in Nigeria. This is to acquaint you with the composition, powers and responsibilities of these agencies in revenue generation and management. The unit will specifically focus on the Federal Board of Inland Revenue, Board of Internal Revenue and the Joint Tax Board.

3.2 Learning Outcomes

By the end if this unit, you will be able to:

- state role of the Board of Inland Revenue in revenue management
- state role of the Board of Internal Revenue in revenue management
- explain role of the Joint Tax Board in revenue management

3.3 Revenue Generation and Management in Nigeria

3.3.1 Federal Inland Revenue Service (FIRS)

The Federal Inland Revenue Service popularly known as FIRS is the federal tax authority and was created by the Companies Income Tax Act (CITA) of 1979 and now under the FIRS establishment Act, 2007. The body responsible for its management is the Federal Inland Revenue Service Board (FIRSB)

Composition of the Board (FIRSB)

The Act stipulates the membership of the FIRSB as follows:

1 There is established for the Service of a Board to be known as the Federal Inland Revenue Service Board which shall have overall supervision of the Service as specified under this Act.

2 The Board shall consist of:

a The Executive Chairman of the Service who shall be experienced in taxation as Chairman of Service to be appointed by the President and subject to the confirmation of the Senate;

b Six members with relevant qualifications and expertise who shall be appointed by the President to represent each of the six-geo-political zones;

c A representative of the Attorney-General of the Federation

d The Governor of the central Bank of Nigeria or his representative.

e A representative of the Minister of Finance not below the rank of a Director;

f The Chairman of the Revenue Mobilisation, allocation and Fiscal Commission or his representative who shall be any of the commissioners representing the 36 states of the Federation;

g The Group Managing Director of the Nigerian National Petroleum Corporation or his representative who shall not be below the rank of a Group Executive Director of the Corporation or its equivalent;

h The Comptroller-General of the Corporate Affairs Commission or his representative not below the rank of a Director; and

i The Chief Executive Officer of the National Planning Commission or his representative not below the rank of a Director;

3 The members of the Board, other than the Executive Chairman, shall be part-time members.

Powers and Duties of FIRSB

FIRSB has the powers to assess and collect the following taxes:

1 The Board shall

a Provide the general guidelines relating to the functions of the Service;

b Manage and superintend the policies of the Service on matters relating to the administration of the revenue, assessment, collection and accounting system under this Act or any enactment or law;

c Review and approve the strategic plans of the Service;

d Employ and determine the terms and conditions of service including disciplinary measures of the employees of the Service;

e Stipulate remuneration, allowances, benefits and pensions of staff and employees in consultation with the National Salaries, Income and Wages Commission; and

f Do such other things in its opinion that are necessary to ensure the efficient performance of the functions of the Service under this Act.

Technical Committee of the FIRSB

This is also a creation of the Companies Income Tax Amendment Act, 2007 as amended.
It has the following as members;

i. Executive Chairman who is also the chairman of the service
ii. Directors and heads of department of the service
iii. The legal adviser of the service
iv. The secretary of the Board

The committee has power to co-opt additional member(s) as may be required in the discharge of its duties. It has the following functions to carry out:

i. To consider tax matters requiring professional and technical expertise and make recommendations to the Board.
ii. To advise the Board on its powers and duties
iii. To carry out any other duty assigned to it by the Board

3.3.2 State Inland Revenue Service Board (SIRSB)

The State Internal Revenue Service was established by the Personal Income Tax Decree of 1993 as the state tax authority. The operational arm of the board is the state internal revenue service board. The PITD (1993) section 85A (1) provide a uniform composition for the boards in all the states of the federation. The composition is follows:

a. The executive head of internal revenue service who shall be designated as the chairman of the board. He shall be a person experienced in tax matters and be appointed by the state government from within the state service.
b. Three persons nominated by the commissioner of finance of the state on their personal merits.
c. All the directors and head of the state internal revenue service
d. A director from the state ministry of finance
e. legal adviser to the board
f. The secretary to the board who shall be an ex-officio member appointed by the board from within SIRSB.

Functions of the Board (SIRSB)

a. Ensuring the effectiveness and optimum collected of all taxes and penalties due to the government under the relevant laws.
b. Doing all such things that may be deemed necessary and expedient for the assessment and collection of the tax and shall account for all amounts so collected in a manner to be prescribed by the commissioner.
c. Making recommendations, where appropriate to the joint tax board on tax policies, tax reforms, tax legislation, tax treaties and exemption as may be required from time to time.
d. Generally controlling the management of the service on matters of policy subject to the provisions of the law setting up the service.
e. Appointing, promoting, transferring and imposing discipline on employees of the state service.

Technical Committee of SIRSB

The technical committee of the board of the State Internal Revenue was also established by the Personal Income Tax Decree (1993). It comprises of the following as members:

i. The Chairman of the State Board of Internal Revenue who is also the chairman of the technical committee.
ii. All the directors of the state internal revenue service
iii. The legal adviser to the state board
iv. The secretary to the technical committee.

Functions of the State Technical Committee SIRS

i. To advise the State Board on matters that requires professional and technical expertise
ii. To carry out any other duty assigned to it by the State Board

3.3.3 Joint Tax Board (JTB)

The Joint Tax Board was established by sec. 85 of PIT as amended. Its function include among things, mediation between tax authorities of the states and the federation in case of tax disputes. The composition of the board as provided by the Personal Income Tax Decree of 1993 is as follows:

i. The Chairman of the Federal Inland Revenue Service who is also the Chairman of the Joint Tax Board.
ii. One member from each state of the Federation, being a person experienced in tax matters nominated by the commissioner of finance.
iii. The secretary to the board who shall be an officer experienced in tax matters, appointed by the federal civil service commissioner, though not a member, but he is responsible for keeping records of the board's proceedings and performing other administrative duties.
iv. The legal adviser of the Federal Inland Revenue Service Board is to be in attendance at the board's meeting and is to be the legal adviser to the board.

Power and Duties of JTB

The personal Income Tax Decree of 1993 stipulates the powers and duties of the Joint Tax Board as follows:

i. To exercise the powers or duties conferred on it by express provision of this decree, and any other powers, and duties arising under this decree which may be agreed by the government of each territory to be exercised by the board.
ii. To exercise powers and perform duties conferred on it by any enactment of the Federal Government imposing tax on the

income and profit, of companies, or which may be agreed by the Federal Inland Revenue service Board.

iii. To advise the federal government requests, in respect of double taxation arrangement concluded or under consideration with any other country, and in respect of rates of capital allowances and other taxation matters having effect throughout Nigeria and in respect of any proposed amendment to this decree.

iv. To use its best endeavours to promote uniformity both in the application of tax laws and in the incidence of tax on individuals throughout Nigeria.

vi. Impose its decision on matters of procedure and interpretation of this decree on any state for purpose of conforming to agreed procedure or interpretation.

vii. Processing for approval decisions on provident funds schemes are to be recognized as tax allowance deductions.

viii. Resolving any dispute in determination of residence between taxpayers and a tax authority.

ix. To exercise any other powers or duties arising under the decree which may be agreed to by government of each state.

From the above powers and duties it could be seen that the JTB harmonises tax administration in the country.

State Joint Revenue Committee (SJRC)

This is established for each state of the federation. It shall comprise:

a. The Chairman of the State Internal Revenue Service as the Chairman
b. The Chairman of the Local Government Revenue Committees
c. A representative of the Bureau on Local Government affairs not below the rank of a director.
d. A representative of the revenue mobilization allocation and fiscal commission, as an observer.
e. The state sector commander of the Federal Road Safety Commission, as an observer.
f. The legal adviser of the State Internal Revenue Service
g. The secretary of the committee who shall be a staff of the State Internal Revenue

Functions of SJRC

The following are the functions of SJRC

i. Implementing decisions of the Joint Tax Board
ii. To advise the Joint Tax Board and the State and Local Government on revenue matters.
iii. Harmonise tax administration in the state.
iv. Enlighten members of the public generally on state and local government revenue
v. Carry out such other functions as may be assigned to it by the Joint Tax Board.

3.3.4 Local Government Revenue Committee (LGRC)

The local government revenue committee is the local government tax authority. The committee was established by the provision of sec. 85 of Personal Income Tax Decree of 1993. The committee is empowered to collect taxes at the local government level. The taxes to be collected by the local government revenue committee are listed in appendix one of the decree. The compositions of the governing body of the revenue committee are as follows:

a. The Chairman who is to the supervisor of finance
b. Three local government councilors
c. Two persons to be nominated by the chairman of the local government. Those to be nominated must be experienced in revenue matters.

Functions of LGRC

The following are the functions of LGRC:

i. It shall be responsible for the assessment and allocation of all taxes, fines and rates under its jurisdiction and shall account for all amounts so collected in a manner to be prescribed by the chairman of the local government.
ii. It shall be autonomous of the local government treasury and be responsible for the day to day administration of the department, which form its operational arm.
iii. Advice the local government on tax related matters.

Self-Assessment Exercise

List the relevant tax authorities in Nigeria, their compositions, power/duties as well as functions?

3.4 Summary

The unit has drawn attention to the historical background of taxation as well as the tax instruments or relevant tax authorities in Nigeria. Specifically, the following aspects have been dealt with relevant tax authorities as well as their compositions, functions, powers and duties

3.5 References/Further Reading /Web Resources

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3.6 Possible Answers to Self-Assessment Exercise(s) within the content

List the relevant tax authorities in Nigeria, their compositions, power/duties as well as functions?

Possible Answers to Self-Assessment Exercise

Federal Inland Revenue Service (FIRS)
The Federal Board of Inland Revenue is the body responsible for its generation and management of revenue at the federal level. FIRS is the federal tax authority and was created by the Companies Income Tax Act (CITA) of 1979 and now under the FIRS establishment Act, 2007. FIRSB has the powers to assess and collect the taxes and provide the general guidelines relating to tax administration

State Inland Revenue Service Board (SIRSB)
The State Internal Revenue Service was established by the Personal Income Tax Decree of 1993 as the state tax authority. The function of the Board is to ensure effectiveness and optimum collection of all taxes and imposition of penalties in line with relevant government laws. It also make recommendations, where appropriate to the joint tax board on tax policies, tax reforms, tax legislation, tax treaties and exemption as may be required from time to time.

Joint Tax Board (JTB)
The Joint Tax Board was established by sec. 85 of PIT as amended. Its function include among things, mediation between tax authorities of the states and the federation in case of tax disputes.

Unit 4 Fiscal Federalism and Resource Allocation in Nigeria

Unit Structure

4.1 Introduction
4.2 Learning Outcomes
4.3 Fiscal Federalism and Resource Allocation in Nigeria
4.3.1 Fiscal Operations of the Federal Government
4.3.2 Distribution of Revenue
4.3.3 Revenue Allocation
4.3.4 National Revenue Mobilisation Allocation and Fiscal Commission (NRMAFC)
4.3.5 Structure for Revenue Allocation from the Federation Account
4.3.6 Federally-Collected Revenue
4.3.7 Value-Added-Tax (VAT)
4.4 Summary
4.5 References/Further Reading
4.6 Possible Answers to Self-Assessment Exercise(s) within the content

4.1 Introduction

In this unit, we will see the adoption of a federal system of political administration with fundamental implications for the fiscal system and economic management of a country through revenue allocation formula.

4.2 Learning Outcomes

Byt the end of this unit, you will be able to:

- describe the distribution of revenue via revenue allocation
- identify the priority accorded each tier of government
- explain Value-Added Tax.

4.3 Fiscal Federalism and Resource Allocation in Nigeria

4.3.1 Fiscal Operations of the Federal Government

As could be sited in Module 1, Unit 3: Fiscal Policy; section 3 subsection 4:

a. Nigeria is a federal system of political administration with fundamental implications for the fiscal system and economic management of the country.
b. The economic role of the public sector in a federal system is the joint responsibility of the multi-levels of government with joint responsibility of local, state and federal governments in performing the fundamental functions of socio-political administration and economic management. Complications in the fiscal system are technically and constitutionally handled and resolved in the light of political factors and pressures that gave birth to the union.

The process of economic transformation and development calls for the collaboration and participation of many interest groups in an economy such as household, firms, public and private sectors etc. The role played by government or public sector in achieving desired changes in the structure of the economy is unique. This uniqueness of the government sector is formed from the fact that apart from being the element of the economy, the government sector plays a decisive role in achieving macroeconomic objectives of stability growth and development through a package of economic policy measures and legal provisions.

4.3.2 Distribution of Revenue

The distribution of revenue from the Federation Accounts is done at two levels:

1. between federal, state and local governments
2. intra-states and local governments.

The formula and principles of revenue distribution have always been subjects of intense debate with the formation of ad-hoc fiscal review commission without satisfaction.

4.3.3 Revenue Allocation

The use of Revenue Allocation Formula for sharing Federation Account revenue among the tiers of government in Nigeria originated from the

colonial administration and the revenue allocation was based on the prevailing political structure then. As the country became independent, the structure changed and the review of revenue formula became necessary. Revenue Allocation Commissions were appointed at ad hoc level according to Binns (1964), Dina (1968), Aboyade (1977) and Okigbo (1980).

4.3.4 National Revenue Mobilisation Allocation and Fiscal Commission (NRMAFC)

These ad hoc Commissions could not come out with a lasting solution; there became need for a permanent body that would regularly review the major sources for revenue and advice on the necessary changes in the revenue allocation formula. In 1989, the Federal Government established it under the Presidency, to find enduring solutions to problems of revenue Mobilisation and adequate allocation to the three tiers of government.

4.3.5 Structure for Revenue Allocation from the Federation Account

The allocation principles of revenue sharing formula that are in use at the inception of the present democratic dispensation are: Population, Equality of States, Internal Revenue Generation, Land mass, Terrain, Population density and Derivation. These principles are expressed in the Nigeria's 1999 Constitution under Section 162 (2), which provides that "in any approved formula, derivation accruing to the area which is home to natural resources being exploited for foreign exchange earnings, takes a magnitude of not less than thirteen percent of the revenue accruing to the Federation Account.

So far, a revenue allocation formula was proposed by the Revenue Mobilisation, Allocation and Fiscal Commission in 2003 and submitted to the National Assembly through the Presidency, as prescribed by the 1999 Constitution. There emerged a structure of sharing of revenue from the Federation Account as typified below:

Vertical Formula

This shows the structure of allocation to the three tiers of government.

S/N Beneficial Percentage

1. Federal Government 46.00%
2. State Government (including FCT) 33.33%
3. Local Governments (including Area Councils) 21.00%

Total 100.00%

Horizontal Formula

This shows the structure of allocation among State Governments (including FCT) and among Local Governments (including Area Councils) to the three tiers of government.

S/N Principles of Allocation Percentage

i. Equality 45.00
ii. Population 25.60
iii. Density 1.45
iv Internal Revenue Generation Effort 8.31
v. Land Mass 5.35
vi. Terrain 5.35
vii. Rural Roads/Inland Waterways 1.21
viii. Portable Water 1.50
ix. Education 3.00
x. Health 3.00

Total 100.00

4.3.6 Revenue Sharing Formula in use in Nigeria

The revenue sharing formula in Nigeria has always tilted in favour of the Federal Government as evident from the recent formula used and presented in the figure below.

Table 1. 1: Practiced Revenue Sharing Formula (1999 – 2007)

Year	*Beneficiaries*	*Formula (%)*
1999 – 2000	Federal Government	54.68
	States	24.72
	Local Councils	20.60
		100.00
2001	Federal Government	41.30
	States	31.00
	Local Councils	16.00
	Special Funds	11.70
		100.00
2002	Federal Government	56.00
	States	24.00
	Local Councils	20.00
		100.00
2003 – 2006	Federal Government	54.68
	States	24.72
	Local Councils	20.60
		100.00
2007	Federal Government	52.68
	States	26.72
	Local Councils	20.60
		100.00

Source*: Abdullahi, S.A. (2008)*

Table 1. 2: Proposed Revenue Sharing Formula by RMFAC

Year	*Beneficiaries*	*Formula (%)*
2001	Federal Government	41.30
	States	31.00
	Local Councils	16.00
	Special Funds	11.70
		100.00
2003	Federal Government	46.63
	States	33.00
	Local Councils	20.37
		100.00
2004	Federal Government	41.30
	States	20.50
	Local Councils	6.50
	Special Funds	20.00
		11.70
		100.00
2007	Federal Government	47.19
	States	31.10
	Local Councils	15.21
	Special Funds:	1.50
	(i) General Ecology Fund	1.70
	(ii) Solid Mineral Fund	1.50
	(iii) National Reserve Fund	1.75
	(iv) Agricultural Dev. Fund	100.00

Source: *Abdullahi, S.A. (2008)*

Self-Assessment Exercise 1

Explain Fiscal Federalism?

The Federal Government independent revenue comprises the following:

i. Personal income tax of personnel in armed forces
ii. Staff of the Ministry of Foreign Affairs
iii. Residents of the Federal Capital Territory, Abuja
iv. Operating surplus of federal agencies
v. Dividends from Federal Government's investment in public quoted companies
vi. Rents on government properties
viii. Interest on and capital repayments of loans on-lent to state government and their agencies.

The State Governments' sources of internally generated revenue are:

i. Personal income tax of citizen resident in the states.
ii. Fees for registration and licensing of vehicles, permits, fees charges and levies with respect to land development etc.

For the Local Governments, the sources of internally generated revenue are:
i. property tax within their boundaries
ii. Licenses on bicycles, tricycles, motorcycles trucks, canoes, wheelbarrows and crafts, collection of rates, radio and television licenses etc.

4.3.7 Fiscal Operation of Government

You should note that under the fiscal system of Nigeria, the multi-levels of government engage in:

i. Fiscal management
ii. Preparing and implementing annual budgets for the provision of services in the respective area of jurisdiction
iii. The main objective of fiscal management over the years is that of promoting accelerated economic growth as a base for achieving higher per capita income and social welfare

Federally-Collected Revenue

Nigeria's fiscal management experience in the 1960s was characterised by narrow revenue base, largely the relative under-development of the economy. However, total federally-collected revenue rose steadily with non-oil revenue dominant, averaging N301 million annually between 1961 to N634 million in 1969 and rose to N467.4 million in 1970, constituting 73.7 per cent of total federally-collected revenue. Federally-collected revenue recorded substantial increase oil revenue during the period, 1970-1980 and contributed to 64.3 percent, while the non-oil revenue accounted for 35.7 percent.
You should note that each regime or administration adopted one measure or the other to improve the mono-economic base of the country- example: Structural Adjustment Programme (SAP) in 1986. The Federally-collected revenue retains the trend of oil based revenue being 70 percent and above till today.

Value-Added-Tax (VAT)

This was introduced by the federal government in 1994 to replace sales tax. Initially, the federal government received only 20 percent of the VAT proceeds to cover administrative cost of collection while state and local governments received 50 and 30 percent respectively. In 1995 the Federal Government decided to take 50 percent while state and local government receive 30 and 20 percent respectively. This formula varied in 1996, 1998, and 1999 as shown on the table below. You should note that revenue from VAT recorded a substantial growth since its inception in 1994, increasing from N726.8 million in 1994, which represented 3.6 percent of totally-collected revenue in that year, to N36,867.7 million or 8.0 per cent of the total revenue in 1998.

Table 1.3: VAT revenue allocation formula (%)

S/N	Governments	1994	1995	1996	1997	1998	1999
1.	Federal	20.0	50.0	35.0	35.0	25.0	15.0
2.	State and FCT	50.0	30.0	40.0	40.0	45.0	50.0
3.	Local	30.0	20.0	25.0	25.0	30.0	35.0
	Total	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**

Sources: CBN Publication (2000). Approved Budgets of the Government of the Federal Republic of Nigeria.

Self-Assessment Exercise 2

When was VAT introduced into Nigeria fiscal system? Which tax did VAT substitute?

4.4 Summary

In this unit, attempts were made to identify the Fiscal Federalism and Resources Allocation narrating from fiscal operation of government base on National Revenue Mobilisation Allocation and Fiscal Commission. Also, we attempted to identify the federal, state and local government independent revenue base and internally generated revenue and VAT.

4.5 References/Further Reading/Web Resources

Central Bank of Nigeria (2000). "*The changing structure of the Nigerian economy and implications for development"*. Lagos: Realm Communications Ltd.

Ogunjimi, S. O. (1997). *Public finance*: *For polytechnics ICAN students*. Bida Nigeria: Lekem Productions.

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4.6 Possible Answers to Self-Assessment Exercise(s) within the content

Explain Fiscal Federalism?

Answers to Self-Assessment Exercise 1

Fiscal federalism is the existence of government in a country which operates more than one tier of government, each with different expenditure responsibilities and revenue raising powers. In other words, the sharing of functions and resources among constituent units of government constitute fiscal federalism.

When was VAT introduced into Nigeria fiscal system? Which tax did VAT substitute?

Answers to Self-Assessment Exercise 2

VAT was introduced by the federal government in 1994 to replace sales tax. Initially, the federal government received only 20 percent of the VAT proceeds to cover administrative cost of collection while state and local governments received 50 and 30 percent respectively. In 1995 the Federal Government decided to take 50 percent while state and local government receive 30 and 20 percent respectively.

MODULE 3 GOVERNMENT ACCOUNTING: PUBLIC EXPENDITURE

Unit 1 Meaning, Objectives and Types of Public Expenditure

Unit Structure

1.1 Introduction
1.2 Learning Outcomes
1.3 Public Expenditure
1.3.1 Definition and Meaning of Public Expenditure
1.3.2 Objects of Public Expenditure
1.3.3 Objectives of Public Expenditure
1.3.4 Types of Public Expenditure
1.4 Summary
1.5 References/Further Reading/Web Resources
1.6 Possible Answers to Self-Assessment Exercise(s) within the content

1.1 Introduction

In this unit, you will be introduced to the concept as well as meaning of public expenditure. The objectives as well as types of public expenditure will also be discussed. For government to perform its basic functions of securing lives and property; and promoting the welfare of its citizenry, finances are hugely required. The execution of policies and programs of governments for the benefit of the citizenry requires that government incur some expenses which are termed government (public) expenditure.

This unit is therefore dedicated to acquainting you with public expenditure, its meaning, objectives and types.

1.2 Learning Outcomes

By the end of this unit, you will be able to:

- define of public expenditure
- state objectives of public expenditure
- state types of public expenditure

1.3 Public Expenditure

1.3.1 Definition/Meaning of Public Expenditure

Public expenditure refers to the expenses which government incurs for their own maintenance, benefits of the society, the economy, external bodies and for other countries. It is simply government spending of revenue derived from taxes and other sources for the purpose of providing security and catering for the general well-being of its citizens. It is the total financial spending or obligations of government to achieve both micro and macro-economic objectives. It is directed mainly for the satisfaction of the collective wants of the society. Summarily, public expenditure refers to all expenses incurred by government in the discharge of its duties to the society as well as other countries.

1.3.2 Objects of Public Expenditure

i. **Defence**: the need to ensure security and territorial integrity of a country is very crucial and therefore demands government expending huge financial resources for defense. Government incur expenses in equipping the armed forces, the police, the prison services and other paramilitary outfits and also maintaining their personnel.

ii. **Social welfare services:** this involves expenses on services such as education, health care, public housing, water and sanitation as well as other attendant services that promote the general well-being of the people.

iii. **Economic expenditure:** these involves expenses incurred by government to achieve set economic objectives. These include road construction, mining activities, commerce and industry, agriculture, communication, etc.

iv. **Public administration**: these are expenses incurred in general administration of the country particularly in salaries and wages. Government must set up institutions and machinery needed to execute its policies and programs. In doing this, government therefore incur administrative expenses.

v. **External affairs**: this has to do with expenses on activities involving contact with other countries. Expenses on running embassies and financial obligations to international bodies such as United Nations (UN), African Union (AU), Economic Community of West African States (ECOWAS), etc. as well as donations and gifts to other countries are aspects of expenses on foreign affairs.

vi. **Debt servicing:** because of the ever increasing requirement for more funds to meet growing pressing and urgent needs, the tendency for government to borrow is always there. These borrowed funds have to be repaid with interest. This repayment often forms a significant portion of government expenditure. This involves the payment of huge interests on such borrowed money either to external creditors or internal ones.

vii. **Miscellaneous expenditure**: there are myriads of expenditure that could be incidental in areas such as disaster relief, conflict management, etc.

Self-Assessment Exercise 1

What do you understand by public expenditure?

1.3.3 Objectives of Public Expenditure

Below are some of the reasons government incurs public expenditure:

i. To ensure economic welfare of the citizens: Government carries out expenditures in order to promote and increase the economic welfare of its people. This goes a long way to improve on the standard of living of its people.

ii. To ensure security of lives and property: The life and property of its people are protected through the provision of social services such as defense, law and order, fire brigade etc.

iii. Provision of public and merit goods and services: Public and merit. Goods and services are very expensive to produce by the private sector. It is therefore the government's responsibility to provide these goods and services in order to bridge the gap between the rich and the poor.

iv. To reduce unemployment: The government carries out expenditure on some economic activities in order to increase the rate of employment.

v. To ensure reduction in crime wave: Government’s expenditure is also aimed at reducing the level of crime wave in the economy. This encourages social stability and economic growth and development.

1.3.4 Types of Public Expenditure

Government expenditure can be examine, from two viewpoints namely:

(a) Transfer and absorptive expenditure (non-exhaustive)
(b) Recurrent and capital expenditure (exhaustive)

Transfer expenditures or non-exhaustive expenditures take the form of outright grants of money to private citizens or private business, i.e. payment from the corresponding transfer of real resources from the private or their use by the state. It is expenditure without quid pro quo statue. Examples are debt services (interest payment and capital repayments on internal financial obligations such as annual subscriptions to international bodies (in Nigeria) while in other countries they include social security benefits, unemployment, compensation, and other welfare payment.

Resource-using or absorptive expenditures are those that involves the transfer of funds from the government to the private sector in return for goods and services. Such non-transfer expenditures have effects that are allocational in nature unlike the transfer, expenditures whose initial effect is on the distribution of income in the society. The examples are expenditures on administration, economic, social and community services.

In Nigeria, between 1970 and 1988, transfer expenditure as a proportion of total expenditure was very small and averaged 18.2 or 3.348 percent of GDP while that of exhaustive expenditures was 86.8 percent (in 1981) and 50.1 percent in 1986. The average shares of transfer expenditures and exhaustive expenditure between 1980 and 1986 were 34 percent and 68.9 percent, respectively (Omoruyi, 1988).

On the other hand, recurrent expenditures are spending on running costs or for day-to day running of government affairs such as payment of workers' salaries and remunerations, administrative expenses and spending necessary to maintain existing levels of government social services. Capital expenditures are those that are capital stock augmenting, i.e. spending on the construction of physical assets such as schools, roads, bridge, and other capital investments. There are expenditure earmark for specific project execution in the forthcoming year.

Others have also tried to classify expenditure on the basis of its effects on production: productive and unproductive expenditures. All spending that is necessary and relevant to improve the productive capacity of the

economy is productive expenditure. On the other hand, unproductive expenditures: are expenditure in incurred to bring about development.

Self-Assessment Exercise 2

Differentiate between transfer and recurrent expenditure?

1.4 Summary

Summarily, public expenditure refers to all expenses incurred by government in the discharge of its duties to the society as well as other countries. These expenses are incurred on objects such as defence, economy, public administration, social welfare, eternal affairs, debt servicing and other miscellaneous. Government raise revenue to fund public expenditure in order to achieve to promote economic welfare of the citizens, to ensure security of lives and property, provide public and merit goods and services, reduce unemployment, and ensure reduction in crime wave.

1.5 References/Further Reading/Web Resources

Benjamin, E. & Martin, N. (2012). *Public finance administration in Nigeria. Cases and issues*. Onitsha: Chambers Books Ltd

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Ola, R.O.F. & Offiong, O.J. (2008). *Public Financial Management in Nigeria*. Lagos: AMFITOP Books.

Oriakhi, D.E. (2004) *Introduction to Public Finance. (*2nd ed.). Nigeria: Mindex Publishing.

1.6 Possible Answers to Self-Assessment Exercise(s) within the content

What do you understand by public expenditure?

Possible Answers to Self-Assessment Exercise 1

Public expenditure refers to the expenses which government incurs for their own maintenance, benefits of the society, the economy, external bodies and for other countries. It is simply government spending of revenue derived from taxes and other sources for the purpose of providing security and catering for the general well-being of its citizens.

Differentiate between transfer and recurrent expenditure?

Possible Answers to Self-Assessment Exercise 2

Transfer expenditures involve outright transfer of money to private citizens or private business which could be payment for services rendered by private organisations to the government. It is expenditure without quid pro quo statue. Examples are debt services, social security benefits, unemployment, compensation, and other welfare payment. On the other hand, recurrent expenditures are spending on running costs or for day-to day running of government affairs such as payment of workers' salaries and remunerations, administrative expenses and spending necessary to maintain existing levels of government social services.

Unit 2 Canons and Classification of Public Expenditure

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Canons and Classification of Public Expenditure
2.3.1 Canons of Public Expenditure
2.3.2 Classification of Public Expenditure
2.3.3 Effects of Public Expenditure
24 Summary
2.5 References/Further Reading/Web Resources
2.6 Possible Answers to Self-Assessment Exercise(s) within the content

2.1 Introduction

Having been acquainted with the meaning of public expenditure and its objectives in the previous unit, this unit will take you further into the concept of public expenditure by discussing the canons of public expenditure otherwise known as principles guiding public expenditure. The unit will also acquaint you with the various classifications of public expenditure.

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- itate canons of public expenditure
- identify the various classification of public expenditure
- state the effects of public expenditure on society

2.3 Canons and Classification of Public Expenditure

2.3.1 Canons of Public Expenditure

There are several principles suggesting the maximization of gains of public expenditure. These principles are known as canons of public expenditure. In other words, canons of public expenditure simply refer to principles guiding government in the utilization of public revenue or

monies to ensure that maximum gains are derived from these expenditure. They are as follows:

1. Canon of economy: Since resources are scare relative to their needs, no wastage should be permitted. Thus, the process of public expenditure should not involves the use of resources more than what are just necessary. Utmost care must be taken to avoid wasteful usage of public funds. This includes avoiding delay in plan formulation, sanction and execution, especially when prices are rising. In most cases, wastage is avoided by using the cost-benefits approach to evaluate projects.
2. Canon of sanction: This requires that no used of public funds embarked upon without proper authorization and that funds must be used only for the purpose for which they have been sanctioned. This ensure the avoidance of unscrupulous and unwanted expenditure, while checking misappropriate of funds.
3. Canon of benefit: Authorities should spend public funds only if they are beneficial to the society. Thus, they should try to choose that combination of item for public expenditure collectively maximizes the social benefit. In this way, the principle of maximum social advantage' is attained.
4. Canon of surplus: Government should be prudent and aim at meeting its current expenditure needs out of its current revenue, and hence should avoid deficit budgeting. By avoiding over spending and debt, the government should achieve a moderate surplus. Moderate surpluses during some years will take care of reasonable but unavoidable deficit during other years.
5. Canon of elasticity: This canon requires that public expenditure should not in any way be rigidly fixed. It should be rather fairly elastic, that is it should be allowed to vary according to needs and circumstances. The expenditure policy should be elastic, rather than rigid in character. There should be enough scope for change in expenditure policy, according to time and requirement. Government should be able to increase public expenditure during periods of economic emergency and to decrease during periods of normalcy.
6. Canon of productivity: public expenditure should stimulate productivity. Public expenditure should be made in such a way to that it fosters capital formation and generate employment opportunities along with increased level of productivity.
7. Canon of equitable distribution: public expenditure should foster equitable distribution of wealth. The government should make expenditure in such a manner as to provide more benefit to the backward section of the society.
8. Canon of certainty: the areas in which public expenditure is to be made should be certain so that the development works may be

carried out properly. The government should determine with certainty the allocation of public expenditure to various uses.

Self-Assessment Exercise 1

What do you understand by canons of public expenditure and state four (4) of those canons?

2.3.2 Classification of Public Expenditure

Public expenditure can be divided according to functions such as administrative and general services, economic services, transfer service, and social and community services.
Administrative and general services: These are expenditure that cover general administration and internal security of the country in order to maintain law and order. It include expenditure on the civil service, the police, army prisons and other armed forces as well as payment of salaries and other allowances of public servants.

Economic services: These are expenditures of government on economic activities that are meant to generate revenue returns. This include the development of agriculture, fisheries, industries and trade, transportation, communication etc.

Social and community services: These include all investments and expenditure of the government in the development and management of health care Service, education, Recreational facilities, refuse and waste disposal, water and electricity good road networks transport and communication.

Transfer services: Government spends money in servicing of both domestic and foreign debts, it also includes expenditures incurred and granting financial aids and assistance to neighbouring countries, grants to state and local government, social security and unemployment benefits etc.

2.3.3 Effects of Public Expenditure

Public expenditure is a very important fiscal weapon to achieve increase in production, equitable distribution of income and wealth, economic stability and growth. The possible effects of public expenditure can be described as follows:

a. **Effects of public expenditure on production**
The character and volume of public expenditure are bound to have some effects on the pattern and amount of production in a

country. Public expenditure can help the economy in numerous ways in attaining higher level of production and growth. It helps to increase the productive capacity of a society. It may help to build up new industries through state patronage.

According to Dalton, effects of public expenditure depend on three factors as follows:

(i) Ability to work, save and invest - efficiency effects;
(ii) (ii) Willing of people to work, save and invest- incentive effects;
(iii) (iii) Effects on diversion of economic resources as between different uses and localities - allocative effects.

Increase in public expenditure on social and economic services will increase the efficiency of persons to work. Expenditure on providing certain services such as education, health, social security measures to the society increases their ability to work more efficiently and thus increases production and productivity. Expenditure of the government on wages, salaries and pensions and above items will increase income of the people and that raises the ability of the people to save and invest.

Public expenditure on infrastructural facilities increases the ability of entrepreneurs to invest. Conditional public expenditure, such as increase in benefits from public expenditure linked to hard work or more saving and more investment leads to favourable effects on the economy. It will increase willingness to work more, save more and invest more. Government expenditure may induce people to divert their resources to more productive uses. Conditional grants and loans to private producers, quality control schemes, etc., may bring about desirable diversions of resources. Such expenditure increases productivity with beneficial effects on total output.

b. **Effects of public expenditure on distribution**

Public expenditure is a powerful tool in the hands of the government to bring about equitable distribution of income and wealth. It tends to reduce inequalities and helps to maintain income and employment of the relatively poorer sections of the community. It is helpful to increase opportunities for them through the provision of education, public health and medical services. Planned expenditure policy of the government can bring the desired results. Compensation to workers in the case of accidents and sickness, expenditure on employment exchanges,

distribution of essential goods through subsidised fair price shops, provision of free education, promoting industries in the backward regions, promotions of small scale industries through various schemes are the type of public expenditure, which can secure distributive justice to the weaker section of the community.

c. **Effects of public expenditure on economic Stability**

Economic stability refers to stability in national income, employment and general price level. During periods of depression, increase in public expenditure helps to sustain income, output and employment levels in a country. Public expenditure can create additional employment and maintain effective demand to ensure price stability. Public expenditure can also help in curbing inflationary conditions prevailing in the country. Inflationary pressure can be reduced by reducing unproductive expenditure on civil services. Under such circumstances the public expenditure should be incurred on those projects which raise sufficiently the volume of production within a short time.

d. **Effects of public expenditure on economic development**

Public expenditure has to play an active role in reducing regional disparities, developing economic and social overheads, growth of capital goods industries, research and development etc., in developing countries. Public expenditure on economic and social overheads assists the productive processes in the economy. In a developed economy, public expenditure maintains a smooth rate of economic growth in order to get the stabilization and stimulation of economic activities. An increase in public expenditure will always tend to have an expansionary effect. The construction of roads, railways and means of communication helps to increase production, trade and commerce. Public expenditure can be used to raise the agricultural production and reducing regional disparities. Subsidies can also help to promote import substitution. Expenditure on education, public health and medical services ensures that the working force is more cultured, healthier and efficient. The total effects produced by public expenditure depend upon the volume of public expenditure.

Self-Assessment Exercise 2

State four effect of public expenditure on the society?

2.4 Summary

Canons of public expenditure simply refer to principles guiding government in the utilization of public revenue or monies to ensure that maximum gains are derived from these expenditure. They are canons of economy, sanction, benefit, certainty, surplus, elasticity, productivity and equal distribution. In terms of classification, public expenditure are classified on the basis of their perceived functions such as administrative and general services, economic services, transfer service, and social and community services. Effect of public expenditure on the society can be seen from the perspectives of economic production, distribution, stability and development

2.5 References/Further Reading /Web Resources

Benjamin, E. & Martin, N. (2012). *Public finance administration in Nigeria. Cases and issues*. Onitsha: Chambers Books Ltd

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2.6 Possible Answers to Self-Assessment Exercise(s) within the content

What do you understand by canons of public expenditure and state four (4) of those canons?

Possible Answers to Self-Assessment Exercise 1

Canons of public expenditure simply refer to principles guiding government in the utilization of public revenue or monies to ensure that maximum gains are derived from this expenditure. The canons of public expenditure are:

i. Canon of economy,
ii. Canon of sanction,
iii. Canon of benefit,
iv. Canon of certainty

State four effect of public expenditure on the society?

Possible Answers to Self-Assessment Exercise 2

a. **Effects of public expenditure on production**
The character and volume of public expenditure are bound to have some effects on the pattern and amount of production in a country. Public expenditure can help the economy in numerous ways in attaining higher level of production and growth. It helps to increase the productive capacity of a society.

b. **Effects of public expenditure on distribution**
Public expenditure is a powerful tool in the hands of the government to bring about equitable distribution of income and wealth. It tends to reduce inequalities and helps to maintain income and employment of the relatively poorer sections of the community. It is helpful to increase opportunities for them through the provision of education, public health and medical services.

c. **Effects of public expenditure on economic Stability**
Economic stability refers to stability in national income, employment and general price level. During periods of

depression, increase in public expenditure helps to sustain income, output and employment levels in a country.

d. **Effects of public expenditure on economic development**

Public expenditure plays active role in reducing regional disparities, developing economic and social overheads, growth of capital goods industries, research and development etc., in developing countries. Public expenditure on economic and social overheads assists the productive processes in the economy.

Unit 3 Theories of Public Expenditure Growth

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Theories of Public Expenditure Growth
  3.3.1 General Theories of Public Expenditure
  3.3.2 Pure Theories of Public Expenditure
  3.3.3 Factors that affect the Size of Public Expenditure
3.4 Summary
3.5 References/Further Reading/Web Resources
3.6 Possible Answers to Self-Assessment Exercise(s) within the content

3.1 Introduction

In the previous unit, you have been introduced to the canons or principles that guide government in incurring public expenditure and effect of public expenditure on the society as well as the various classifications of public expenditure. This unit will therefore take you further into the concept of public expenditure by discussing the theories of public expenditure. This unit will focus particularly on Wagner's Hypothesis of Increasing Government Activity and Wiseman Peacock Hypothesis.

3.2 Learning Outcomes

By the end of this unit, you should be able to:

- state the key submissions of General theories of public expenditure as submitted by Wagner and Wiseman Hypotheses
- state the key features of Pure theories of public expenditure
- state factors that affect the size of public expenditure

3.3 Theories of Public Expenditure Growth

Historically, public expenditure has recorded a continuous uptrend over time in almost every country. However, traditional thinking and philosophy did not pay much attention to frame and theory regarding the increase of public expenditure. It considered market mechanism as a better guide in working of the economy and allocation of its resources. However, in 20th century the modem state is termed as welfare state in which the government has enormous functions to perform.

Theories of increasing public expenditure can be classified into two parts as: (1) General theories of public expenditure, and (2) Pure theories of public expenditure. 1. General theories of public expenditure: There are two important and well-known theories of increasing public expenditure which are as follows: (i) Wagner's law of increasing state activities (ii) Wiseman-Peacock hypothesis

3.3.1 General Theories of Public Expenditure

Wagner's Law of Increasing State Activities

Adolph Wagner (1835-1917) was a German economist who based his Law of increasing state activities on historical facts, primarily of Germany. He believed that there is a functional cause and effect relationship between the growth of an economy and the relative growth of public sector. The law states that the development of an industrial economy will be accompanied by an increased share of public expenditure in GNP. In his famous 'Law of increasing state activities,' Adolph Wagner opines; 'Comprehensive comparisons of different countries and different times show that among progressive people, with which alone we are concerned, an increase regularly takes place in the activity of both the central and local governments. This increase is both extensive and intensive; the central and local governments constantly undertake new functions, while they perform both old and new functions more efficiently and completely.'

According to Wagner, there are inherent tendencies for the activities of different layers of a government to increase both intensively and extensively. Wagner's hypothesis was supported by the famous economist F. S. Nitti. He concluded with empirical evidence that this Taw' was not only applicable to Germany but to various governments which differed widely from each other. All kinds of governments irrespective of their type of governments (say, the central or state

governments), size had shown the same tendency of increasing public expenditure. It means that Wagner's hypothesis of increasing state activity has enlisted two major points, i.e. intensive increase in state activities; and extensive increase in state activities. Intensive increase refers to expansion of the traditional activities and extensive increase refers to the increase in the new activities of the state.

According to Wagner hypothesis, there are traditional and new activities of the state which are responsible for persistent increase in public expenditure. Traditional activities are defence, maintenance of law and order in the country, construction and maintenance of roads and railways, and provision of education to the people. New functions of the state are encouragement to industry, agriculture and labour, promotion of public welfare through welfare measures, extension of control over the economy, urbanisation. Wagner admitted that continuous extension of economic and social activities was the basic reason of the relative growth of public expenditure.

Wagner's hypothesis is criticised by Allan T. Peacock and Jack Wiseman on the following grounds: it lacks inter-disciplinary relationship, it lacks comprehensive analytical framework, it is not the accepted theory in the west countries and it ignores the influences of war.

Wiseman Peacock Hypothesis

This hypothesis of the growth of public expenditure was put forth by Wiseman and Peacock in their study of public expenditure in Great Britain for the period 1890-1955. It highlights the fact that public expenditure does not increase in a smooth and continuous manner, but in jerks or step-like fashion. In other words governmental fiscal activities rise step by step due to some social or other disturbances such as war or depression which the existing public revenue cannot meet.

During this phase, some social or other disturbances takes place which shows the need of increased expenditure as the existing revenue could not meet the situation. Wiseman and Peacock observed that the relative growth of the public sector in the United Kingdom followed a discrete step-like pattern rather than a continuous growth pattern. The step by step like spending took place in United Kingdom in a period of major social disturbances which creates a 'displacement effect'.

The movement from the older level of expenditure and taxation to a new and higher level is the displacement effect. After the social disturbance is over, the new levels of 'tax tolerance' make the society to support a higher level of public expenditure. The inadequacy of the revenue as compared with the required public expenditure creates an 'inspection

effect.' War and other social disturbances frequently force the government and the people to review the revenue position and the need to find out the solution of problems which previously had been neglected. Wiseman-Peacock also mentioned a 'concentration effect' which refers to the tendency for central government economic activity to grow faster than that of the state and local governments. Moreover, concentration effect is closely connected with the political set up of the country.

3.3.2 Pure Theories of Public Expenditure

The pure theories of increasing public expenditure can be further classified into three parts- Pigou's ability to pay, benefit analysis and Samuelson theory.
Prof. A. C. Pigou in his chapter V 'Range of Government Expenditure' in A Study in Public Finance gave the most comprehensive treatment to ability to pay theory in the determination of optimum level of public expenditure. According to him, the optimum amount of government expenditure is determined at the point at which the satisfaction obtained from the last money spent is equal to the satisfaction lost in respect of the last money. The optimal determination of public expenditure on the basis of benefit principle finds its clear statement in the voluntary exchange theory of Swedish Economist Erik Lindahl. According to his theory, determination of public expenditure and taxation will happen on the basis of public preferences which they will reveal themselves.
Samuelson's pure theory of public expenditure goes back to Italian and Australian writers who are responsible for the renaissance of the benefit approach. It solves two problems under the assumptions of given preferences and distribution of income.

Self-Assessment Exercise 1

Give highlights of the key features of General theories of public expenditure?

3.3.3 Factors that affect the Size of Public Expenditure

The following are factors that influence the size of public expenditure:

a. Macro-economic objectives
b. Change in per capital income.
c. Change in size of population
d. Change in political and social awareness
e. Increasing rate of urbanization

Macro-economic objective: The economic objective in term or policies to be pursued by government within a particular period of time can determined the size of government expenditure. When there is a change of objectives, there will be rise of fall in the level of government expenditure. For instance, the macro-economic policy of the government in 2003 which include a holistic diversification of the revenue base of the country into agriculture, the monetization policy and the 12.5% increase in wages of public servants will increase government expenditure compared with the year 2002 budgeted expenditure.

Change in per Capita Income: income Per capita income is minimum attributable to each citizens residing within the geographical region of a country. Any time there is an increase in the per capita income, citizens in the economy increase demand for social goods and services in order to meet this level of demand. It becomes absolutely necessary for government to increase its expenditure. This was experienced in Nigeria in 1998. The increase in the salary of civil servants led to increase in demands for goods and services most especially motor vehicle.

Change in Size of Population: When the level of population rises, it implies that government needs to increase the quantity of social goods and services in the economy by increasing its budgetary expenditure.

Change in Political and Social Awareness: When there is change in political awareness, it implies that government must spend more money in order to satisfy the request of the citizens in the economy. Few year ago when there was persistent advocate for the creation of states and local government which the government eventually acceded to government has to contend with the huge take off grant and the monthly finance of the general apparatus of these newly created states and local councils.

Increasing Rate of Urbanization: In a developing country like Nigeria where problem of rural-urban migration is highly pronounced, concentration of many people in urban centres has created physical distress e.g. Lagos, Abuja Kano etc. The cost of maintaining these cities is certainly huge.

Self-Assessment Exercise 2

Mention four factors that affect the size of a country's public expenditure?

3.4 Summary

Theories of increasing public expenditure can be classified into two parts as: (1) General theories of public expenditure, and (2) Pure theories of public expenditure. 1. General theories of public expenditure: There are two important and well-known theories of increasing public expenditure which are as follows: (i) Wagner's law of increasing state activities (ii) Wiseman-Peacock hypothesis.

Theories of public expenditure growth submit that:

i. there exist a functional cause and effect relationship between the growth of an economy and relative growth of the public sector, that is increase in public expenditure leads to increased growth of the economy.
ii. intensive (traditional roles) and extensive (new roles) increase in state activities is responsible for the growth in public expenditure.
iii. traditional activities are defence, maintenance of law and order in the country, construction and maintenance of roads and railways, and provision of education to the people. New functions of the state are encouragement to industry, agriculture and labour, promotion of public welfare through welfare measures, extension of control over the economy, urbanisation.
iv. public expenditure does not increase in a smooth and continuous manner but in jerks and step-like fashion, that is a gradual rise due to some social or other disturbances such as wars, depression, etc.

Factors that have influence the growing size of public expenditure include macro-economic objectives, change in per capital income, change in size of population, change in political and social awareness, and increasing rate of urbanization

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3.6 Possible Answers to Self-Assessment Exercise(s) within the content

Give highlights of the key features of General theories of public expenditure?

Possible Answers to Self-Assessment Exercise 1

The key features highlights of the General theories of public expenditure are:

i. that there exist a functional cause and effect relationship between the growth of an economy and relative growth of the public sector, that is increase in public expenditure leads to increased growth of the economy.
ii. that intensive (traditional roles) and extensive (new roles) increase in state activities is responsible for the growth in public expenditure.
iii. Traditional activities are defence, maintenance of law and order in the country, construction and maintenance of roads and railways, and provision of education to the people. New functions of the state are encouragement to industry, agriculture and labour, promotion of public welfare through welfare measures, extension of control over the economy, urbanisation.
iv. that public expenditure does not increase in a smooth and continuous manner but in jerks and step-like fashion, that is a gradual rise due to some social or other disturbances such as wars, depression, etc.

Mention four factors that affect the size of a country's public expenditure?

Possible Answers to Self-Assessment Exercise 1

The factors that affect the size of a country's public expenditure are:

i. Macro-economic objectives
ii. Change in per capital income.
iii. Change in size of population
iv. Change in political and social awareness
v. Increasing rate of urbanization

Unit 4 Public Debt

Unit Structure

4.1 Introduction
4.2 Learning Outcomes
4.3 Public Debt
  4.3.1 Definition of Public Debt
  4.3.2 Rationale for Public Debts
  4.3.3 Types of Public Debts
  4.3.4 Sources of Public Debt
  4.3.5 Public Debt Management
4.4 Summary
4.5 References/Further Reading/Web Resources
4.6 Possible Answers to Self-Assessment Exercise(s) within the content

4.1 Introduction

In the previous unit, you were introduced to theories explaining public expenditure growth and factors accounting for growth in public expenditure by governments. The growth in public expenditure by governments across the globe occasioned by expanding traditional role as well as new roles being undertaken by governments have resulted in nations incurring debts both local and international. This unit will introduce you to the concept of public debt. This unit will focus particularly on meaning of public debt, sources of public debt as well as the management of public debt.

4.2 Learning Outcomes

At the end of this unit, you should be able to:
i. Define the term 'public debt'
ii. State the various sources of public debt
iii. Explain how public debts are managed

4.3 Public Debt

4.3.1 Definition of Public Debt

The short-fall between domestic savings and the desired level of investments in most countries (especially developing ones) has led to both internal and external borrowings to fill the gaps. These led to financial liabilities (public debt) by government to individuals and institutions within and outside the country. In a developing country like Nigeria, the Central Bank on behalf of the government borrows money from both internal and external sources to bridge gaps between revenue and expenditure. Public debt therefore is the amount of money owed by the government to institutions, governments and individuals' resident in or outside Nigeria.

Deficit financing is the creation of extra purchasing power by government which then utilises it for purchasing away resources from the market. It could also be defined as the net increase in the amount of money in circulation where such an increase result from a conscious government policy designed to encourage economic activities which ordinarily would not have taken place; and from another angle amounts to domestic credit creation which is not off-set by increased taxation, more restrictive bank credit policy and similar deflationary measures.

This involves running down the government accumulated cash balances, net borrowing from the banking system, issuing of new currency by the central bank, net borrowing from abroad and drawing down of foreign assets There is no single approach to economic development; multi-frontal attack on social, economic, political, cultural and attitudinal obstacles to it, which deficit financing is one tool. On the whole, you should note that there can be no deficit financing without deficit budgeting.

4.3.2 Rationale for Public Debts

Below are some of the reasons that have accounted for public debts by governments:
Budget deficit: a government like any other economic units collect revenue and spend it. It is also a fact that its revenue and expenditure may not match each other during a given period. To bridge the gap between revenue and expenditure especially when expenditure outweighs revenue, government resort to borrowing. This borrowing majorly constitute public debts.

Sudden spurt in government expenditure: there may be wars or natural calamities in which case the government would be forced to incur much larger expenditure and may run into debts.

Functional finance: this is a process in which the government is ready to have repeated surplus or deficit budgets for achieving a variety of objectives including those of economic growth and stabilisation.

Loan for development purpose: it is a widely held belief these days that governments of developing countries should play an active role in the development of an economy. As such, government of developing or under developed countries embark borrowing both from local and international financial institutions to augment their budgets in order to execute projects and programs capable of promoting development.

Self-Assessment Exercise 1

i. What is Public Debt?
ii. Mention three (3) rationale for Public Debt?

4.3.3 Types of Public Debts

The type of public used in this book, reflect the purpose in which the debts was contracted.

1. Trade debts: A trade debt arises when there is imbalance of trade between two countries. It can be called balance of trade deficit when a country is unable to ay pay partially or wholly for the tangible goods supplied to it. For example, if Nigeria import #200m cost of Gold from Ghana and export # 150m cost of oil to Ghana, the remaining# 50m is called trade debts.
2. Balance of payment support loan: This covers the overall economics transaction between a country and the rest of the world. The transaction includes visible and invisible transactions, classified into current_ and capital accounts; official settlement balance etc., which can be favourable or unfavourable balance of payment (surplus or deficit). Government can borrow money to augment persistent balance of payment deficit.
3. Project-tied loans: investment which have good economic potentials and can accelerate economic growth and development may force the government to borrow money to execute. That type of debts can be called project feed loan or loan for specific

purposes. The loan should not be diverted to any project outside the purpose which the debt is incurred. This type of loan is self-liquidating.

4. Loan for social economic needs: this a debt incurred for the provision of socio- economic needs of a country. It is not targeted on a specific project, but for general purpose like social amenities, infrastructure, health, education, etc.

4.3.4 Sources of Public Debts

We have two sources of public debts namely: -

a. Internal Source
b. External Sources

1. **Internal Sources:** The internal sources of public debts are the Central Bank of Nigeria, commercial banks, the merchant banks and the non-bank public. The nonbank public includes insurance companies saving institutions, state and local governments, statutory boards/corporations, and individuals. The debts are usually · contracted through instruments such as treasury bills, treasury certificate and government development stocks etc. The central bank of Nigeria has been underwriting: the instrument on behalf of the federal government. Arrangements are on to the board underwriting functions of the CBN to discount houses under the Banks open market operation.

b. **External Sources:** These represent the Paris club of creditors, (for example USA, UK, Federal Republic of Germany, France and Canada, representing government official creditors. The London club of creditors (representing commercial banks in industrialized countries), the multilateral creditors such as the world B~ international monetary fund, African development Bank (ADB), European investment Bank, international Development Association (IDA) and International Fund for Agricultural Development (IFAD). Promissory note holders are creditors in respect of refinance. The bilateral and private sectors are also included in eternal debts.

4.3.5 Public Debt Management

Every country has its own way of managing its public debt and for this purpose, a number of policy instruments with different objectives have over time evolved. Debt management policies are, for the most part, designed to go in tandem with the broader macroeconomic objectives of Stabilisation and growth. It is important to note that debt management

strategies relate largely to the question of repayment and reduction of domestic as well as foreign debts.

In Nigeria the Central Bank of Nigeria is statutorily with the responsibility of debt management in conjunction with the Federal Ministry of Finance and other agencies. Recent development has witnessed the establishment of Debt Management Office in the Vice President's Office to oversee the work of all the above named agencies on Public Debt Management. Debt Management is the technical, operational, and institutional arrangements engaged in managing a country's liabilities so that the debt stock and the debt service burden are contained at a tolerable and sustainable level. The technical aspect focuses on the need to determine the level of external debt required and to ensure that terms and conditions of those borrowings are in consonance with the future debt service capacity of the country.

Institutional arrangements include the administrative, organisational and monitoring aspect of managing both new borrowings and the total stock of debt. Nigeria has made efforts by successive government administration to restructure the county's debt over the years. Measures adopted include, refinancing, rescheduling restructuring of debt arrears and outright payment/settlement of the debt.

Internal (Domestic) Debt Management

The Federal Ministry of Finance (Treasury) manages government domestic debt; while Federal Government loans publicly issued in Nigeria is issued and managed by the Central Bank by:

- Advising the government on timing of floating debt instruments and terms of issue.
- Advertising for public subscription to the issues.
- Collecting the proceeds of issues on government behalf.
- Supervising the issue of certificates and warrants.
- Paying principal and interest on matured debts and in addition manages the sinking fund that facilitates redemption.

The authority controlling the above responsibilities could underwrite the unsubscribed portion and provide a secondary market where the divestment of public holdings could be carried out at a discount as it is done in Nigeria. Thus, adequate guarantee is provided for debt instruments.

The Federal Ministry of Finance (a controlling agency) manages other domestic debts such as contractual debts and organises the mode of

payment through appropriate consultation with the Federal Government and the Central Bank.

1. **Acquisition of Domestic Debts**
   The Central Bank of Nigeria advises government as to the timing of floatation of debt instruments and terms of issue. Advertisements are usually put up and subscription made through the banks and acceptance houses. The duty lies on the CBN to maintain appropriate books and accounts of such transaction.

2. **Restructuring of Domestic Debts**
   The Central Bank of Nigeria accommodates government short term financial shortfalls through the provision of overdraft facility by Ways and Means Advances.
3. **Servicing of Domestic Debts**
   The CBN makes the interests and principal payments of domestic debts which fall due. It provides discount as well as rediscount facilities in respect of debt instruments held by its customers. This later function is however being transferred to the Discount Houses. In the case of development stocks, the CBN publishes due dates for redemption of maturing stocks through redemption schedule statements and payment forms. This is further facilitated by the creation of a sinking fund. Sinking fund is a fund into which government pays in amount from time to time for the purpose of redeeming its liabilities on the development stocks under various balances. The balance of the sinking fund of each development stock is at times reinvested in another development stock with a higher rate of interest and of nearer maturity.

External (Foreign) Debt Management

External Debt Management is a conscious and carefully planned schedule of loans acquired either for development purposes or to support the balance of payment. It incorporates estimates of foreign exchange earnings, sources of finance, the projected returns from the investment and the repayment schedule. It also includes the assessment of the countries capacity to service existing debts and whether further loans could be contracted.

Nigeria's external debt management strategies have varied from time to time to time since the early 1980s, when the debt crisis was pronounced. However, in 1988, comprehensive measures were set out with the following policy objectives:
To evolve strategies increasing foreign exchange earnings thereby reducing the need for external borrowing.

1. To set out the criteria for borrowing from external sources and determine the type of projects for which external loans may be obtained.
2. To outline the mechanism for servicing external debts of the public and private sectors.
3. To outline the role and responsibilities of various organs of the federal and state governments as well as the private sector in the management of external debt.

The action on the above named policy objectives motivated the Nigerian government desire to reduce the burden of external debt and the following steps were developed over the years:

Embargo on New Loans: To check un-manageable hike in debt stock leading to preventing more debt burden. This is used to prevent a situation where the public debt becomes unmanageable as a result of unnecessary increases. The federal government directed in 2001 that no applicant for external loans, whether a state or federal government agencies, was allowed to borrow more than US$500m for any projects unrelated to poverty alleviation endeavours. Such a loan must be guaranteed by the Federal Government after being assessed with the approval of the National Planning Commission. In addition, for such loans, debt service is not expected to exceed 40 percent of state government's allocation from the Federation Account (The Guardian, December 17, 2001).

Limit on Debt Service Payments: This encourages the use of a particular proportion of our external earnings to service the external debt.

Debt Restructuring: Outstanding debts are converted into another type of debt. Refinancing, re-scheduling, buy-back, issuance of collateralised bond and provision of new money are different categories of debt financing are discussed below:

Re-financing of Trade Arrears: This is a new loan procured by a debtor to pay-off an existing debt if it involved short-term trade debt. This relates to procurement of a new loan by a debtor country in order to pay off an existing debt especially when it involves short term trade debt. The new loan may be contracted from the same creditor countries or a different set of creditor. However, what is important is that the repayment schedule is always contained in the loan agreement. In July and September, 1983, Nigeria had her first and second refinancing agreements. In both agreements, the sum of US$2.1 billion worth of trade arrears, unconfirmed letters of credit were refinanced. There are

two processes involved in re-financing of trade arrears. They are: debt rescheduling and debt buy back.

Debt re-scheduling: This is the postponement of the effective maturity date of debt owed to a future date. This relates to deferment of debts. It is the postponement to the future effective maturity date of the debts. This measure serves to give more temporary relief to the debtor nation or country. In December, 2001, Nigeria signed rescheduling agreement with Germany, Austria and Switzerland. The amount involved totaled US3.267 billion (Onuorah, 2001 quoted in Edosa and Osaze, 2003).

Debt Buy-Back: When a substantial discount is offered by the creditor to the debtor for the payment of outstanding debt. This is when the debtor is offered a substantial discount by the creditor nation for the payment of outstanding debts. Nigeria got involved in February, 1992, when USA 3.395 billion USD commercial debts owed to the London Club was bought back by Nigeria at 60 percent discount. The implication is that Nigeria paid USD1.352 billion to liquidate or buy back the commercial debts (Oriakhi, 1992 quoted in Edosa and Osaze, 2003).

New Money: This is the provision of new money which involves essentially the granting of new loans to assist a much indebted and burdened country by a creditor state or a group of creditor countries.

Debt Conversion: The exchange of monetary instruments like promissory notes for tangible assets or other financial instruments. In simple terms, it means exchange of monetary instrument e.g. promissory notes for tangible assets or other financial instruments. It is designed for the reduction of a country's external debt burden by changing the character of the debts.

Collateralisation*:* Under this arrangement, the yield of a bond collateralised within a specified period is expected to offset or pay off a collateralised amount referred to as the zero coupon option.

Debt Swap: This is a loan that could be paid for by other means like crude oil as was carried out between 1984 and 1985 (Buhari/Idiagbon Regime).

Debt Servicing: This is paying interest on loan.

Debt Settlement: This implies paying up the debt which Nigeria did in 2005.
Nigeria's external debt outstanding at the end of 1998 was $28.8 billion, made up of debts owed to Paris and London Clubs of creditors, multi-

lateral institutions, promissory notes and other multi-nationals. These agencies will be discussed later in Unit 5 of this Module.

The Federal Government through the Ministry of Finance and Economic Development during President Obasanjo administration passionately negotiated Nigeria debt burden and effectively settled the debts with the international agencies in 2003, hence the name of Nigeria was de-listed from international debtors list. The debt which has been accumulating over the years and the growth of the debt was attributable largely to the need to finance budgetary gaps.

4.4 Summary

Public Debt Management is shown as the technical, operational and institutional arrangements engaged in managing a country's liabilities so that the debt stock and the debt service burden are contained a tolerable and sustainable level. This will be performed by the agencies of government be it internal or external debts. In this unit, attempts were made to define public debt, deficit financing, identify sources of public debt and discuss debt management strategies. The Central Bank of Nigeria, Federal Ministry of Finance and other agencies have been identify with debt management in Nigeria. Recent development establishes a Debt Management Office in the office of the Vice President of the Federation.

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4.6 Possible Answers to Self-Assessment Exercise(s) within the content

1. *What is Public Debt?*
2. *Mention three (3) rationale for Public Debt?*

Possible Answers to Self-Assessment Exercise

1. Public debt is the amount of money owed by the government to institutions, governments and individuals' resident in or outside Nigeria.

2. The Rationale for Public Debts are as follows:

a. Budget deficit
b. Sudden spurt in government expenditure
c. Functional finance
d. Loan for development purpose

Unit 5 Nigeria's Public Debt Profile

Unit Structure

5.1 Introduction
5.2 Learning Outcomes
5.3 Nigeria's Public Debt Profile
 5.3.2 Sources of Public Debt
 5.3.3 Public Debt Management
5.4 Summary
5.5 References/Further Reading/Web Resources
5.6 Possible Answers to Self-Assessment Exercise(s) within the content

5.1 Introduction

In the previous unit, you were introduced to the concept of public debt, its rationale, source and types. You were also introduced to the concept of public debt management. Public debt basically occurs as a result deficit in revenue as against expenditure. Governments, especially in developing countries have had to incur public debt in their bid to fast track development. This unit will acquaint you with the debt profile of the country. Focus will be on the fourth republic, that is, from 1999 till date.

5.2 Learning Outcomes

By the end of this unit, you will be able to:

- trace the trend of Nigeria's public debt from 1999 till date
- state factors responsible for the rising debt profile of the country

5.3 Nigeria's Public Debt Profile

Nigeria's public debt has been on the rise. Despite securing debt relief during the Olusegun Obasanjo-led administration, successive governments have continued on a borrowing spree — the Federal Government's component of the public debt surging 658 percent to N26.9 trillion in the last 21 years. This has raised concerns among Nigerians on the debt sustainability of the country amid dwindling revenue to meet the debt obligations to creditors. As of March 2021,

Nigeria's total public debt has hit N33.1 trillion ($87.24 billion) — an accumulation of borrowings from successive governments, of which most were borrowed since the return to democratic rule in 1999. The overall public debt is the total debt accrued by federal, states, and the FCT from local and international lenders.

Of the N33.1 trillion, the Federal Government alone borrowed N26.91 trillion — this includes the FGN bonds, Sukuk, green bonds and Euro bonds. (TheCable, 2022)

Debt Profile under Olusegun Obasanjo's Administration (1999-2007)

During the tenure of former president Olusegun Obasanjo, the debt level of the federal government reduced from N3.55 trillion in 1999 to N2.42 trillion at the end of 2007.

The 8-year term of Obasanjo resulted in a dip in FG's local and foreign debt level, representing a 31.8 percent decline. The country's exchange rate was between N98.02 to N116.8 to a dollar during the tenure. Analysis of the figures showed that external debt decreased from $28.04 billion by 1999 to $2.11 billion at the end of 2007. However, the domestic component increased from N798 billion to N2.17 trillion within the same period. The huge decline in foreign debt was a result of the substantial reduction following the pay-off of the outstanding debts owed to the London Clubs of Creditors in the first quarter of 2007. (TheCable, 2022)

Debt Profile under Yar'adua/Jonathan's Administration (2007-2011)

Under the Umar Musa Yar'Adua/Goodluck Jonathan-led government between 2007 and 2011, domestic debt of the federal government moved from N2.17 trillion to N5.62 trillion. The foreign component of the debt also increased from $2.11 billion to $3.5 billion within the period. The country's exchange rate also moved from N116.8/$1 to N156.7/$1. The combined debt profile increased from N2.42 trillion to N6.17 trillion in four years, representing a 155 percent jump. Of the debt figure, Jonathan completed the tenure from May 2010 to May 2011 after the death of Yar'Adua. The period saw a surge in the federal government's debt from N4.94 trillion to N6.17 trillion. This represents a 24.9 percent increase in one year.

Debt Profile under Jonathan's Administration (2011-2015)

At the beginning of former President Goodluck Jonathan's tenure in 2011, the federal government had an accumulated debt of N6.17 trillion. Analysis of the debt figure showed that local debt amounted to N5.62 trillion while foreign debt stood at $3.5 billion (about N548.65 billion, using the exchange rate of N156.7/$1).
By the end of 2015, the foreign debt component hit $7.3 billion, while domestic debt increased by N8.4 trillion. The country's exchange rate also stood at N197/$1.
Overall, the federal government component of the total public debt increased from N6.17 trillion in 2011 to N9.8 trillion in 2015, representing an increase of N3.63 trillion or 58.8 percent.

Debt Profile under Buhari's Administration (2015 till date)

The Budget Office's medium-term expenditure framework and fiscal strategy paper from 2015 showed that the Buhari-led administration incurred N7.63 trillion in domestic debt from June 2015 to December 2020. On external borrowings, President Buhari increased debt from $7.3 billion in 2015 to $28.57 billion as of December 2020. This means that the president incurred $21.27 billion on foreign loans to the country's debt portfolio. The country's exchange rate moved from N197 to a dollar in 2015 to N381 at the end of December 2020. Analysis of consolidated debt showed that the external debt increased by 291.37 percent while domestic debt grew by 86.31 percent in the last six years of the Buhari government. Overall, the Buhari-led government has had an accumulated debt of N17.06 trillion as of March 2021, using the N381 exchange rate. This represents a 173.2 percent increase from when he was elected president in 2015.

Increasing Public Debt Worrying

While borrowing is required to support the economy, sustainability transparency and sustainable repayment plan are crucial. Femi Oke, an economist, said Nigeria's soaring high debt profile is not good for the country. "The Nigerian government borrows in the worst possible way and in a very outdated manner. This causes a backlash to the government. Because Nigeria's debts are not linked to any assets, we just go to the treasury bill market and borrow, at any rate, that anybody wants to give you," he said.
"There are many other countries who borrow more than what Nigeria is borrowing and don't have any problem paying back. They borrow intelligently and efficiently, in a way that their debts service themselves.

"A more efficient way of borrowing is for the Federal Government to migrate all the debts to asset-linked debts. This means structuring the borrowing transaction like investments. There must be an underlying asset to which borrowers can use to recover the principal they gave the country plus profit."
Vahyala Kwaga, senior researcher and policy analyst at BudgIT, said the level of borrowing – specifically in 2021- is the highest it has been in the last six years.
"The government is borrowing more, spending more and earning less revenue. For context, the government budgeted about N5.37 trillion in revenue in 2020 but only earned a total of N3.42 trillion," Kwaga said.
"There is also no commensurate rise in revenue to counteract the continuing rise in debt servicing. A casual look at the debt servicing level from 2015 to 2020 shows that the level has steadily increased since then. "These amounts include debt servicing on interests for 'ways and means' and 'sinking fund to retire maturing Loans.'" While borrowing is required to support the economy, especially given the impact of the pandemic, the country should be more concerned about sustainability of the debts. "Debt has risen N33.1 trillion as of March 2021, an increase of 162.7% in the space of about five years.

Recently, market researchers at United Capital also expressed concern over the country's rising debt sustainability risk. "The government has historically justified its rising debt profile by the compliant debt-to-GDP ratio of less than 30.0%," the research firm said. "However, we reiterate our position that the FG's debt service cost as a percentage of revenue is a fairer reflection of the country's debt sustainability position."
At an overall public debt of N33.1 trillion ($87.24 billion), the implication remains that every Nigerian owes both local and foreign organisations N165, 500.

5.4 Summary

Nigeria's public debt has been on the rise. Despite securing debt relief during the Olusegun Obasanjo-led administration, successive governments have continued on a borrowing spree — the federal government's component of the public debt surging 658 percent to N26.9 trillion in the last 21 years. This has raised concerns among Nigerians on the debt sustainability of the country amid dwindling revenue to meet the debt obligations to creditors. As of March 2021, Nigeria's total public debt has hit N33.1 trillion ($87.24 billion) — an accumulation of borrowings from successive governments, of which most were borrowed since the return to democratic rule in 1999. The

overall public debt is the total debt accrued by federal, states, and the FCT from local and international lenders.

Of the N33.1 trillion, the federal government alone borrowed N26.91 trillion — this includes the FGN bonds, Sukuk, green bonds and Euro bonds.

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MODULE 4 BUDGETING IN THE PUBLIC SECTOR

Unit 1 Meaning, Objectives and Types of Budget

Unit Structure

1.1 Introduction
1.2 Learning Outcomes
1.3 Main Content
 1.3.1 Definition of Budget
 1.3.2 Objectives of Budget
 1.3.3 Types of Budget
1.4 Summary
1.5 References/Further Reading/Web Resources
1.6 Possible Answers to Self-Assessment Exercise(s) within the content

1.1 Introduction

Module 3 and the units contained therein dwelt extensively on public expenditure and public debt. For government to live up to its responsibilities of security provision and citizens' welfare promotion, it has to incur public expenditures. Public expenditure as well as the means of funding it are provided for in government budgets. This unit will therefore acquaint you with the concept of budget. It will seek to explain budget and lay emphasis on its application in the public sector especially as it affects developing economy like Nigeria. Budget is presented as a major financial management tool. The execution of a government's budget is carried out within an established legal framework for management of public finances as enshrined in the constitution and further elaborated in other statutes.

1.2 Learning Outcomes

At the end of this unit, you should be able to:

- Define the term 'budget' and state its objectives
- Identify objects and types of budget
- Explain the theory and practice of budgeting

1.3 Budget

1.3.1 Definition of Budget

The word 'budget' according to Adams (1998) means the money bag or the public purse which serve as a receptacle for the revenue and expenditure of a state. Budget is an official document containing financial plan of government within a fiscal year. It is an estimate of public revenue and expenditure over s stipulated period of time usually a year.

According to Chartered Institute of Management Accountants, a budget could be defined as a plan stated in quantitative monetary terms which is prepared and approved prior to a defined period of time usually showing planned income to be generated and or expenditure to be incurred during that period and capital to be employed to attain a given objective. Budget is applied by users differently. In the individual / personal, business and public sector the scenario differs. For personal budget instinct and personal idiosyncrasies come to play; while in the business sector liquidity and profitability are the guiding barometer. The public sector budget considers the availability of funds and socio-political consideration uppermost alongside regulations cum policies.

Budgeting is the most important decision making process in public institutions. It is also a jurisdiction of most important reference document. A public budget has four basic dimensions. It is a political instrument that allocates scarce public resources among the social and economic needs of the jurisdiction. It is a managerial and administrative instrument: it specifies the ways and means of providing public programs and services; it establishes the cost of programme and criteria by which these programme are evaluated for efficiency and effectiveness; it ensures that the programme will be reviewed or evaluated at least once during the budget year. It is an economic tool that can direct a jurisdiction's economic growth and development. It is an accounting instrument that holds government officials responsible for the expenditure of funds with which they have been entrusted.

1.3.2 Objectives of Budget

The goals or objectives of budget are numerous and depends on the public policy or what government wants to achieve. It includes the following:

i. To establish a workable financial plan for the period under review.
ii. To discourage wasteful expenditure of public funds
iii. To promote cost-efficiency in executing government projects
iv. To improve revenue generation capacity for the periods
v. To discourage unlawful spending of public funds
vi. To establish a goal or standard for actual measurement and comparison
vii. To establish adequate control mechanism and accountability

Self-Assessment Exercise 1

Define budget and state three objectives of budget?

1.3.3 Types of Budget

In public sector, budgets are basically classified as balanced, surplus or deficit. However, major classification of budget include line-item budgeting, performance budgeting, program budgeting and zero-based budgeting.

Basic classification of budget

Balanced budget:- this is a situation where revenue projections and expected expenditures in a budget are presumed equal.

Surplus budget:- here, there is presumed excess of revenue projections over estimated expenditure.

Deficit budget:- this is a situation where expenditure estimates in a budget outweigh the revenue projections.

Major classification of budget

- **Line-Item Budgeting**

  The line-item budget was the original budget format where each item of expense had a literal line in a ledger book. This is the Traditional or Incremental system. It classified budgetary accounts according to narrow, detailed objects of expenditure (such as motor vehicles, clerical workers or reams of paper) used within each particular agency of government, generally without reference to the ultimate purpose or objective served by the expenditure. It is useful as a record of expenditures and the criteria against which audits could measure compliance. It is widely used mostly in the local governments as their basic budget

format or as a supplement to more sophisticated formats. This is so because it offers such comprehensive details on proposed expenditures.

A major weakness of this budget is that it might allow the test to be made as to whether funds had been spent on the purposes for which they had been appropriated. Despite several budgetary innovations and experimentations, the line- item or incremental budget is the most commonly used method of budgeting. The main advantage of line-item budget is the ease of its preparation and it makes a simple comparison of performance from one fiscal period to another.

- **Performance Budgeting**

The concept of performance budgeting requires a performance measure to be stated alongside each line item, so that elementary calculations of unit cost and efficiency could be made. Performance Budgeting (PB) is a system wherein managers are provided with the flexibility to utilize organisation's resources as required, in return for their commitment to achieve certain performance results. It is a system of planning, budgeting and evaluation that emphasizes the relationship between money budgeted and result expected.

Performance Budget helps in identification of mission, goals and objectives of organisation; links strategic planning information with the budget; develop and integrate performance measures into budget; and classify expenditures into very broad areas like, personnel, operating expenses and capital outlays, rather than specific line-items.

- **Programme Budgeting**

Programme budgeting system focuses on the output services that the programme provides to its users. It also readily relates to overall organisational goals and objectives. Under this system, budget request of public agencies or departments include funding and outputs and outcomes they expect to produce as a result of that funding. The legislature establishes performance targets for outcomes and outputs in the implementing act to appropriations act. Public organ then report their actual performance in their long range programme plans and budget requests for the following fiscal year. Incentives are given when performance exceeds standard or disincentives when it falls below standards.

These incentives and disincentives can be monetary or non-monetary.

- **Zero-Based Budgeting (ZBB)**

Zero based budgeting is a cost benefit approach to budgeting which ensures value for money activities which involves the use of decision packages. It is a budget for public sector organisation in which all expenditures must be justified afresh each year and not just amounts in excess of the previous year. Under zero based budgeting, nothing is considered as sacrosanct. Every time, the managers or directors are supposed to start from scratch or writing on a "clean slate". ZBB is claimed to be a new technique of planning and decision-making. It reverses the working process of traditional budgeting. In traditional budgeting, departmental managers or directors need to justify only increases over the previous year budget. This means what has been already spent is automatically sanctioned. While in ZBB, no reference is made to the previous level of expenditure, every department function is reviewed comprehensively and all expenditures rather than only increases, are approved. ZBB is a technique, by which the budget request has to be justified in complete detail by each divisional manager or director starting from the zero-base. The zero-base is indifferent to whether the total budget is increasing or decreasing.

Self-Assessment Exercise 2

Differentiate between performance budgeting and zero-based budgeting?

1.4 Summary

Canons of public expenditure simply refers to principles guiding government in the utilization of public revenue or monies to ensure that maximum gains are derived from these expenditure. They are canons of economy, sanction, benefit, certainty, surplus, elasticity, productivity and equal distribution. In terms of classification, public expenditure are classified on the basis of their perceived functions such as administrative and general services, economic services, transfer service, and social and community services. Effect of public expenditure on the society can be seen from the perspectives of economic production, distribution, stability and development

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1.6 Possible Answers to Self-Assessment Exercise(s) within the content

Define budget and state three objectives of budget?

Possible Answers to Self-Assessment Exercise 1

Budget is an official document containing financial plan of government within a fiscal year. It is an estimate of public revenue and expenditure over s stipulated period of time usually a year.

The Objectives of budget include:

1. To establish a workable financial plan for the period under review.
2. To discourage wasteful expenditure of public funds
3. To promote cost-efficiency in executing government projects

Differentiate between performance budgeting and zero-based budgeting?

Possible Answers to Self-Assessment Exercise 2

Performance budgeting requires a performance measure to be stated alongside each line item, so that elementary calculations of unit cost and efficiency could be made. It is a system of planning, budgeting and evaluation that emphasizes the relationship between money budgeted and result expected. While Zero-based budgeting on the other hand, classify budgetary accounts according to narrow, detailed objects of expenditure (such as motor vehicles, clerical workers or reams of paper) used within each particular agency of government.

Unit 2 Budgetary Process

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Budgetary Process
 2.3.1 Budgetary Cycle
 2.3.2 Stages in the Budgetary Process
2.4 Summary
2.5 References/Further Reading/Web Resources
2.6 Possible Answers to Self-Assessment Exercise(s) within the content

2.1 Introduction

In the previous unit, you were acquainted with the meaning of budget, objectives of budget and the various types of budget. This unit will take you further into the budget concept by acquainting with the series of activities that must be carried out to evolve a budget. This unit will discuss the various stages involved in evolving a budget. There are basically four stages involved in producing a budget.

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- explain the budgetary process
- state the various stages involved in preparing a budget

2.3 Budgetary Process

2.3.1 Budgetary Cycle

Budgeting is a dynamic ongoing process. The budget process also known as budget cycle refers to various steps and stages which are undertaken by different actors from budget formulation till the budget is evaluated. A budget process is a system of rules governing decision-making at various stages that leads to a budget, from its formulation, through its legislative approval, to its execution and evaluation. This system of rules is rooted in constitutional mandates and statutory

requirements. It is generally agreed that there are at least four stages in the budget process. They are the formulation stage, authorization stage, execution stage and evaluation stage (audit).

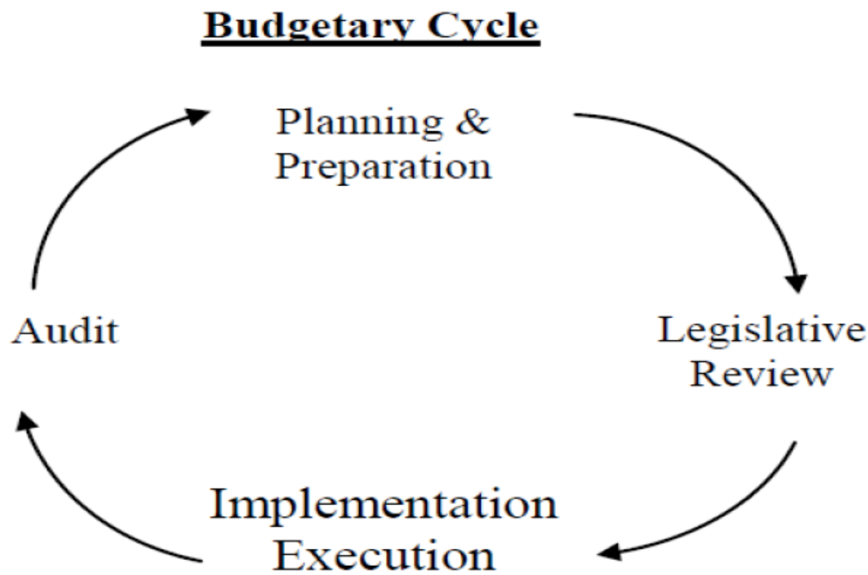

Figure 1: Budgetary Cycle

2.3.1 Stages in the Budgetary Process

Although a budget is intended to look at the future, it cannot meaningfully do this without appraising the past. The government budgetary process is briefly discussed below:

1. Planning and Preparation - This is an Executive-dominated process in most countries. Budget preparation at the state level starts with the issuance of the budget call circular from the state's budget and planning division to all ministries and state government departments. The budget call circular provides the format for budget presentation. Completed budget call circulars - are collated by the budget and planning division (ministry) and presented to the state-Executive council for approval. The budget is then presented to the Legislature.

2. Legislative Review - the Constitutions of most countries confer on their Legislatures the power of budget oversight. The power of the Legislature over budgetary matters varies considerably

from country to country and on the type of political system practiced. Premchand (1999) stated that a global look at the power of the Parliament over budgetary matters reveal five (5) types of institutional arrangements. The first group comprises the United States, Italy and to a certain extent, the Russian Federation after 1991. The institutional arrangements in these countries reveal the dominant influence of the Parliament, which has power to reject the proposals of the Executive and is empowered to craft its own legislation, which is then subjected to presidential veto or approval.

3. Execution or Implementation: Once the Legislature has voted funds, the control of expenditure shifts back to the Executive branch. Budget execution or implementation is a management process (Premchand, 1999). Burkhead (1959) believes that budget execution is an Executive responsibility. He divides budget execution techniques into two classes: those concerned with financial controls and those concerned with administrative controls. Financial controls are directed at the various accounts used to record government transactions for both receipts and expenditures. Administrative controls are concerned with executing and adjusting the budget plan that was developed and refined in the Executive branch and reviewed and approved in the legislative branch. Burkhead suggests that the goals of budget execution involve preserving legislative intent, observing financial limitations and maintaining flexibility at all levels of administration.
4. Audit: The final phase in the budget process, is however an important part of the budget cycle. The budget requires public disclosure, evaluation and auditing. The report of the auditor shows how the budget has been implemented and managed (Dye and Stapenhurst 1998). Dye and Stapenhurst (1998) argued that auditing is a function that serves accountability as it adds credibility to the assertions of the person or entity rendering account and it provides valuable insights and information to the person or entity conferring the responsibility. The agency responsible for the audit of government accounts is the Auditor-General or what is commonly referred to as 'Supreme Audit Institution' (SAI), it has the duty of overseeing the management of public funds and the quality and credibility of governments reported financial data.

Whether Supreme Audit Institutions will succeed in their assigned role of being the watchdog over financial integrity and the credibility of government reported information will depend on the following factors (Dye and Stapenhurst 1998 and Stapenhurst and Titsworth 2001):

Supportive environment - Supreme Audit Institutions require a strong Legislature, properly maintained accounts; timely submission of financial statements, an Executive branch of government that does not pay lip service to accountability among other factors to function effectively. Wrongdoing identified by the institution must be addressed seriously. Audit queries should be responded to promptly.

Clear mandate - The auditor's independence, and reporting responsibilities, the scope of audits and the entities to be audited must be clearly stated.

Independence - The Auditor-General needs the freedom to do his work and to report his findings directly to the Legislature without interference from other arms of government. Additionally, those being audited should have no influence on the choice of whom or what gets audited. The Auditor-General also needs the freedom to determine what shall be reported.

Self-Assessment Exercise

State the four basic stages involved in the budget process?

2.4 Summary

Budget process also known as budget cycle refers to various steps and stages which are undertaken by different actors from budget formulation till the budget is evaluated. A budget process is a system of rules governing the decision-making that leads to a budget, from its formulation, through its legislative approval, to its execution and evaluation. This system of rules is rooted in constitutional mandates, statutory requirements, House and Senate rules and practices (as in the federal level), and administrative directives (Bill and Keith, 2004). It is generally agreed that there are at least four stages in the budget process. They are the formulation stage, authorization stage, execution stage and evaluation stage.

2.5 References/Further Reading /Web Respurces

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2.6 Possible Answers to Self-Assessment Exercise(s) within the content

State the four basic stages involved in the budget process?

Possible Answers to Self-Assessment Exercise

i. Budget formulation stage
ii. Legislative scrutiny and approval
iii. Implementation stage
iv. Evaluation stage (Audit)

Unit 3 Budgeting in the Public Sector

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Budgeting in the Public Sector
    3.3.1 Budget process at the Federal Level
    3.3.2 Budget process at the State Level
    3.3.3 Budget process at the Local Level
3.4 Summary
3.5 References/Further Reading/Web Respurces
3.6 Possible Answers to Self-Assessment Exercise(s) within the content

3.1 Introduction

In the previous unit, you were taken through the series of activities that must be carried out to evolve a budget which basically involves budget formulation, budget authorization, budget execution and finally budget evaluation or audit. This unit will however discuss the budgeting process at each level of government. That is federal, state and local government.

3.2 Learning Outcomes

By the end of this unit, you will be able to:

- explain the budget process at the federal level
- explain the budget process at the state level
- explain the budget process at the local level

3.3 Budgeting in the Public Sector

Budget process also known as budget cycle refers to various steps and stages which are undertaken by different actors from budget formulation till the budget is evaluated. A budget process is a system of rules governing decision-making at various stages that leads to a budget, from its formulation, through its legislative approval, to its execution and evaluation. This system of rules is rooted in constitutional mandates,

statutory requirements, House and Senate rules and practices (as in the federal level), and administrative directives (Bill and Keith, 2004).

3.3.1 Budget Process at the Federal Level

In Nigeria, the preparation of the budget is a shared responsibility of the Executive and Legislative arm of the Federal Government. The budget, which is officially referred to as the Appropriation Act, is introduced by the Executive, approved by the Legislature and signed into law by the President. A summary of the Nigerian budget process is set forth below.

a. Budget Formulation

The Budget Office of the Ministry of Finance develops the budget in accordance with the Federal Government's fiscal policy. The Budget Office meets early in the fiscal year with key revenue generating agencies (including the Federal Inland Revenue Service, Nigerian Customs Service and the NNPC) as well as key economic agencies (including NPC, NBS and CBN) to assess and determine trends in revenue performance and macroeconomic indicators and the implication of such trends for the next three fiscal years. This discussion leads to the preparation of a Medium-Term Revenue Framework ("MTRF") pursuant to which projected revenue from various oil and non-oil sources is determined over the medium-term. Following this determination with respect to revenue, the Medium-Term Expenditure Framework ("MTEF") is developed outlining key areas of expenditure (statutory transfers, debt service, MDAs' Expenditure) as well as the projected fiscal balance. If this fiscal balance is a deficit, sources of financing this deficit are also considered. MDAs' expenditures comprise both capital and recurrent expenditures. The MTEF is further developed into a formal Medium-Term Expenditure Framework Report, which includes the Fiscal Strategy Paper and MDAs expenditure ceilings.

Once the MTEF, Fiscal Strategy Paper and MDAs' expenditure ceilings have been approved by the Federal Executive Council, the Budget Office under the supervision of the Minister of Finance, issues a "Call Circular". The Call Circular instructs the MDAs to allocate their allotted capital expenditure ceilings across their existing and new projects, programmes and other initiatives. MDAs are also required to submit estimates of their recurrent expenditure requirements for personnel costs and overhead. The Budget Office evaluates and consolidates the

submissions of the various MDAs and prepares the draft budget. This process most times, takes place in August.

The draft budget is presented by the Minister of Finance to the President for approval. The approved budget, together with supporting documents, is formally presented by the President to the National Assembly for consideration and appropriation, typically at a joint session of the Senate and the House of Representatives.

b. Legislative Scrutiny and Approval

The budget is considered separately by the both chambers of the National Assembly in accordance with the legislative practice and procedures. The two houses harmonize their drafts and the recommendations of the various committees are considered and collated with the oversight of the MDAs. The harmonized budget is approved separately by each chamber of the National Assembly, after which it is presented as the Appropriation Bill to the President for assent. Once the President assents to the Appropriation Bill, it becomes an Act of parliament passed into law. It should however be noted that during the deliberation of the Appropriation Bill in both Chambers of the National Assembly, all the relevant Committees in both Houses review and recommend changes to various segments of the budget.

During the process, there is usually “horse trading” between the executive and the legislature looking for a common ground for speedy passage of the Appropriation Bill. Various parameters used in drafting the budget are debated and in some cases adjusted by the relevant Committees in the House of Representatives, particularly by the Finance, Appropriation, National Planning and Legislative Budget during their deliberation on the Medium Term Expenditure Framework submitted by the Executive to the National Assembly. Their decisions guide the general debate in the plenary who also adjust other benchmarks such as the oil price benchmark, the production of crude oil, and the size of funding for oil and gas production in the joint venture agreement, as well as the level of debt repayments to be made in any fiscal year. After an exhaustive deliberations culminating in series of adjustments, the budget is passed by the legislature.

c. Budget Implementation

The implementation of the budget is carried out by the various Ministries, Department, and Agencies (MDAs) of the federal government. Funds for capital projects are released on a quarterly basis to the relevant spending MDAs in line with what is allocated to them in the budget. It should be noted that the Federal Ministry of Finance instituted since 2005, a cash Management Committee, that ensures funds availability for the smooth financing of government budget. This structure reduces discretionary borrowing from the overdraft (Ways and Means) account of the Central Bank and avoids delays towards completing capital projects.

d. Monitoring and Evaluation

The oversight of budget implementation is the final stage of the budget process. The monitoring is done by the Ministry of Finance, the National Planning Commission (NPC), the National Assembly, the National Economic Intelligence Agency (NEIA), the Presidential Monitoring Committee (PBMC), the Office of the Auditor General of the Federation and the Accountant General of the Federation. Actual inspection of the capital projects are carried by these agencies in various capacities, predominant among them is the Ministry of Finance; the National Planning Commission and National Assembly through its think-tank – the Policy Analysis and Research Project (PARP) which is now, National Institute for Legislative Studies (NILS). While copies of the budget Implementation reports are on the website of the Federal Ministry of Finance, such reports from the PARP now NILS is made available to the National Assembly presiding officers and relevant Committees.

Self-Assessment Exercise 1

State the four basic stages involved in the budget process?

3.3.2 Budget process at the State Level

The procedure for the preparation of the state budget is similar to the procedure enhanced by the constitution for the preparation of the federal government budget. The commencement of the budget requires any government department to make projection for its service incorporating the capital and recurrent estimates for the next financial year.

The capital expenditure estimates are for expenditure on capital projects such as construction of roads, dams etc. the recurrent expenditure estimates are meant for government operational services personnel emolument, maintenance costs, repairs of machinery etc. Next is the transfer of budgets of various departments to the ministry of finance for their perusal, where the department heads have to appear to defend the estimates. The defended estimates prepared by the departments, titled Appropriation bill are sent to the state house of assembly. The appropriation bill is then published in the gazette for public comments and debate. The governor is then expected to go and formally present the budget speech to the house of assembly after the appropriation bill would have been introduced in the house. The budget proposal goes through the readings, committee stage and debate in the course of the normal process of legislative law making before it is pass into law i.e. become appropriation act.

3.3.3 Budget process at the Local Level

The procedure for the preparation of the annual local government (budget) estimate is exposed in chapter 3 of the Financial Memoranda. Especially 3.2 provide that the local government executive committee is to issue a circular calling for the preparation by local government departments estimates for the coming financial year. The financial memoranda also states that the call circular for the preparation of budgetary estimates be issued out by June 1st of every year, so as to reach each local government department in good time for the commencement of the budgetary process. The treasurer, as provided by section 3.4 of the Financial Memoranda, upon the receipt of the executive committees call circular and not less than 10th of June shall issue an estimate call circular to heads of department. Heads of department will prepare the estimates of the circular supported by full explanation notes and shall be forwarded to the treasurer by July 10th. The treasurer will then consolidate everything and submit to the executive committee through the secretary. The treasurer shall also prepare a report on general financial applications of the estimates, Proposals and the effect they have on the financial position of the local government, to accompany the estimate proposals.

3.3.4 Challenges with Budgeting Process in Nigeria

The budget process in Nigeria is characterized by some challenges such as:

a. *Over bloated nature of the budget*: The partial funding of projects across the country and the high risk of these projects being abandoned in their partial state. In Nigeria, where some projects are ongoing and poorly funded, new projects are introduced, thereby increasing the risk of neglect, while some projects are poorly maintained through the various stages of completion; some are approved without detailed costing and engineering design.
b. *Weak reporting culture of MDAs*: The MDAs reports do not adequately reflect projects that are ongoing as various stages of implementation are not stated. The MDAs do not adhere to proper monitoring and evaluation technique on their projects and the large number of MDAs projects makes it difficult to individually visit each project.
c. *Unplanned Size of the recurrent expenditure*: Increases in the wage bill and in allocation to certain MDAs have resulted in bloated budget. This has made the budget skewed towards the recurrent spending white capital expenditure remained inadequate.
d. *The nature of the budget process*: The budget is required to be reviewed at different stages with the possibilities of delays, like the drafting stage, legislative approval stage, implementation stage, and monitoring and evaluation stage.

Self-Assessment Exercise 2

Describe the budget process at the state level?

3.4 Summary

Budget process also known as budget cycle refers to various steps and stages which are undertaken by different actors from budget formulation till the budget is evaluated. A budget process is a system of rules governing the decision-making that leads to a budget, from its formulation, through its legislative approval, to its execution and evaluation. This system of rules is rooted in constitutional mandates, statutory requirements, House and Senate rules and practices (as in the

federal level), and administrative directives (Bill and Keith, 2004). It is generally agreed that there are at least four stages in the budget process. They are the formulation stage, authorization stage, execution stage and evaluation stage.

3.5 References/Further Reading/Web Resources

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3.6 Possible Answers to Self-Assessment Exercise(s) within the Content

State the four basic stages involved in the budget process?

Possible Answers to Self-Assessment Exercise 1

The four basic stages involved in the budget processes ar:

i. Budget formulation stage
ii. Legislative scrutiny and approval
iii. Implementation stage
iv. Evaluation stage

Describe the budget process at the state level?

Possible Answers to Self-Assessment Exercise 2

The commencement of the budget requires any government department to make projection for its service incorporating the capital and recurrent estimates for the next financial year. Next is the transfer of budgets of various departments to the ministry of finance for their perusal, where the department heads have to appear to defend the estimates. The defended estimates prepared by the departments, titled Appropriation bill are sent to the state house of assembly. The appropriation bill is then published in the gazette for public comments and debate. The budget proposal goes through the readings, committee stage and debate in the course of the normal process of legislative law making before it is pass into law i.e. become appropriation act.

Unit 4 Budgetary Control in the Public Sector

Unit Structure

4.1 Introduction
4.2 Learning Outcomes
4.3 Budgetary Control in the Public Sector
    4.3.1 Concept of Budgetary Control
    4.3.2 Budgetary Control in the Public Sector
    4.3.3 Objectives of Budgetary Control
4.4 Summary
4.5 References/Further Reading/Web Resources
4.6 Possible Answers to Self-Assessment Exercise(s) within the content

4.1 Introduction

Having looked at the budget process and budgetary procedures as practiced in the public sector in the previous unit, this unit will take you further into the budget process by acquainting you with the various control measures available to ensure that the budgetary procedures as provided in different statutes are adhered to. The unit will be concerned with the concept of budgetary control, budgetary control in the public sector and objectives of budgetary control.

4.2 Learning Outcomes

By the end of this unit, you will be able to:

- define budgetary control
- explain budgetary control in the public sector
- state objectives of budgetary control in the public sector

4.3 Budgetary Control in the Public Sector

Budgeting is the process of demanding funds by the president from the National Assembly in support of the programmed activities. The budget needs to be controlled because once approved, it becomes the operating plan for the ministries and departments concerned.

4.3.1 Concept of Budgetary Control

Budgetary control is a system of controlling costs which include the preparation of budgets. Budgeting is thus only a part of the budgetary control. Budgetary control is defined by Chartered Institute of Management Accountants as "the establishment of the budgets relating to the responsibilities of the executive to meet the objective if an organisation and the continuous comparison of actual with budgeted estimates so that if remedial is necessary it may be taken at an early stage".

It can also be defined as "a continuous process which reviews and adjusts budgetary targets during the financial year and produces a control mechanism to hold budget holder to account". This means that budgetary control is a technique encompassing the entire process starting from the preparation of the budget or the action plan, covering monitoring and review culminating in corrective action.

The focus of budgetary control is to:

i. establish target of performance/budget
ii. record the actual performance
iii. compare the actual performance with the budgeted
iv. establish the differences and analyze the reason
v. respond immediately, for corrective actions

4.3.2 Budgetary Control in the Public Sector

Budget and Budgetary Control is the backbone of any financial control system. The emphasis of financial control was in the private sector. Recently, the general attitude in the public sector has geared toward financial control because of the reality of scarce public resources which need proper management even at the macro-level. Nowadays, Public accounts Committees have been formed at the ministerial level and other agencies of government. Government prepare master budget which is supported by budget classification as; revenue, capital expenditure and cash budget. The budget targets are conventionally evolved not by consensus but from top to bottom. The incremental approach to budgeting overshadows the zero-base and programme-cum-performance approaches.

Costing and Cost Control in most of the public sector enterprises is not given appropriate attention. They pay lip service to cost and maintain no standards. Cost reduction drives are seldom undertaken. The concept of just-time-inventory is not practiced in public sector undertakings.

Variance analysis is not a regular feature and the resultant effect of such analysis is not effectively utilized. Raw material consumption norms and optimum inventory limits have been developed by some of them. To be effective in this, extensive costing systems and appropriate procedure need be in place for their operation.

Internal audit is an important component of financial controls. It has been given adequate attention in public enterprise's management in terms of its location, organisation, empowerment, resource allocation, staffing and performance. It is usually headed by an executive at the middle or senior level.

Budgetary control in the public sector involves the following steps:

a. Preparation of a budget or a detailed action plan.
b. Identification· of responsibility centers in the organisation to carry out specific activities or operations.
c. Adaptation of mutually agreed targets of achievement or output to serve as milestones or other indicators of progress
d. A system for periodical monitoring of performance or activities of all responsibility centers involved.
e. Careful comparison of the actual performance and outcomes with *the* corresponding parts of the plan
f. Assessment of the deviations and variances in actual performance or activities in relation to the plan and identification of the causes of such deviations
g. Initiation of corrective action aimed at ensuring that the planned activities and actions are adhered to accordingly
h. It became obvious from the above description of the term "budgetary control", that it is a technique encompassing the entire process starting the process of preparation of the budget or action plan, covering, .monitoring and review including corrective actions

4.3.3 Objectives of Budgetary Control

The following are the objectives of budgetary control.

1. To plan – a budget provides a detailed plan of action for activities over a definite period of time. By planning, many problems are anticipated long before they arrive and solutions sought through careful study. Example relates to government's plan for infrastructural development in a particular year for an area that is in need.

2. To coordinate – budgeting aids managers in coordinating their efforts so that objectives of the organisation are harmonised with the objectives of its constituents. This will help in achieving result. Like the different sector need to be achieved and prioritised in the light of the scarce resources.
3. To communicate – a budget is a communication device. The approved budget indicating the details of planned activities assist in communicating the plans. The copies are distributed to the different ministries, extra ministerial departments and agencies.
4. To control – the budget ensures that plans and objectives are being achieved. Control in budgeting may be synthesised effort aimed at keeping management informed of what pre-determined plans will be achieved. Control comes through variance analysis and reporting
5. To motivate – careful budgeting control motivates the human resource of the organisation.

Functions of Budgeting Control

Its main purpose is to enable management to plan and carry out projects; operations or activities with efficiency and effectiveness in the use of resources. The concept of control in budgeting cannot be over emphasized particularly in terms of cost efficiency and cost effectiveness. The concept encompasses the following:

- Fund Control
- Expenditure Control
- Revenue Control
- Payment or Disbursement Control
- Cash Control
- Cost Control
- Salary/Payroll Control

Advantages of budgetary control

i. Planning- it provides a well-organised plan based on facts. It provides definite objectives with regard to future operation.
ii. Control- it enables management to control each function, sector, ministry or department in order to achieve the best possible result.
iii. Coordination- it promotes and encourages coordination between departments of activities for the attainment of the overall good of the organisation/institution
iv. Cost consciousness- it makes management to become more cost conscious and eliminate waste and inefficiency in its operations

v. Management by exception- it is a time saving mechanism as attention is directed to areas of more pressing needs.
vi. Management Responsibility- it enables each manager to assume responsibility which is clearly established
vii. Measurement of performance- it provides a means of measuring the performance of individual managers and the various cost centers or departments by comparing targets against the performance of the manager can be assessed.
Viii. Communication and motivation- it involves communication between top management and lower levels on how to attain the objectives. This motivates managers to achieve the target set.
ix. Prevention of waste- it prevents waste of physical resources such as labour, equipment, machinery etc. Duplication of efforts is avoided as the most efficient and effective use of these resources is expressed in the budget
x. Authorization and delegation- it explicitly and expressly authorizes the budget's policy thrust on approval of the master budget of the organ be it private or public. By the acceptance of the budget by the sectors concerned, responsibility for executing the policy can be delegated to desk officers.

Self-Assessment Exercise 1

State four (4) functions of the budgetary process?

4.4 Summary

Budgetary Control is explained as the establishment of the budgets relating to the responsibilities of the executive to meet the objective if an organisation and the continuous comparison of actual with budgeted estimates so that if remedial is necessary it may be taken at an early stage".

4.5 References/Further Reading/Web Resources

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4.6 Possible Answers to Self-Assessment Exercise(s) within the Content

State four ($) functions of the budgetary process?

Possible Answers to Self-Assessment Exercise 1

i. Fund Control
ii. Expenditure Control
iii. Revenue Control
iv. Payment or Disbursement Control
v. Cash Control

Unit 5 Concept of Transparency and Accountability

Unit Structure

5.1 Introduction
5.2 Learning Outcomes
5.3 Concept of Transparency and Accountability
    51.3.1 Different Dimensions of Transparency and Accountability
    5.3.2 Issues of Transparency and Accountability in the Public Sector
5.4 Summary
5.5 References/Further ReadingWeb Resources
5.6 Possible Answers to Self-Assessment Exercise(s) within the content

5.1 Introduction

This unit will acquaint you with issues of transparency and accountability which has largely and unfortunately eluded the Nigerian leadership both in the public and private sectors of the socio-economic and political systems. Firstly, you will be introduced to what transparency and accountability constitute. Having clearly conceptualized these siamese-twin like concepts, efforts will then be made to examine the different dimensions of accountabilities ranging from political, legal, financial, ombudsman and public opinion inclusive as avenues constituting accountabilities.

5.2 Learning Outcomes

By the end of this unit, you will be able to:

- define the concept ‘transparency’
- define the concept ‘accountability’
- state the various dimensions of transparency and accountability in the public sector

5.3 Concepts of Transparency and Accountability

The concepts of Transparency and Accountability have become common parlance within the Nigerian political economy. These twin concepts are expected behaviour patterns of people serving in public and private organisations. It is · expected that members of both organisations should be transparent and accountable in their various roles, irrespective of their ranks and files. What then do these two concepts really mean? We shall now briefly examine each of them

Concept of transparency

Ordinarily, when something is transparent, it means it can easily be seen through without any difficulty. Transparent behaviour therefore, connotes honesty, probity, straight forwardness and like meanings in executing or carrying out ones responsibilities in any organisation or society.

Concept of Accountability

Generally refers to the ability to furnish satisfactory analyses and explanations of one's actions in the process of discharging one's responsibilities at all levels, whether technical, administrative, political, financial or otherwise. A number of scholars have attempted to conceptualise accountability. For example, Peter Bird explains accountability in the following manner:

Every steward is held accountable to the person or body which entrusted resources to him, whether the latter is a 'superior steward or the ultimate owner Accountability places two obligations upon a steward; he must render an account of his dealing with the stewardship resources, and then, he must submit to an examination (usually known as an audit) of that account by or on behalf of the person *or* body to whom he is accountable. This means that he must not only allow the audit to take place, but he must provide the evidence from which the auditor can verify the account rendered. This double duty of stewards, including an audit has a long and continuous history. The need for independent check or control (inspection or audit) lies deep in human history.

In a similar vein, Etzioni, (1975) associated accountability with three different meanings:

1. Greater responsibility to elected superiors;
2. Greater responsiveness to community groups; and

3. Greater commitment to "values and higher standards of morality

Apart from traditional notion of stewardship report by official in respect of their responsibilities, other scholars consider that operational responsibilities should also be related to accountability. For example, Oshisami (1992) emphasized two key elements, that of Efficiency in accountability and Effectiveness in accountability.

Efficiency in Accountability

Efficiency normally will connote improvement in the desired results. This then implies that managers and executives should use the resources within their disposals towards the improvement of their outputs. Few questions then arise such as, firstly whether the goods and services rendered are really needed Secondly, whether the costs incurred or expenditure made on such goods and services are reasonable. Thirdly, whether there are adequate safeguards and care over resources or assets. Fourthly, whether revenue are adequate for goods sold or services provided and whether there are wastages in providing the necessary goods and services. Efforts to provide answers to provide answers to these questions would contribute in no small measure to accountability.

Effectiveness in Accountability

Effectiveness ordinarily connotes the act of achieving the desired results in a particular endeavour. In ·this wise, managers and executive should be accountable in the achievement of the desired results as well as goals and objectives of an organisation. Effectiveness in accountability could then raise a number of questions such as:

(a) Is the organisational expenditure justified by the resultant results?
(b) Are there alternatives which are less costly?
(c) Can the quantity of services or goods delivered be increased without additional cost?

These and some other relevant questions are the issues which accountability regarding effectiveness will likely address. All said and done, the drive for accountability should obviously begin with the pursuit for transparency or probity and integrity on the part of managers and executives in different organisations be they in public or private sector.

5.3.2 Different Dimensions of Transparency and Accountability

Dimension or Patterns of Accountability

There are two broad dimensions of accountability measures. They are, internal and external dimensions. We shall discuss each of these dimensions one after the other.
Internal dimension of accountability refers to the internal norms, certain professional ethics and pragmatic guidelines that guide the managers and the executives in their day to day functions within the governmental administrative system. In the Nigeria Public Service, the General Services Rules and Regulations formerly called the General Order or more appropriately Nigeria Civil Service Rules, financial. Regulations, periodic circulars or circular letters issued by different ministries when necessary, all constitute sources of internal accountability. The Civil Service Rules and the Financial Regulations however remains the major sources of accountability. The Nigerian Civil Service Rules and Regulations spell out precisely different rules and regulations guiding different level of officers, executives and administrators in the execution of their various responsibilities.
The second major source of internal accountability is the Financial Regulations along with periodic financial circulars or circular letters issued by the Ministry of Finance. The Financial Regulations are meant to establish standards of financial management with a view to ensuring a high degree of uniformity and maintaining judicious expenditure of government resources.

The Financial Regulations

This is an important document meant to establish standards of financial management with a view to ensuring high degree of uniformity and maintaining judicious expenditure of government resources.

The Financial Regulation (FR) cover among other provisions the duties of specific government officials in financial matters, methods of accounting, the control of revenue collection, vote control, payment procedures, security arrangement for public money, different types of imprest, advances, procurement and internal audit. Circulars issued by the Ministry of Finance are general intended to guide the day to day operations of government in respect to financial matters.

The provision of FR if adhered to, suggests these provisions could enhance the concept of transparency and accountability in the Nigerian Public Service.

External Dimension of Accountability

There are five (5) major dimension of accountability outside the internal ones which is within the public service of the country. They are:

i. Political Accountability
ii. Legal Accountability
iii. Financial Accountability
iv. Ombudsman Institution or Public Complaints Institution as a form of accountability and public opinion as a means of accountability

Political Accountability

(i) The political office holder of any rank should be accountable to the electorate (the people) he has been elected to serve. This is to obtainable during periodic elections in which the people decide whether to retain or to throw out the incumbent political executives by refusing to vote for such incumbent based on his/her performance while in office. The constitution of the · land provides for checks and balances between the executive and the legislature. The legislature watches and constraints the executive through legislative process while the executive through its veto power could check the excesses of the legislature.
The Judiciary then acts as a sort of referee between the executive and the legislature through its power of establishing the constitutionality or otherwise of any action of either arms of government. This type of accountability can only take place in a democratic government and not during a military regime where dictatorship is the order of the day and accountability IS thrown into the dustbin.

The Administrative Class

The administrative class can be made accountable for their actions through the executive, legislative and judiciary controls. Other sources of control over this class could include the Nigerian Public Complaints Commission and the mass media.

Legal Accountability

Legal accountability is usually enforced through the courts, tribunals and other quasi-judicial institutions. In developed countries of the world such as Britain, France, U.S.A and others, they ensure that anyone whose conduct is questionable in one form or the other is subjected to legal accountability regardless of the person's political status in the society. In Nigeria, legal accountability is sometimes vague and selectively enforced. Some persons are deemed to be above the law based on their societal status and affinity with persons in power.

Financial Accountability

Financial Accountability according to Burkhead (1965) means legal liability_ the establishment of the pattern of control over the receipts and expenditures that permits a determination either by the executive or by legislature (or both bodies) that public monies have been used for the public purposes.

Constitutional Provision over the Control of Public Funds

The 1999 constitution had made provisions concerning financial accountability in the following way:
The responsibility for· approving federal government expenditure is placed in the National Assembly section 80 (2) and (3) of the 1999 constitution specifically state that~ No moneys shall be withdrawn from the Consolidated. Revenue Fund except to meet expenditure that is charged upon the fund by this constitution or where the issue of those moneys has been authorized by an Appropriation Act, Supplementary Appropriation Act or an Act passed in pursuance of section 81 of this constitution.

In the same vein, according to section 81 (1) the constitution states that; The president shall cause to be prepared and laid before each House of the National Assembly at any time in each financial year estimates of the revenues and expenditure of the federation for the following financial years." · The appointment of the Auditor-general and the power vested in him or her is derived from Section 85 (5) of the 1999 constitution which states that:

a. The Auditor-General shall, within ninety days of receipt of the Accountant-General's financial statement, submit his reports under his section to each House of the National Assembly and each House shall cause the reports to be considered by a

committee of the House of the National Assembly responsible for public accounts".

b. The Public Accounts Committee (PAC) constitute another source of accountability. The PAC is a Committee of the legislature on accounting matters. The idea of the PAC was imported to Nigeria from Britain where it has served, as one of Parliament's instrument of controlling public expenditure. The PAC is responsible to examine the report of the Auditor-General. Both Committees have the right to raise issues with the executive branch of government regarding, finances of the state and bow they are expended. From the provision provided by the 1999 constitution, it should be noted that:

(i) It is the duty of the Accountant-General of the Federation to prepare the financial statements and annual accounts of government and to present same to the Auditor-General for auditing.

(ii) The Auditor-General in tum shall audit these accounts within ninety (90) days of the receipt of the accounts.

(iii) The report of the Auditor-General shall be presented to the National Assembly which shall appoint a Public Accounts Committee (PAC) to consider and report on the accounts to the General House.

Ombudsman or Public Complaints Institution

Nigeria happened to be one of the few African states that have established Ombudsman Institute to provide additional avenue for citizens seeking protection from administrative injustices and source of accountability from administrators who might have taken undue advantage in exercising their administrative responsibilities on behalf of the citizens. Perhaps, many Nigerians who might have felt aggrieved by administrators may be unaware of the existence of this institution and the role it could play in dealing with their complaints. The guts to lay their complaints to this institution may also serve as another factor hindering citizens from taking advantage of the services provided by the institution of the Ombudsman.

5.4 Summary

The concepts of Transparency and Accountability have become common parlance within the Nigerian political economy. These twin concepts are expected behaviour patterns of people serving in public and private organisations. It is expected that members of both organisations

should be transparent and accountable in their various roles, irrespective of their ranks and files. Transparency Ordinarily means when something is transparent, it means it can easily be seen through without any difficulty. Transparent behaviour therefore, connotes honesty, probity, straight forwardness and like meanings in executing or carrying out ones responsibilities in any organisation or society. Accountability on the other hand, refers to the ability to furnish satisfactory analyses and explanations of one's actions in the process of discharging one's responsibilities at all levels, whether technical, administrative, political, financial or otherwise. There are two broad dimensions of accountability measures. They are, internal and external dimensions. There are five (5) major dimension of accountability outside the internal ones which are: Political Accountability, Legal Accountability, Financial Accountability and Ombudsman Institution or Public Complaints Institution.

5.5 References/Further Reading/Web Resources

Benjamin, E. & Martin, N. (2012). *Public finance administration in Nigeria. Cases and issues*. Onitsha: Chambers Books Ltd

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Unit 6 Multi-National Institutions and Public Finance

Unit Structure

6.1 Introduction
6.2 Learning Outcomes
6.3 Multi-National Institutions and Public Finance
 6.3.1 Multi-National Institutions
 6.3.2 Multi-National Functions
6.4 Summary
6.5 References/Further Reading/Web Resources
6.6 Possible Answers to Self-Assessment Exercise(s) within the content

6.1 Introduction

In this unit, you would be introduced to the role of multi-lateral institutions that help in underwriting external debt of nations in international trade and enhancing the expansion and development of the respective economies thereof. Their functions with regard to lending/borrowing, especially, to developing countries will be discussed.

6.2 Learning Outcomes

By the end of this unit, you will be able to:

- identify different multi-national institutions
- state the functions of multi-national institutions

6.3 Multi-National Institutions and Public Finance

6.3.1 Multi-National Institutions

Here, let us consider the following.

A. World Bank (International Reconstruction and Development) Bank for

The World Bank is a multi-lateral institution which provides loans to needy counties. It was established as International Bank

Reconstruction and Development (IBRD) in 1945 under the Bretton Wood Agreement of 1944, after the World War II, to mid-wife reconstruction and development from Wartime to peace time.

Functions of World Bank

1. To partake in the development of territories of it members by facilitating the investment of capital for productive purpose and to that of less developed countries.
2. To promote private foreign investment by means of guarantees on participation in loans and other investment made by private investors
3. To promote long-range balance growth of international trade and maintenance of equilibrium in the balance of payments of member countries by encouraging international investment for the development of their productive resources.
4. To arrange the loans made or guaranteed by it in relation to international loans through other channels so that more useful and urgent small and large projects are prioritised.

The memberships consist of financial members of International Monetary Fund (IMF). If a country resigns it shares, the assets and liabilities of the bank as at that time.

Borrowing and Lending Activities of the World Bank

The World Bank capital is subscribed by members. It finances its lending operations from its medium and long-term borrowings in the international capital markets and Currency Swap Agreements (CSA). In these agreements, the proceeds of a borrowing country are converted into a different currency and simultaneously a forward exchange agreement is executed providing for schedule of future exchange of two currencies in order to recover the currency converted. The Bank's mode of lending to member countries takes any of these ways.

1. Marketing or participating loans out of its own funds;
2. Making or participating in direct loans out of funds raised in the market of a member or otherwise borrowed from the bank;
3. Guaranteeing in whole or in part loans made by private investors through the usual investment channels.

The Bank guarantees, participates in or makes loans to its members on different conditions as follows.

1. If it is satisfied that in the prevailing market conditions, the borrowers would be unable to obtain the loan under conditions which the Bank presumes is reasonable to the borrowers.
2. Loans are for specific developmental projects or deemed to be so implied.
3. If the member in whose territory the project is located is not itself the borrower, the member or its central bank fully guaranteed the repayment of the principal, the payment of interest and other charges on the loan.
4. The project in question has been duly recommended by a competent committee in the form of a written report after a careful appraisal of the proposal.
5. The borrower or the guarantor is in a position to meet its obligation under the loan.

The World Bank Facilities to member countries varies according to needs and circumstances.
Structural Action Programme (SAP)- Started in 1983 to strengthen World Bank's ability to assist member countries in adjusting to current economic environmental realities with the following elements:

- An expansion of lending for high-priority operations that support structural adjustment, policy changes, production for export, optimal use of existing capacity and maintenance of crucial infrastructure
- Accelerated disbursements under existing and new investment commitments to ensure timely implementation of nigh priority projects
- Expanded advisory services on the design and implementation of appropriate policies
- Enlisting familiar efforts by other donors for fast disbursing assistance in support of programme of the Bank and International Monetary Fund (IMF).

Structural Adjustment Facility (SAF) – Introduced in 1985 to borrowing countries in order to reduce their balance of payments deficits while maintaining their economic growth potency. The funds are used to finance general imports with a few exceptions of luxury military imports. They are released based on stiff conditions of the Bank and it spans between 5 to 7 years.

Enhanced Structural Adjustment Facility (ESAF) –It was set up to increase the availability of concession resources to low-income member countries totaling Special Drawing Right (SDR) 6 billion financed by special loans and contribution from developed and Oil Producing and Exporting Countries. Like others it helps in addressing positively the

borrowing nation balance of payments problems and enhances growth and development.

Self-Assessment Exercise 1

Name the facilities provided by the World Bank to member countries.

B. International Monetary Fund (IMF)

The IMF is one of the multi-lateral institutions; an affiliate of the World Bank, involved in the act of providing loans for needy nations. It is established by different countries after the World War II with the objective of providing exchange stability throughout the world and increasing liquidity to enhance balanced multilateral trade through the cooperation of the member nations.

Objectives of IMF

The main purposes of the IMF, summarised in the article of agreement, are as follows.

1. To promote international monetary cooperation through a permanent institution that provides the machinery for consultation and collaboration on international monetary problems.
2. To facilitate the expansion and balanced growth of international trade and to contribute to the promotion and maintenance of high levels of employment and real income and to the development of productive resources of all members economy.
3. To promote exchange stability, to maintain orderly exchange arranges among member and to avoid competitive exchange depreciations.
4. To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade.
5. To give confidence to members by the Fund's resources available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures inimical to national or international prosperity.
6. In accordance with the above, to shorten the duration and lesson, the degree of disequilibria in the international balance of payments of members.

C. International Development Association (IDA)

The International Development Association (IDA) was established in 1960 as an affiliate to the World Bank. There are many projects such as irrigation, railway construction, education, public health, housing etc. in under-developing countries which are vital to general economic development, with long gestation period and insufficient yield returns to meet the amortization charges. The IDA was established to supplement the World Bank's development assistance and to make available loans to the developing countries on soft terms and for long period. That is, IDA is 'Soft Loan Window of the World Bank.'

Objectives of IDA

1. To provide development finance to the less developed counties on easy and flexible terms
2. To promote economic development, increase productivity and improve the standard of living in the developing countries
3. To supplement the objectives and activities of the World Bank

Self-Assessment Exercise 2

List the objectives of International Development Association

D. International Financial Corporation (IFC)

International Financial Corporation (IFC) was established in July 1956 as an affiliate of the World Bank to provide finance to the private sector. You may note that, conventionally, World Bank loans are to governments of the member countries; or it provides loan capital to the private enterprises with the guarantee of the member governments. Moreover, the World Bank does not offer risk capital. The IFC was with specific purpose of providing risk capital to the private sector/enterprises in the developing countries without government guarantee.

IFC investment policy

The main features of the IFC investment policy are as follows.

1. It considers predominantly industrial enterprises which contribute to economic development of the country.
2. The project to be financed must be in the productive, private sector.
3. The IFC affirm that the enterprise has experience and competent management.

4. The loan must not be more than half of the capital needed for the enterprise.
5. The minimum investment to be made by the IFC to a single enterprise is fixed at $100,000:00 with no upper limit.
6. The rate of interest for the loan is determined by mutual negotiation, depending on the degree of risk involved and other terms of investment.
7. The loans are disbursed in lump-sum or in installments and are repayable in a period of 5 to 15 years.

E. Parish Club and London Club

These are some of the sources of external debt contraction.

- **Paris club of creditor**
  This consists of mainly credit guaranteed by government. It is made up of United Kingdom, Federal Republic Government, The United States, Canada and France, who guarantee the export activities of their nationals through their official export credit agencies. If the recipient nation's government is unable to pay the foreign exchange equivalent of the domestic currency cover paid by the importer, it becomes public debt owned to the creditor nations. The Club commenced meeting in Paris in 1956.

- **London club of creditors**
  This consists of mainly commercial banks in industrial countries where credit are extended by commercial banks to citizens of debtor countries, largely un-insured and un-guaranteed. It was in 1976 the first meeting was held in London.

F. African Development Bank (ADB)

The African Development Bank was established under the auspices of Economic Commission for Africa (ECA) in 1966.
Functions (as express in the statute establishing ADB) are as follows.

1. Use the resources at its disposal for financing of investment projects relating to the economic and social development of its members
2. Undertake and participate in the selection, study and preparation of projects enterprises and activities contributing to such development
3. Mobilise both within Africa and outside Africa, resources for the financing of such investment programme
4. Promote investment in Africa of public and private capital in projects or programme.

5. Provide such technical assistance as may be needed in Africa for the study, preparation, financing and execution of development project or programme
6. Undertake such other activities and provide such other activities as may advance its purpose

Self-Assessment Exercise 3

List the functions of the African Development Bank.

6.4 Summary

In this unit, we have attempted to identify the different multilateral institutions mentioning their functions. We have identified different multi-national institutions and have stated their functions, depending on need and the level of the developing country.

6.5 References/Further Reading/Web Resources

Benjamin, E. & Martin, N. (2012). *Public finance administration in Nigeria. Cases and issues*. Onitsha: Chambers Books Ltd

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6.6 Possible Answers to Self-Assessment Exercise(s) within the content

Name the facilities provided by the World Bank to member countries?

Possible Answers to Self-Assessment Exercise 1

1. Structural Adjustment facility
2. Expansion lending for high-priority operations
3. Accelerated disbursements under existing and new investment commitments to ensure timely implementation of nigh priority projects
4. Expanded advisory services on the design and implementation of appropriate policies

List the objectives of International Development Association?

Possible Answers to Self-Assessment Exercise 2

1. To provide development finance to the less developed counties on easy and flexible terms
2. To promote economic development, increase productivity and improve the standard of living in the developing countries
3. To supplement the objectives and activities of the World Bank

List the functions of the African Development Bank.

Possible Answers to Self-Assessment Exercise 3

1. Use the resources at its disposal for financing of investment projects relating to the economic and social development of its members
2. Undertake and participate in the selection, study and preparation of projects enterprises and activities contributing to such development
3. Mobilise both within Africa and outside Africa, resources for the financing of such investment programme
4. Promote investment in Africa of public and private capital in projects or programme
5. Provide such technical assistance as may be needed in Africa for the study, preparation, financing and execution of development project or programme
6. Undertake such other activities and provide such other activities as may advance its purpose.

MODULE 5 FINANCIAL REPORTING AND AUDITING IN THE PUBLIC SECTOR

UNIT 1 Regulatory Framework for Managing Public Finance

Unit Structure

1.1 Introduction
1.2 Learning Outcomes
1.3 Regulatory Framework for Managing Public Finance
 1.3.1 Legal Framework that Governs Public Finance Management in Nigeria
 1.3.2 Regulatory Framework that Governs Public Finance Management in Nigeria
 1.3.3 Some Reforms in the Nigerian Public Finance Management
1.4 Summary
1.5 References/Further Reading
1.6 Possible Answers to Self-Assessment Exercise(s) within the content

1.1 Introduction

The legal and regulatory framework that underlies the Public Financial Management system includes tax laws, budget system laws and country‟s constitution besides laws, there are regulations relating to public finance management. Laws, budgets and regulations are essential to the task of public finance management. An appropriate legal and regulatory framework for a public financial management system should reflect an awareness of the link/between the strategic policy objectives of the government and the system and process relating to public financial management with referred to expenditure, so as to conform to the constitution principles and legislative responsibility and good governance, apart from the legal and regulatory framework that help to govern public finance management in Nigeria. The country also embarked in Economic Reforms and Governance Project (ERGP)sponsored by the world Bank to address the challenges of transparency, accountability, corruption and poor public service delivery this lead to the introduction of integrated personnel payroll and information system, Government integrated financial management information system, E- payment, Treasury Single Account etc.

1.2 Learning Outcomes

BY the end of this unit, you will be able to:

- identify legal framework that governs public finance management in Nigeria
- identify regulatory framework that governs public finance management in Nigeria
- discuss key submissions of reforms in the Nigerian public finance management

1.3 Regulatory Framework for Managing Public Finance

Public finance is the study of the role of the government in the economy. It is the branch of economics that deals with the revenue and expenditure of government or public institutions to achieve desirable objectives. Public financial management is the administration of funds used to deliver or provide public services such as education, health care, infrastructure among others. However, public finance management is concerned with public accountability and it is therefore governed by various statutory act or laws. Legal framework is a broad system of rules that governs and regulates decision making, agreements, laws, etc. It includes procedures regulations, guidelines, codes of conduct and other regulatory documents.

1.3.1 Legal Frameworks that Governs Public Finance Management in Nigeria

i. Nigeria Constitution: Public finance management is governed by the Constitution of the Federal Republic of Nigeria, 1979 as amended in 1989 and 1999 is one of the legal frameworks that regulate the mobilization of revenues, allocation of public funds, undertakes public spending account for funds and audit results. It also defines the expenditure and revenue collection responsibilities that are under their review

ii. Audit Ordinance of 1956 Or Act of 1956: These Act section 13 sub-sections 1-3 mandates the Accountant-General of the Federation to furnish the Auditor-General for the Federation with the nation’s financial statement. This will enable the results obtain on how the financial resources of the public to be audited to ensure public accountability and transparency.

iii. Finance (Control and Management) Act of 1958, cap 144, 1990: The Act governs the management and operation of public funds. It regulates the accounting system, the books to be kept and the procedure to be followed in the preparation of accounts and financial statements.

iv. Public Procurement Act 2007
This act established the National Council on Public Procurement (NCPP) and the Bureau of Public Procurement (BPP) as the regulating authorities responsible for monitoring and over sight of public procurement, harmonising the existing government policies by regulating setting standards and developing the legal framework and professional capacity for public procurement in Nigeria. The Act sets standard for organization procurements, methods of procurements of works, goods, consultancy and non-consultancy service as well as the procurement approval threshold for the Bureau of Public Procurement, Tenders Boards and Accounting officers for all Ministries, Department and Agencies.

v. Fiscal Responsibility Act 2007
This Act provides for the prudent management of the country resources, ensures long term macro-economic stability of the national economy, and secures greater accountability and transparency in fiscal operation in within a medium term fiscal policy framework the establishment of the fiscal responsibility and commission to ensure the promotion and to enforcement of the country's economic objectives. The Act emphasises the preparation of Medium Term Expenditure Framework Annual Budget, Budgetary Execution and Achievement Targets, collection of public revenue, Public Expenditure, Debt and indebtedness, borrowing, transparency and accountability.

vi. Other Laws Guiding Public Finance Management: Other laws guiding public frame management include the Independent Corrupt Practices and Other Related Offences Commission (ICPC) Act of 2000, Economic and Financial Crime Commission Establishment Act,2002, Nigeria Extractive Industries Transparency Initiative (NEITI) Act,2007 Appropriation Acts, Code of Conduct Bureau and Tribunal Act, 1991 and Money Laundering Act,1995.

1.3.2 Regulatory Framework that Governs PFM in Nigeria.

Regulatory framework is an accountability mechanism, a method by which the regulator accounts for the responsibilities conferred upon it. Regulatory framework for public financial management is essential to ensure that the needs of the public (stakeholders) are met and to regulate the behaviour of government towards their citizens in order to

achieve sustainable development. International Financial Reporting Standards (IFRS) argued that regulatory framework includes procedures, regulations, guidelines, codes of conduct, and other regulatory documents- complements financial and budget laws by clarifying or filling in gaps and should be regulatory reviewed. Public Finance Management is regulated by the following Regulations:

i. Financial Regulations: these are the accounting manual of government ministries, extra-ministerial departments that deals with financial and accounting matters. They set out the procedures and steps to be followed in treating most of government transactions.
ii. Finance/ Treasury Circulars: these are admin -tools that are used to amend the existing provision of financial regulations, public services rules and the introduction of new policy guidelines.
iii. The Financial Regulations (2009 Edition): The financial regulations are powerful control tools used in the public sector funds management. They are the accounting manuals of the three tiers of government of public frauds. The rules spelt out the system concerning the receipts and disbursements of funds and the procedures to ensure good accountability, prevention and early detection of frauds and errors and other financial malpractices.

Self-Assessment Exercise 1

Write short note on the Fiscal Responsibility Act, 2007?

1.3.3 Some Reforms in the Nigerian Public Finance Management

In 2004, the country embarked on economic reform and government project (ERGP) sponsored by the world bank to address the challenges of transparency, accountability, corruption and poor service delivery faced by the Federal Government of Nigeria.
Some reforms in the Nigeria public finance management are as follows:

1. **Treasury Single Account (TSA):** This unified structure of government bank accounts gives a consideration view of government cash resources. The primary objective of this TSA is to ensure effective aggregate control over government cash balances, thus, facilitates government cash management by minimising borrowing costs and effective aggregate control of cash as a key element in monetary and budget management. It also permits complete and timely information in government cash resources. TSA enhance greater transparency in public

finance management; facilitate more reliable and accurate accounting and improved reporting.

2. **Government Integrated Financial Management Information System (GIFMIS)**
GIFMIS is a sub component of the ERGP that will support the public resource management and targeted anti-corruption initiatives area through modernising fiscal processes using better methods, techniques and information technology. The GIFMIS aid strategic management of public financial resources for enhanced accountability, transparency, cost effective, public service delivery, and economic growth and poverty reduction efforts. The broad objective of GIFIMIS is to implement a computerised financial management information system for the government, which is efficient, effective, and users friendly and which increases the ability to demonstrate accountability and transparency to the public and cooperating partners. However, GIFMIS can only be successful if these are present: sustained management support, effective organization change; good project scope management; adequate project team composition etc.

3. **National Chart Of Account (NCOA):** The chart of accounts (COA) also called national chart of account provides a robust mechanism and form the classification of public resource under the budget as well as tracking public resources under the budget executive and seeks to support the adoption of more transparent and modern economic and financial management systems and process that are less prone to corruption.

4. **Integrated Personnel Payroll and Information System (IPPIS)**
IPPIS is one of the transformation agenda of the Federal Government of Nigeria with the aim of creating a centralised data base system for Nigerian public service with single accurate source of employee information that provides integration with other business application. The objective of IPPIS is to provide a centralised data base to aid government's manpower planning and decision making; greatly improve management reporting and information and enhance the confidence in payroll costs and budgeting.

5. **Excess Crude Account (ECA):** ECA is the name of Nigerian government account that is creating to save revenues- in excess of budgeting benchmark price -that were generated from the sales of oil. The primary objective of ECA was to protect

Nigeria planned budgets against shortfall caused by the volatility of crude oil prices. By detaching go averment expenditures from oil revenues, the ECA aimed to insulate the Nigerian economy form external shocks. It sought to protect public expenditure from being pattered on the boom- and bust cycles of the international oil market

6. **Sovereign Wealth Fund (SWF):** SWF was approved in 2011, by Nigeria's National Economic Council a plan to replace (ECA), primarily to ameliorate the controversies surrounding the ECA"S legality. SWF consisted of three sub-funds i.e. the stabilization to support the budget in times of economic stress including to hedge against volatile crude oil prices, the future generations fund – to save for future generations of Nigerians; and the Nigeria infrastructure fund – to invest in domestic infrastructure. The objective of SWF was structured to ensure more productivity and transparency by statute.

7. **Debt Management Office (DMO):** DMO was established to harmonize the monitoring of Nigeria's debt profile which was hitherto done by a great number of government units without any form of coordination. The DMO shrewd sourcing of fund to finance government deficit at affordable costs and manageable risks, mindful avoidance of debt crisis and achievement of steady growth and economic development- improvement of the nation borrowing capacity and other debt related functions

8. **E-Payment System:** This is a set of interactive elements, operational mechanisms and institutional arrangement for domestic currency payments in an economy. The objectives of e-payment among others are to enhance quality of service and there will be better value or money spent, to eliminate corruption associated with the previous payment system through cheques and cash. E-payment system provides positive effects on fiscal and monetary policy management as it reduces the amount of cash in circulation and this enables monitoring by regulators; and will reduce fraud, corruption; and financial irregularities.

Other Reforms of Nigerian Public Finance Management:
The other reforms include adoption of:

International Public Sector Accounting Standard (IPSAS): These are set of accounting standards issued by IPSAS Board for use by the public sector entities around the world in the preparation of financial statements. It major objectives is to improve the quality of general purpose financial reporting by public entities, leading to better

informed assessments of the resource allocation decisions made by governments, thereby increasing transparency and accountability.

Automated Accounting Transactions Reading Reporting System (ATRRS): This is an ICT based Accounting Software application which facilitates the input of Accounting Transactions, reconciliation and the generation of Standard Accounting Reports that meet required Standard of the Treasury. The implementation of the Accounting Transaction Recording and Reporting System (ATRRS) has opened the doors widely for the Treasury to appreciate the essence and benefits derivable from the computerization of Government Accounting System.

Medium Term Expenditure Framework (MTEF): is a medium term high level strategic plan of the government, usually three years in Nigeria and which form the basis of annual budgeting taking into consideration the law requirement that spending should not exceed revenue by more than 3% of GDP. It shifts the psychology of budgeting from "needs" to an "availability of resources". The objectives includes; 1. To improve macroeconomic balance, including fiscal discipline through good estimates of the available resource envelop, which are then to make budget that fit squarely within the envelop; to increase greater budget predictability as a result of commitment to more credible sectoral budget ceilings; etc.; and

Fiscal Strategy Paper (FSP): This is a 3- year transparent planning and budget formulation tool used for linking policy, planning and budgeting over a medium term. The FSP consists of the macroeconomic model that indicates estimates of revenue and expenditure, fiscal targets, risks as well as government financial obligations.

Self-Assessment Exercise 2

Write short note on the following:
i. Treasury Single Account (TSA).
ii. Government Integrated Financial Management Information System (GIFMIS).
iii. Integrated Personnel Payroll and Information System (IPPIS).

1.4 Summary

In this unit, we discussed extensively on economic reforms that guides public finance management such as the legal framework (constitution, audit ordinance, fiscal responsibility, public procurement, etc.) and

some economic reforms that were introduced when the country embarked on Economic Reforms and Governance Project (ERGP) sponsored by the World Bank to address the challenges of transparency, poor services delivery, accountability, corruption, etc.

1.5 References/Further Reading /Web Resources

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1.6 Possible Answers to Self-Assessment Exercise(s) within the content

Write briefly on Fiscal Responsibility Act?

Possible Answers to Self-Assessment Exercise 1

The Act provides for the prudent management of the country resources, ensures long term macro-economic stability of the national economy, and secures greater accountability and transparency in fiscal operation. The Act emphasises the preparation of Medium Term Expenditure Framework Annual Budget, Budgetary Execution and Achievement Targets, collection of public revenue, Public Expenditure, Debt and indebtedness, borrowing, transparency and accountability.

Write short note on the following:
i. Treasury Single Account (TSA).
ii. Government Integrated Financial Management Information System (GIFMIS).
iii. Integrated Personnel Payroll and Information System (IPPIS).

Possible Answers to Self-Assessment Exercise 2

i. Treasury Single Account (TSA): This unified structure of government bank accounts gives a consideration view of government cash resources. The primary objective of this TSA is to ensure effective aggregate control over government cash balances, thus, facilitates government cash management by minimising borrowing costs and effective aggregate control of cash as a key element in monetary and budget management. It enhances greater transparency in public finance management; facilitate more reliable and accurate accounting and improved reporting.
ii. Government Integrated Financial Management Information System (GIFMIS)
GIFMIS is a sub component of the ERGP that will support the public resource management and targeted anti-corruption initiatives area through modernising fiscal processes using better methods, techniques and information technology. The GIFMIS aid strategic management of public financial resources for enhanced accountability, transparency, cost effective, public service delivery, and economic growth and poverty reduction efforts. The broad objective of GIFIMIS is to implement a computerised financial management information system for the

government, which is efficient, effective, and users friendly and which increases the ability to demonstrate accountability and transparency to the public and cooperating partners.

iii. Integrated Personnel Payroll and Information System (IPPIS)
IPPIS is one of the transformation agenda of the Federal Government of Nigeria with the aim of creating a centralised data base system for Nigerian public service with single accurate source of employee information that provides integration with other business application. The objective of IPPIS is to provide a centralised data base to aid government's manpower planning and decision making; greatly improve management reporting and information and enhance the confidence in payroll costs and budgeting.

Unit 2 Financial Reporting

Unit Structure

2.1 Introduction
2.2 Learning Outcomes
2.3 Financial Reporting
    2.3.1 Meaning of Financial Reporting
    2.3.2 Objectives of Financial Reporting
    2.3.3 Challenges of Public Financial Report
    2.3.4 Benefits of Public Financial Report
2.4 Summary
2.5 References/Further Reading
2.6 Possible Answers to Self-Assessment Exercise(s) within the content

2.1 Introduction

In the preceding unit, you were introduced to the legal and regulatory framework that underlies the Public Financial Management system which includes tax laws, budget system laws and country's constitution. Therefore, having been acquainted with regulatory framework both legal and otherwise guiding public financial management, this unit will acquaint you with the meaning of financial reporting, the characteristics, benefits and challenges of financial reporting and its importance to users of accounting information.

2.2 Learning Outcomes

By the end of this unit, you will be able to:

- Define financial reporting
- State the challenges and importance of financial reporting
- Explain the importance of financial reporting to the users such as the government

2.3 Financial Reporting

2.3.1 Meaning of Financial Reporting?

Financial Reporting refers to the communication of financial information, like financial statements, to the financial statement users, such as potential investors, employee, creditors and the public at large. Financial reporting is typically viewed as public and private companies issuing financial statements. The accounting and financial aspects of each and every department are recorded and are reported to various stakeholders. Schiavo-Campo and Tommasi (1999) viewed financial reporting as an aim to improve budget compliance. They provide a means for internal or external stakeholders to assess government performance. Financial reporting entails extracting and presenting data from the accounting system in ways that facilitates analysis. Governments produce a range of reports for internal and external consumption.

Financial Reporting is a very important and critical task of an organization. A typical report include daily flash reports on cash flows, monthly reports on budget execution, revenue reports, mid-year reports and annual financial statements or fiscal reports. Financial reports form a basis for the audit review of government performance.

Self-Assessment Exercise 1

What is Financial Reporting?

2.3.2 Objectives of Financial Reporting

According to International Accounting Standard Board (IASB), the objective of financial reporting is "to *provide information about the financial position, performance and changes in financial position of an enterprise that is useful to a wide range of users in making economic decisions."*
The following are the objectives of financial reporting:

1. Providing information to the management of an organization which is used for the purpose of planning, analysis, benchmarking and decision making.
2. Providing information to investors, promoters, debt provider and creditors which is used to enable them to male rational and prudent decisions regarding investment, credit etc.

3. Providing information to shareholders and public at large in case of listed companies about various aspects of an organization.
4. Providing information about the economic resources of an organization claims to those resources (liabilities and owner's equity) and how these resources and claims have undergone change over a period of time.
5. Providing information as to how an organization is procuring and using various resources.
6. Providing information to various stakeholders regarding performance management of an organization as to how diligently and ethically they are discharging their fiduciary duties and responsibilities.
7. Providing information to the statutory auditors which in turn facilitates audit.
8. Enhancing social welfare by looking into the interest of employees, trade union and Government.

2.3.3 Challenges of Public Financial Report

Deloitte, (2018) Identified some challenges as follows:

1. Statutory deadlines for government financial reporting are decreasing as the legislature demands information to support policy decisions.
2. Orderly and controlled business processes through budget execution are required to ensure accurate accounting data is generated real-time.
3. Public Sector Accountants with excellent professional training are being hired but finds public sector workplaces do not live up to their training.
4. It also lack integration and in many cases still being largely paper-based and inefficient.
5. Whole-of-government financial reporting is generally the largest accounts consolidation exercise in any economy.

2.3.4 Benefits of Public Financial Report

1. Faster close strategies and implementation: It improves the usefulness of financial statements through earlier release while achieving efficiency in the financial reporting function.
2. Outsourced reporting services: Government can outsourced accounting and financial reporting services to an audit firm e.g. Deloitte, KPMG, PWC, etc. for a better and good financial report.
3. Government can hire expert who are knowledgeable in International Public Sector Accounting Standards (IPSAS)/

International Financial Reporting Standards (IFRS) to review compliance to international standards and to develop strategies for improving disclosures
4. Financial Management Information Systems: Strategies; Requirements Definition; project Management; Quality Assurance; Human Resource Development.
5. Audit firm can assist government entities to go beyond compliance and deliver financial statements as part of an Annual Report providing enhanced transparency to her citizens.
6.
For the purpose of bidding, labor contract, government supplies etc., organizations are required to furnish their financial reports & statements.

Self-Assessment Exercise 2

Discuss the Challenges and Benefits of Financial Reporting?

2.4 Summary

Summarily, Financial Reporting refers to the communication of financial information to financial statement users. Financial reporting is typically viewed as public and private companies issuing financial statements. Financial Reporting is a very important and critical task of an organization. A typical report include daily flash reports on cash flows, monthly reports on budget execution, revenue reports, mid-year reports and annual financial statements or fiscal reports. The objective of financial reporting is to provide information about the financial position, performance and changes in financial position of an enterprise that is useful to a wide range of users in making economic decisions.

2.5 References/Further Reading /Web Resources

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2.6 Possible Answers to Self-Assessment Exercise(s) within the content

What is Financial Reporting?

Possible Answers to Self-Assessment Exercise 1

Financial Reporting refers to the communication of financial information to financial statement users. Financial reporting is typically viewed as public and private companies issuing financial statements. Financial Reporting is a very important and critical task of an organization. A typical report include daily flash reports on cash flows, monthly reports on budget execution, revenue reports, mid-year reports and annual financial statements or fiscal reports.

Discuss the Challenges and Benefits of Financial Reporting?

Possible Answers to Self-Assessment Exercise 2

The Challenges of Public Financial Report include:

1. Statutory deadlines for government financial reporting are decreasing as the legislature demands information to support policy decisions.
2. Orderly and controlled business processes through budget execution are required to ensure accurate accounting data is generated real-time.
3. Public Sector Accountants with excellent professional training are being hired but finds public sector workplaces do not live up to their training.
4. It also lack integration and in many cases still being largely paper-based and inefficient.
5. Whole-of-government financial reporting is generally the largest accounts consolidation exercise in any economy.

The Benefits of Public Financial Report are as follows:

1. Faster close strategies and implementation:
2. Outsourced reporting services:
3. Government can hire expert who are knowledgeable in International Public Sector Accounting Standards (IPSAS)/ International Financial Reporting Standards (IFRS) to review compliance to international standards and to develop strategies for improving disclosures

4. Financial Management Information Systems
5. Audit firm can assist government entities to go beyond compliance and deliver financial statements as part of an Annual Report providing enhanced transparency to her citizens.

Unit 3 Analyzing Financial Report and Audit

Unit Structure

3.1 Introduction
3.2 Learning Outcomes
3.3 Analyzing Financial Report end Audit
  3.3.1 Analysing Financial Reporting
  3.3.2 Ratio Analysis
  3.3.3 Concept of Audit
  3.3.4 Objectives of Auditing
3.4 Summary
3.5 References/Further Reading
3.6 Possible Answers to Self-Assessment Exercise(s) within the content

3.1 Introduction

In the last unit, you were introduced to the concept of financial reporting, its objectives, benefits as well as challenges. This unit will introduce you to analyses of financial reporting using ratio analysis. The concept of audit as well as the advantages and disadvantages will be discussed. Financial reporting has to be analysed or interpreted in order to measure the quality of management and how solid the capital base of the sector is.

3.2 Learning Outcomes

By the end of this unit, you will be able to:

- analyse Financial Reporting using ratio analysis.
- explain the importance and limitation of using ratio to analyse financial reporting.
- define Audit and state its advantages and disadvantages

3.3 Analysing Financial Report and Audit

3.3.1 Analysing Financial Reporting

This can be defined as the art and science of translating the figures shown in the financial statements in such a way as to reveal the strengths and weaknesses of a business and the attributable causes. Any financial statement can be interpreted; consequently, management accounts, final accounts and interim account lend themselves to critical analysis.

Financial reporting analysis is also defined as the judgment process, which aims at evaluating the current and past financial positions and the results of an entity with the primary objectives of determining the best possible estimates about future conditions and performances. In analysing financial reporting using ratio analysis in single or number of variables to compute for a given ratio and compare it with a given standard to determine whether performance is good or bad. In other words, for the purpose of this lecture, we will restrict our analysis of financial reporting to ratio analysis.

3.3.2 Ratio Analysis

Ratio analysis involves expressing one figure as a ratio or percentage of another, to bring out the weakness or strength in an organisation's day to day affairs. In public sector, looking at the financial statement of Government department, Ministry or Corporation, the various figures disclosed would not be sufficiently revealing in terms of the strength or otherwise of the establishment, for well-informed judgment to be made. Ratios can be grouped into four categories such as:

- Profitability ratios
- Gearing ratios
- Liquidity ratios and
- Shareholders" investment ratios

The Federal, State and Local Government councils use mostly liquidity ratios to measure the ease with which obligations due in the year can be met. The three tiers of Administration operate the cash basis of accounting. Government parastatals, Agencies, Ministries and Extra-Ministerial department while some commercial or quasi-commercial makes use of accrual basis.

In line with the aforementioned ratios above, public sector activities considers them relevant.

Current Ratio

This is the ratio of current asset to current liabilities and can be obtained from statement of financial position and this is the formula:

$$\frac{\text{Current Assets}}{\text{Current Liabilities}}$$

An organisation should have enough current assets that give a promise of cash to meet short-term commitments of paying off current liabilities. However, as a general rule, the ideal ratio for Government parastatals, Agencies and Departments is 2:1.

Quick Ratio or Acid Test

This is the ratio which is more revealing of the solid liquidity position, it is also obtained from the statement of financial position and this is the formula:

$$\frac{\text{Current Assets less stock}}{\text{Current Liabilities}}$$

Public Sector or Private Organisations are not able to convert all their current assets into cash quickly. For Government parastatals, Agencies and Departments with a fast stock turnover, a quick assets ratio can be computed. The ideal ratio is 1:1. And it is important in improving the liquidity.

Debtors' Payment Period

This measures the average length of time it takes a Corporation's debtors to pay; it is only an estimated average payment period. The formula for computing the payment period is:

$$\frac{\text{Debtors for Goods or Services}}{\text{Sales (Credit)}} \times 365 \text{ days}$$

The immediate payment of cash by the debtors put the Government parastatals, Agency and Departments in a better cash position.

Creditors' Payment Period

This measures the average length of time it takes Government parastatals, Agency and Departments under focus to pay its creditors. The formula is as follows:

$$\frac{\text{Trade or Expense Creditors}}{\text{Credit Purchases}} \times 365 \text{ days}$$

Stock Turnover Period
This indicates the average number of days that items of stock are held for sale or in the store. The stock turnover is calculated as:

$$\frac{\text{Cost of Goods Sold} \times 365 \text{ days}}{\text{Opening stock} + \text{Closing stock}/2}$$

Average stock is the average of the opening and closing stock figures. The shorter the period, the healthy the situation is in making the best use of funds.

Self-Assessment Exercise 1

What is Ration Analysis of Financial Reporting?

3.3.3 Concept of Audit

Public audit is the examination of the records and reports of an enterprise or governmental department by experts or persons other than those responsible for their preparation. Although every transaction cannot be verified by an independent authority, external audits can nonetheless provide reasonable assurance about the governance and discharge of the financial management responsibility by the organisation and that it represents value for money. It can also highlight any shortcomings for management action. (Arsalan & Nida, 2012). Auditing is a process carried out by qualified Auditors during which the accounting records and the financial statements of an enterprise are subjected to examination by independent Auditors with the main purpose of expressing an opinion in accordance with his terms of appointment. (Adams, 2014).

3.3.4 Objectives of Auditing

The objectives of auditing could be divided into two:

a. The primary objectives and
b. The secondary objectives

a. The primary objectives is to enable the Auditor to report as to whether the financial statement present „a true and fair view" of the financial affairs of the organisation during the period under review and as at the end date.
b. The secondary objectives of an audit are to detect and prevent Errors and Frauds. Errors are omission or mistakes made by an accountant that are not intentional while Fraud is a deliberate

omission or mistake made by an accountant in order to enrich himself/herself.

Advantages of Audit

1. Auditing helps to assure the shareholders that their business enterprise is been run or managed in their interest.
2. Audited accounts could be more easily acceptable by the Inland Revenue for Tax purposes.
3. Audited accounts can be very useful for investigating bank loan or overdraft.
4. Audited accounts can be used as a basis for business combination such as merger and acquisition.
5. Auditing helps to prevent or detect fraud or errors within an enterprise.
6. Strengthen the internal country system of the enterprise.

Disadvantages of Audit

1. When the financial statements are not properly prepared, it can lead to poor financial report
2. Auditing attracts extra cost
3. Auditing could also lead to delay in the presentation of the audited financial statement.

Self-Assessment Exercise 2

What are the advantages and disadvantages of Audit

3.4 Summary

Ratio analysis involves expressing one figure as a ratio or percentage of another, to bring out the weakness or strength in an organisation's day to day affairs. Ratios can be grouped into four categories such as profitability ratios, gearing ratios, liquidity ratios and shareholders‟ investment ratios. Audit, however is the examination of the records and reports of an enterprise or governmental department by experts or persons other than those responsible for their preparation. Advantages of audit include helping to assure shareholders that their business enterprise is been run or managed in their interest, acceptability of companies accounts by the Inland Revenue for Tax purposes, investigating bank loan or overdraft, preventing or detecting fraud or errors within an enterprise, and strengthening the internal country

system of the enterprise. However, disadvantages of audit include attraction of extra cost by firm, delay in presentation of financial statement and production of poor financial report.

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3.6 Possible Answers to Self-Assessment Exercise(s) within the content

What is Ration Analysis of Financial Reporting?

Possible Answers to Self-Assessment Exercise 1

Ratio analysis involves expressing one figure as a ratio or percentage of another, to bring out the weakness or strength in an organisation's day to day affairs. Ratios can be grouped into four categories such as profitability ratios, gearing ratios, liquidity ratios and shareholders" investment ratios.

What are the advantages and disadvantages of Audit?

Possible Answers to Self-Assessment Exercise 2

Advantages of Audit

1. Auditing helps to assure the shareholders that their business enterprise is been run or managed in their interest.
2. Audited accounts could be more easily acceptable by the Inland Revenue for Tax purposes.
3. Audited accounts can be very useful for investigating bank loan or overdraft.
4. Audited accounts can be used as a basis for business combination such as merger and acquisition.
5. Auditing helps to prevent or detect fraud or errors within an enterprise.
6. Strengthen the internal country system of the enterprise.

Disadvantages of Audit

1. When the financial statements are not properly prepared, it can lead to poor financial report
2. Auditing attracts extra cost
3. Auditing could also lead to delay in the presentation of the audited financial statement.

Unit 4 Accounting Practice and Financial Management Cycle

Unit Structure

4.1 Introduction
4.2 Learning Outcomes
4.3 Accounting Practice and Financial Management Cycle
4.3.1 Accounting Practice
4.3.2 Financial Management Cycle
4.4 Summary
4.5 References/Further Reading
4.6 Possible Answers to Self-Assessment Exercise(s) within the content

4.1 Introduction

The previous unit introduced you to analyses of financial reporting using ratio analysis. The concept of audit as well as the advantages and disadvantages were also discussed. This unit is to define, discuss Accounting practice and financial management cycle for a better and transparent public sector.

4.2 Learning Outcomes

By the end of this unit, you will be able to:

- define Accounting practice
- explain the Financial Management Cycle
- explain the meaning and importance of Accounting and Management cycle

4.3 Accounting Practice and Financial Management Cycle

4.3.1 Accounting Practice

Accounting practice is the system of procedures and controls that an accounting department uses to create and record daily/weekly/monthly

transactions. Accounting practice should ideally be extremely consistent, since there are a large number of business transactions that must be dealt with in exactly the same manner in order to produce consistently reliable financial statements. (Bragg, 2018). The importance of accounting practice cannot be overemphasized and that will lead us to the type of accounting practice. The types of accounting practice include the following:

i. Public Sector Accounting practices
ii. Audit practices
iii. Tax practices
iv. Forensic Accounting practices
v. Management Information System practices
vi. Management Accounting practices
vii. Financial Management practices
viii. Book Keeping/ Accounting operation practices

The above listed types of accounting practices can further be explained below:

i. Public Sector accounting practices: Is the presentation, measurement and budgeting and interpretation of public funds to the users. The basis of accounting is divided into two:

a. Cash basis and
b. Accrual basis

a. Cash basis: This is the basis of accounting under which revenue is recorded only when cash received, and expenditure recognized only when cash is paid, irrespective of the fact that the transactions might have occurred in the previous accounting period.
b. Accrual basis: Under this basis, revenue is recorded when earned and expenditure acknowledged as liabilities when known or benefits received, notwithstanding the fact that the receipts or payments of cash have taken place wholly or partly in other accounting periods.

However, prior to this date, the public sector accounting was based on cash basis but as at today, the public sector accounting is based on accrual basis.

In the public sector, there is a shift in the budgeting system from the conventional budgeting system to Activity base budgeting and Zero base budgeting. While, the financial measurement is based on value for money, the non-financial measurement is based on Balanced score card and key performance indicator.

ii. Audit practices: This is the independent examination of financial statement by an independent person called the auditor in order to ensure that the financial statement presents a true and fair view in his professional opinion. There are other services that can be rendered by the auditor and these services include;

a. Accounting
b. Taxation
c. Secretarial services
d. Management Advisory
e. Investigation
f. Liquidation and Receivership.

iv. Tax Practices: A tax preparation practice specializes in preparing individual, partnership and corporate income tax returns. In this type of practice, tax returns are generally assigned to accountants by their specific area of specialization. Tax practice is a different aspect on its own and it require an accounting knowledge and that is why Chartered Accountant practices tax also.

v. Forensic Accounting Practices: Forensic accounting is a special type of auditing that is most often discussed in the legal arena. Forensic Accounting provides an accounting analysis that is suitable to the court which will form the basis for discussion, debate and ultimately dispute resolution. The integration of accounting, auditing skills yields the specialty known as Forensic Accounting.

vi. Management Information System practices: This is the processing of data to information in specialized accounting software. More companies are realizing the benefits of specialized accounting software, specifically management information systems, but many companies do not have personnel with the education or knowledge needed to perform a complicated software setup or conversion.

vi. Management Accounting Practices: Chartered Institute Management Accountant (CIMA) defines Management accounting as the application of the principles of accounting and financial management to create, protect, preserves and increase value for the stakeholders of for-profit and non-profit enterprises in the public and private sectors. Management accounting is essentially necessary for an organization in reacting positively to the rising changes and developments affecting business profitability. Management Accounting Practice areas are: Cost

transformation and Management; External Reporting; Financial strategy; Internal control; Investment Appraisal Management and Budgetary control. And based on the definition of Management accounting provided in earlier. The major purposes of management accounting are:

a. Provision of financial and non-financial information for taking decisions on how to efficiently utilize an organization's resources through proper planning.
b. Establishing of an effective control system.
c. Providing better means of measuring performance of different segments in the organization.
d. Examining the competitive strength of an organisation.
e. Assisting the organisation in the areas of product and technological innovations.
f. Motivating managers and subordinates in improving productivity.
g. Assisting the organisation to identify and eliminate non value-added activities.
h. Focusing on continuous improvement towards cost and quality.
i. Safeguard an organisation's resources.

vii. Financial Management practices: Financial management entails planning, organising, controlling, monitoring and evaluating the financial resources of an organisation to achieve its overall objectives. And it is concerned with making decisions about the provisions and use of a firm's finances. Financial management is the life wire of every business organization.

The objective of financial management practices is to gain a better understanding of the financial management best practices and the areas are:

a. Working Capital Management
b. Budgeting process, roles and the responsibilities
c. Investment Appraisal system
d. Financial Statements
e. Cash Flow system
f. Auditor" report

viii. Book- Keeping Practices: Bookkeeping is the term used to describe everyday accounting such as processing accounts payable and accounts receivable, making bank deposits, processing payroll and preparing month-end financial statements. This is also another type of accounting practice but does not require the professional interpretation aspect to the users of accounting information. This type of practice is

common among small businesses. For example, a sole proprietor business, partnership business, joint venture business etc. Bookkeeping helps in maintaining and providing the latest financial position of the business and, therefore, assumes great significance. It is advisable to maintain books of account for the following reasons:

a. They provide up-to-date information about the business
b. They reflect the outcome of transaction made during the period under review.
c. They give information about the state of affairs of the business at regular intervals.
d. They help government, individuals and other authorities to decide about the incidence of various Taxes.
e. Their books help to analyse the performance of the business and
f. It also help to compare the performance of several businesses

Self-Assessment Exercise 1

State six types of accounting practices?

4.3.2 Financial Management Cycle

Financial management cycle can be defined as the monitoring of finance involving receiving income and reporting income and expenditure to organizational policy makers (such as the Board) and to donors. The financial management cycle has to do with the planning and control of financial spending for effective and efficient purposes. Effective public sector financial management and service delivery is a continuous process of planning, implementation, evaluation, audit and improvement based on the outcomes. Financial management cycle can be represented diagrammatically. Thus:

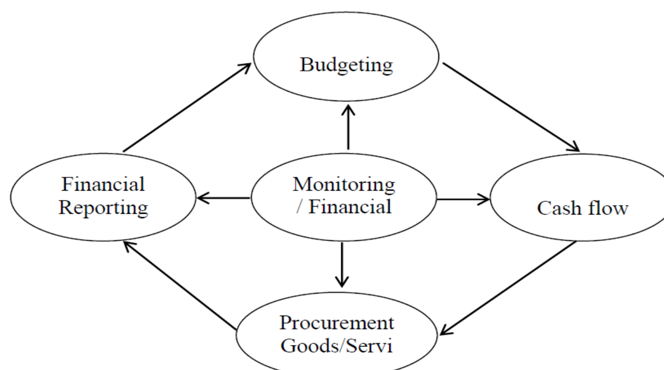

Figure 1: Financial Management Cycle:
Source: Financial Planning Management Development. Winter (2000)

The key factors of the cycle are:

- Budgeting is all about what the organisation plans to do and how it allocates the necessary resources to make goods/service delivery possible.
- Cash flow is the total amount of money being transferred into and out of a business especially as its affecting liquidity.
- Monitoring/Financial Control is confirming that planned service outcomes are achieved within allocated budget and controls are been put in place.
- Financial Reporting is all about the strength and weakness of the financial statement and how it can be improved upon.

However, in conclusion, FMC stands for Financial Management Cycle and relates to the way governments manage public resources (both revenue and expenditure) and the immediate and medium to-long-term impact of such resources on the economy or society. As such, FMC has to do with both process (how governments manage) and results (short, medium, and long term implications of financial flows).

Self-Assessment Exercise 2

Discuss Financial Management Cycle?

4.4 Summary

In this unit, we have discussed extensively on accounting practices and Financial Management Cycle. Accounting practice is the system of procedures and controls that an accounting department uses to create and record daily/weekly/monthly transactions. Accounting practice should ideally be extremely consistent, since there are a large number of business transactions that must be dealt with in exactly the same manner in order to produce consistently reliable financial statements. (Bragg, 2018). The importance of accounting practice cannot be overemphasized and that will lead us to the type of accounting practice.

Types of accounting practice include public Sector Accounting practices, Audit practices, Tax practices, Forensic Accounting practices, Management Information System practices, Management Accounting practices, Financial Management practices and Book Keeping/ Accounting operation practices.

Financial management cycle can be defined as the monitoring of finance involving receiving income and reporting income and

expenditure to organizational policy makers (such as the Board) and to donors. The financial management cycle has to do with the planning and control of financial spending for effective and efficient purposes. Effective public sector financial management and service delivery is a continuous process of planning, implementation, evaluation, audit and improvement based on the outcomes.

4.5 References/Further Reading/Web Resources

Bragg, S. M. (2018). Accounting Best Practices.(5thed), John Wiley & Sons. Inc

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4.6 Possible Answers to Self-Assessment Exercise(s) within the content

State six types of accounting practices?

Possible Answers to Self-Assessment Exercise 1

The types of accounting practice include the following:

i. Public Sector Accounting practices
ii. Audit practices
iii. Tax practices
iv. Forensic Accounting practices
v. Management Information System practices
vi. Management Accounting practices

Discuss Financial Management Cycle?

Possible Answers to Self-Assessment Exercise 2

Financial management cycle can be defined as the monitoring of finance involving receiving income and reporting income and expenditure to organizational policy makers (such as the Board) and to donors. The financial management cycle has to do with the planning and control of financial spending for effective and efficient purposes. Effective public sector financial management and service delivery is a continuous process of planning, implementation, evaluation, audit and improvement based on the outcomes.

Unit 5: Financial Misconduct

Unit Structure

5.1 Introduction
5.2 Learning Outcomes
5.3 Financial Misconduct
  5.3.1 Fraud
  5.3.2 Factors that Enhanced Financial Statement Fraud
  5.3.3 Solutions on how to curb financial misconduct
5.4 Summary
5.5 References/Further Reading Web Resources
5.6 Possible Answers to Self-Assessment Exercise(s) within the content

5.1 Introduction

The previous unit introduced you to accounting practice and financial management cycle for a better and transparent public sector. This unit is to define financial misconduct, reasons for financial misconduct, effects and solution to curb the financial misconduct. Financial misconduct is aspect that needs to be checked by providing and the necessary checks and controls for better governance.

5.2 Learning Outcomes

By the end of this unit, you will be able to:

- define financial misconduct.
- state effects of financial misconduct on our economic development?
- identify the types of fraud and how they are been perpetuated

5.3 Financial Misconduct

Financial Misconduct should be taken to cover “fraud, corruption, theft, dishonesty or deceit by an employee, whether at the expense of institution, other employees or any other body or organisation”, as well as actions or inactions which fall below the standards of probity expected in public. That is to say any intentional act is regarded or

termed as fraud. However, it is the responsibility of every employees working in the public sector or private sector to ensure or be aware that:
Public Asset are protected
Ensure that management and other practices accord with the standards of probity expected of public sector bodies
Ensure that the resources available to it are used only for the organizational objectives as allocated.
Fraud, corruption or any other kind of financial misconduct cannot be tolerated.

5.3.1 Fraud

Financial misconduct is seen as fraud. And Fraud is a false representation of a matter of fact, whether by words or by conduct, by false or by concealment of that which should have been disclosed that deceives and is intended to deceive another, so that the individual will act upon it to her or his legal injury(Black Law Dictionary,2004). Fraud is commonly understood as dishonesty calculated for advantage. A person who is dishonest may called a fraudster.

Types of Fraud
The types of fraud include:

i. Misappropriation of assets;
ii. Bribery and corruption;
iii. Financial statement Fraud.

i. Misappropriation of assets: Misappropriation of asset is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing, indirectly causing accounting irregularities in financial statements (Kwok, 2005). Misappropriation of assets can be accomplished in a variety of ways including:

a. Embezzling receipts(for example, misappropriating collections on accounts receivables or diverting receipts in respect of written-off accounts to personal bank accounts);
b. Stealing physical assets or intellectual property (for example, stealing inventory, for personal use or for sale, stealing scrap for resale, colluding with a competitor by disclosing technological data in return for payment)
c. Causing an entity to pay for goods and services not received (for example payment to fictitious vendors, kickbacks paid by vendors to the entity's purchasing agents in return for inflating process, payments to fictitious employees);

d. Using and entity's asset for personal use (for example, using the entity's assets as collateral for personal loan or a loan to a related party)

ii. Bribery and corruption: Corruption is defined as bribery, that is, payment in money or in kind that is given or taken in a corrupt relationship. It can also involve the abuse of entrusted power for private gain, or an inducement to show favour. The perversion or destruction of integrity in the discharge of public duties by bribery, favour and the use or existence of corrupt practices especially in a state or public corporation (Black Law Dictionary, 2004)

iii. Financial statement fraud: According to the American Institute of Certified Public Accounts (AICPA,1988), Financial statement fraud is intentional or reckless conduct, whether intentional act or omission that results in materially misleading financial statements. It also entails gross and deliberate distortion of corporate records such as inventory manipulation or fraudulent transactions such as fictitious sales or orders. Fraudulent financial reporting may also entails the misapplication of accounting principles.

Self-Assessment Exercise 1

What is financial misconduct?

5.3.2 Factors that Enhanced Financial Statement Fraud

Association of Certified Fraud Examiners (2015) investigated a study and found that fraudulent financial reporting usually occurs as a result of certain environmental factors and opportunities, institutional or individual. These forces and opportunities add pressures and incentives that encourage individuals and companies to engage in fraudulent financial reporting. Where the right mix of forces and opportunities is reached, it can produce fraudulent financial reporting. The reason people commit fraud was first examined by Cressey Donale, a criminologist in 1950s. He wanted to find out what made people to commit fraud. According to him, there are three major factors that push people to commit fraud. They include pressure, opportunity and rationalization. In an attempt at explaining fraud in accounting, Cressey (1973) proposed the following function:

FRAUD = f (Pressure, Opportunity, Rationalisation)

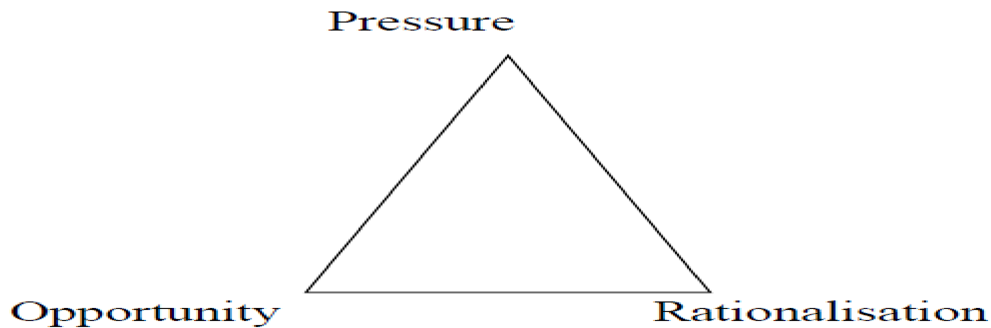

Fig. 2: The Triangle of Fraud
Source: Cressey (1973)

a. Pressure is the first factor that influences individuals to commit fraud and it refers to excessive force to achieve financial targets (for corporate entities and for individuals receives force from friends and relatives in order to measure up with the current trend or material things), to induce optimistic and unrealistic messages in annual reports. In addition, a firm may be threatened and pressured also by intense competition, by market saturation of sudden changes, acquisitions (merger) the financing need or cash flow problems.

b. Opportunity refers to those factors that enable fraud to be more easily committed and detection less probable. Therefore, ineffective controls or absence of control favours fraud intensions. These factors can be related directly to inadequate monitoring by management or the ineffectiveness of the board of directors or of the audit committee to oversee the reporting and the internal control.

c. Rationalisation is the trigger factor of the fraud act and refers to the fact that the perpetrator must have a mindset that would justify or rationalize the act of fraud. Detection of risk factors that push board members, management, employees to be predisposed to such intent may be quite difficult. Thus, when a company monitors people and processes to discourage and detect fraud, it must follow the three aspects, because fraud involves incentives or pressure to commit a fraudulent act, a perceived to do so, and some reasoning.

5.3.3 Solutions on how to Curb Financial Misconduct.

The following are some of the solutions on how to curb Financial Misconduct:

1. There should be Principles, rules and laws on the conduct of every staff or employees of the organization as it relates to financial misconduct.
2. Reporting Suspected Financial Misconduct is also a major impact in curbing financial misconduct in the public and private sector.
3. Immediate investigation of allegation on financial misconduct could also serve as a means of curbing fraud.
4. There should be encouragement in the aspect of employee emolument i.e. staff should be paid good pay in line with their performance. Thus, it will reduce or minimize theft and fraud.
5. There should be reward for hard work such as bonus, Gifts, Promotion, etc it will curb financial misconduct.

Self-Assessment Exercise 2

State three causes of financial misconduct?

5.4 Summary

Financial misconduct refers to "fraud, corruption, theft, dishonesty or deceit by an employee, whether at the expense of institution, other employees or any other body or organisation", as well as actions or inactions which fall below the standards of probity expected in public. The types of fraud include misappropriation of assets; bribery and corruption; and financial statement. Factors that promote financial misconduct include pressure, opportunity and rationalization.

5.5 References/Further Reading /Web Respurces

Bragg, S. M. (2018). Accounting Best Practices.(5thed), John Wiley & Sons. Inc

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Winter (2000).The Manager series "Understanding and Using Financial Management Systems to Make Decisions" Boston MA.FPMD.

5.6 Possible Answers to Self-Assessment Exercise(s) within the content

What is financial misconduct?

Possible Answers to Self-Assessment Exercise 1

Financial misconduct refers to "fraud, corruption, theft, dishonesty or deceit by an employee, whether at the expense of institution, other employees or any other body or organisation", as well as actions or inactions which fall below the standards of probity expected in public. The types of fraud include misappropriation of assets; bribery and corruption; and financial statement.

State three causes of financial misconduct?

Possible Answers to Self-Assessment Exercise 2

Factors that promote financial misconduct include pressure, opportunity and rationalization.

a. Pressure refers to excessive force to achieve financial targets (for corporate entities and for individuals receives force from friends and relatives in order to measure up with the current trend or material things), to induce optimistic and unrealistic messages in annual reports.
b. Opportunity refers to those factors that enable fraud to be more easily committed and detection less probable. Therefore, ineffective controls or absence of control favours fraud

intensions. These factors can be related directly to inadequate monitoring by management or the ineffectiveness of the board of directors or of the audit committee to oversee the reporting and the internal control.

c. Rationalisation is the trigger factor of the fraud act and refers to the fact that the perpetrator must have a mindset that would justify or rationalize the act of fraud.