



**COSTING AND FUNDING
STRATEGIES TRAINING FOR
SEEDS PRACTITIONERS**

**Centre for Management
Development**

**Management Village, Shangisha
P. M. B. 21578
Ikeja - Lagos State,
Nigeria**

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CMD MISSION STATEMENT

OUR MISSION is to Stimulate, Promote and Co-ordinate
Management Development for the Achievement of
Management *Excellence in Nigeria and Beyond*

BRIEF ON CMD

The Centre for Management Development (CMD) is a resource institution established in 1973 by the Federal Government of Nigeria. It is the operational arm of the Nigerian Council for Management Development (NCMD). As a resource institution under the National Planning Commission, CMD has responsibilities to simulate, promote and co-ordinate management education, training, research and consultancy in Nigeria.

Specifically, CMD pursues its role of capacity building and economic management by:

- identifying the type and quality of programmes required for the development of the country's managerial manpower;
- developing resources for management research, training and consultancy;
- institution building to meet the needs of national development; and
- improving the quality and enhancing the use of management research, training and consulting.

In addition to these roles, CMD undertakes the management development component of small and medium scale industries development through the design and provision of suitable training packages for industrialists and officials of Federal/State agencies.

TARGET AUDIENCE

CMD's scheduled programmes are designed primarily for:

- entrepreneurs and managers in the public and private sectors of the economy;
- management educators, trainers, consultants, industrial extension officers, researchers, human resource specialists in institutions and agencies;
- planners at the federal, state, local government and organisational levels; and

- professionals and other self-employed Nigerians whose employment and self-fulfilment depend upon enhancing their managerial and supervisory effectiveness.

Note: This specific course on Costing and Funding SEEDS is designed for members of the State Planning Commission or its equivalent, members of the SEEDS Implementation Team (SIT), SEEDS Implementation Committee (SIC), Planning and Budget Officers, and other relevant Middle and Senior Level Officers.

CMD, through its portfolio of management development Programmes, has made and will continue to make significant contributions to the development of the country's managerial capability. In response to the dynamic needs of its clientele, CMD has positioned itself and redesigned its process in order to improve its delivery system to keep pace with the ever-changing and challenging environment of the new millennium. Also CMD explores opportunities that abound as a result of the emergence of a New World Order.

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COURSE SCHEDULE

A Short Course Work for SEEDS Practitioners – Costing and Funding Strategies			
Day 1 – Monday			
Activity	Duration (mins)	Time	Responsibility
1. Introduction/Opening Ceremony	120	9:00 – 11:00 am	
2. Tea/Coffee Break	30	11.00 – 11.30 am	
3. Module 1	120	11.30 – 1.30 pm	
4. Lunch Break	60	1:30 – 2:30 pm	
5. Questions, Discussions, Exercises	120	2:30 – 4:30 pm	

A Short Course Work for SEEDS Practitioners – Costing and Funding Strategies			
Day 2 – Tuesday			
Activity	Duration (mins)	Time	Responsibility
1. Recap of day 1	30	8:30 – 9.00 am	
2. Module 2	120	9.00 – 11.00 am	
3. Tea Break	30	11:00 – 11:30 am	
4. Module 2 Contd.	120	11.30 – 1.30 am	
5. Lunch Break	60	1.30 – 2.30 pm	
6. Questions, Discussions, Exercises	120	2:30 – 4:30 pm	

A Short Course Work for SEEDS Practitioners – Costing and Funding Strategies			
Day 3 – Wednesday			
Activity	Duration (mins)	Time	Responsibility
1. Recap of Day 2	30	8:30 – 9:00 am	
2. Module 3	120	9.00 – 11.00 am	
3. Tea Break	30	11.00 – 11.30 pm	
4. Module 3 Contd.	120	11:30 – 1:30 pm	
5. Lunch Break	60	1:30 – 2:30 pm	
6. Questions, Discussions, Exercises	120	2.30 – 4.30 pm	

A Short Course Work for SEEDS Practitioners – Costing and Funding Strategies			
Day 4 – Thursday			
Activity	Duration (mins)	Time	Responsibility
1. Recap of Day 3	30	8:30 – 9:00 am	
2. Module 4	120	9.00 – 11.00 am	
3. Tea Break	30	11.00 – 11.30 pm	
4. Practical Illustration and Exercises	120	11:30 – 1:30 pm	
5. Lunch Break	60	1:30 – 2:30 pm	
6. Practical Illustration and Exercises	120	2:30 – 4:30 pm	

A Short Course Work for SEEDS Practitioners – Costing and Funding Strategies			
Day 5 – Friday			
Activity	Duration (mins)	Time	Responsibility
1. Programme Evaluation and Action Plan	120	9:00 – 11:00 am	
2. Tea Break	30	11.00 – 11.30 am	
3. Closing Ceremony	30	11.30 – 1.30 pm	

GOALS OF THE TRAINING PROGRAMME

GOALS OF THE TRAINING PROGRAMME

To enable Practitioners to:

- 1 Establish the Link between SEEDS targets, strategies, costing and budgeting
- 2 Identify the current challenges of SEEDS implementation
- 3 Use Activity Based Costing technique to cost SEEDS strategy
- 4 Identify the various sources of funds for SEEDS
- 5 Adopt measures to increase internally generated revenue
- 6 Make revenue projections using acceptable forecasting techniques
- 7 Adopt sustainable debt management strategies

REFERENCE MATERIAL

Federal Ministry of Finance (Budget Office) and World Bank Training Material on 2007 – 2009 Medium Term Sector Strategies (MTSS)

Gill, Jit B. S., (2003) Nuts and Bolts of Revenue Administration Reform

Makridakis, S, and Wheelwright, S.C., (1989) Forecasting Methods for Management, Fifth Edition

National Planning Commission, (2005) SEEDS NIGERIA MANUAL

Svensson Maude, (2006) PRSP Costing Manual for Developing Countries.

MODULE 1 - INTRODUCTION

OUTLINE

- 1.1 Overview of The SEEDS Framework
- 1.2 Linkage between Targets, Strategies, Costing and Budgeting
- 1.3 Current Challenges of SEEDS Implementation Process

LEARNING OBJECTIVES

At the end of this module, participants will be able to:

- Explain the stages of the SEEDS framework
- Discuss the linkage between targets, strategies, costing and budgeting
- Analyze the challenges faced in the implementation of SEEDS

1.1 OVERVIEW OF THE SEEDS FRAMEWORK

State governments in the country have evolved their economic development blueprint referred to as State Economic Empowerment and Development Strategy (SEEDS) or its equivalent. In consonance with the National Economic Empowerment and Development Strategy (NEEDS) at the federal level, the goals of SEEDS are:-

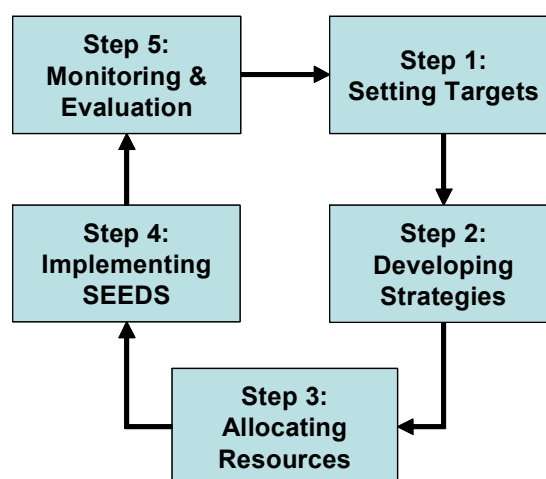
- I. Wealth Creation,
- II. Employment Generation,
- III. Poverty Reduction, and
- IV. Value Re-orientation

These goals of SEEDS are to be achieved by empowering people, promoting private enterprise, and changing the way government works, which are the tripod pillars giving support to the goals. For a good understanding of the SEEDS process, there is need to put its framework in proper context.

The SEEDS framework comprises the entire gamut of SEEDS processes and stages from setting targets through deciding strategies, allocating resources, implementing SEEDS, to monitoring and evaluation. The SEEDS framework anticipates “a reasoned and fully costed strategy”, showing how the goals set in SEEDS will be met. The SEEDS Manual presents a structured approach to achieving the strategy and shows step by step how to implement the programmes needed to make a reality of the targets that have been set.

The step by step approach is titled the SEEDS Framework. It is based on the standard strategic planning cycle shown in Figure 1.1 below:

Figure 1.1: The SEEDS Framework



However, one of the weaknesses of the SEEDS documents in many states is lack of realistic costing of the strategies to ensure affordability.

1.2 LINKAGE BETWEEN TARGETS, STRATEGIES, COSTING AND BUDGETING

A target is a quantifiable or quantified goal/objective that helps to improve performance through planned and output directed activities.

Strategies describe how to achieve the targets that have been set from government policies. But strategies can not be implemented until the programmes and projects contained in them have been costed.

Costing is the process of calculating the value of resources required to undertake the programmes and projects contained in the strategy. It is only when the

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cost has been correctly estimated that it will be possible to tell if the targets are truly achievable. Analysing the cost implications of a particular SEEDS milestone will indicate whether a particular target is achievable or realistic. Costing facilitates an assessment of the resource requirements for implementing the strategies in SEEDS. As such, costing gives an indication of the funding requirement including the human capacity for implementing SEEDS.

Costing will enable government service managers evaluate the feasibility and affordability of different strategies, and determine an appropriate budget for the selected strategies. To make a choice between possible alternative strategies, it is important to quantify the differences between them. This can only be assessed if information on the cost of implementing each possible strategy is available. This presents costing as an interface between strategy formulation and implementation.

Costing is a critical element of allocating resources in the SEEDS framework. The other segment of allocating resources is budgeting, which is built on the Medium Term Sector Strategies (MTSS).

The MTSS is an aggregation of the prioritized strategies of all the ministries, departments and agencies of government over a period of about three years. With the MTSS, annual budgets of MDAs are consistent with their Medium Term Strategies, the Fiscal Strategy Paper, SEEDS and MDGs. Furthermore, expected outcomes and outputs from MDAs spending are clearly defined, monitored, variances explained and communicated to the people. This will result in greater value for money spent.

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Directly linked to the MTSS is the Medium Term Expenditure Framework (MTEF). MTEF is an annual rolling three-year expenditure planning process. It consists of the following components:

- Estimate of aggregate available resources pooled on a three year basis;
- Three year capital and recurrent costing of strategies of sectors based on sectoral analysis; and
- The allocation of aggregate resources to these strategies based on priority.

MTEF is designed to:

- Achieve macro-economic stability without compromising economic development;
- Direct the bulk of public spending to the state's strategic priorities as articulated in SEEDS and for the attainment of the MDGs;
- Assure predictability of funding; and
- Improve the value for money of state spending.

MTEF is a three stage process comprising:

- A Medium Term Fiscal Framework (MTFF) which documents a set of integrated medium-term fiscal policy objectives as well as fiscal targets and projections, including resource availability.
- A Medium Term Budget Framework (MTBF) which documents medium term budget estimates for individual spending agencies based on the state's strategic priorities and in a manner consistent with overall fiscal objectives.
- A Medium Term Expenditure Framework (MTEF), which consolidates the MTBF of spending agencies and adds programme and output-based budgeting.

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The benefits of MTFF, MTBF and MTEF are:

Medium Term Fiscal Framework (MTFF)

- Achieves the right balance between economic development and macro-economic stability.

Medium Term Budget Framework (MTBF)

- Directs the bulk of state spending towards capital spending on the state's priorities and ensures that budget holders are accountable for monies allocated to them.

Medium Term Expenditure Framework (MTEF)

- Adds programme and output based budgeting. This affords opportunity for comparing agreed output with actual output and identifying variances.

1.3 CURRENT CHALLENGES OF SEEDS IMPLEMENTATION PROCESS

At the moment, there are numerous challenges faced by states in their SEEDS implementation. The SEEDS is either not properly prepared or implemented or both. This explains why development in states is not correlated to the quantum of resources used by them.

In specific terms, the challenges facing states include:-

- I. Weak Prioritisation: Resource constraints impose restrictions on what states can do at a time. This underscores the need to prioritise so that resources are not spread too thinly and that value for money is guaranteed in government's quest to provide services for the people. The MTSS is very central to good and strong

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prioritisation. However, most states still do not have their MTSS and consequently no prioritisation or at best weak ones.

- II. Over-ambitious medium term targets: Targets derive from state policies, but a review of states' targets contained in SEEDS revealed that they are not specific, measurable, achievable, realistic and time bound (SMART). When targets are not SMART, they display over-ambitiousness. This problem arises from the fact that most states lack baseline data for setting targets and the human capacity is also weak. As such, even when state targets look good they may not be attainable, since they are not based on historical performances and the resource profile of the state.

- III. Inadequate Links Between Targets, Strategies and Projects: A major problem with most SEEDS is that they do not have 'reasoned and fully costed' strategies. What states call targets in their SEEDS documents are mostly not targets. Some targets do not benefit from the policies of government. In the same vein, there is a very weak link between targets and strategies. This portrays a problem of incoherence in most states' SEEDS. But it is the projects/initiatives contained in the strategies that are the objects of costing. Thus, if the strategies are not linked to the targets and by extension to the policy thrust of government, the overall development agenda of states would be difficult to achieve.

- IV. Limited Unit Cost Data: For costing to be meaningful, it must be based on a reliable data base. There is need for the costing expert to be abreast of the unit cost of the various initiatives to provide information on the likely cost of the projects. This will allow for an analysis of projected income and expenditure. Unit costs data is unavailable or untimely, unreliable and conflicting. The Budget Monitoring and Price Intelligence Unit (BMPIU) in the Presidency provides unit costs for MDAs at the federal level. This agency can be replicated at the state level to ease the problems of data, particularly unit

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cost, in costing initiatives and procurement practices.

- V. SEEDS not fully costed: From the above problems, it is not surprising to observe that most states do not have a reasoned and fully costed SEEDS. This problem stems from inadequate coverage of all the initiatives and the fact that the recurrent cost implications of the capital projects are often ignored during costing

SUGGESTED EXERCISES

1. List and discuss the major steps in the development of the SEEDS framework.
2. Is there a logical sequence to the steps in the development of the SEEDS framework? Explain.
3. What are the elements in allocating resources in the SEEDS framework?
4. Based on your understanding of MTEF what will be the benefits of adopting this approach in your state?
5. What are the challenges faced by your state in its SEEDS implementation? Suggest ways of overcoming these challenges.

MODULE 2 – COSTING

OUTLINE

- 2.1 Concepts of Cost and Costing
- 2.2 Benefits of Costing
- 2.3 Framework for Costing
- 2.4 Approaches for Costing SEEDS
- 2.5 Types of Cost and Cost Behaviour
- 2.6 Capital and Recurrent Costing
- 2.7 Prioritisation of SEEDS Strategies
- 2.8 Practical Illustration of Costing

LEARNING OBJECTIVES

At the end of this module, participants will be able to:

- Discuss the concept and benefits of costing within the context of the SEEDS framework
- Analyze the framework and approaches for costing SEEDS
- Identify the types of costs and discuss how costs behave
- Apply appropriate costing techniques to capital and recurrent costing
- Discuss prioritisation issues in costing SEEDS strategies

2.1 CONCEPTS OF COST AND COSTING

Cost is the value of resources used in the process of achieving set goals. It is the value in monetary terms, of all inputs, tangible and intangible, used in the provision of services, production of goods or the achievement of specific goals. Cost refers to the total materials, labour and other overhead utilised to achieve specific objectives.

Costing is a process of quantifying the resources required to implement the strategies of SEEDS.

Targets are important because stressing the need for realistic and achievable targets.

2.2 BENEFITS OF COSTING

There are several benefits of costing. These include:-

- Costing contributes to transforming strategies (i.e. SEEDS) to action plans that are financially monitorable via annual and medium-term budgets.
- It gives an answer to what it takes every year in terms of human resources, infrastructure, and financial resources to meet development targets.
- It provides important guidance on implementation to policy makers, especially on efficiency of budget allocations.
- It offers important guidance to policy makers and donors on funding
- It provides an important input for strategies on increasing revenue and funding.
- It serves as a financial basis for prioritising and monitoring strategies and programmes.

2.3 FRAMEWORK FOR COSTING

Costing is intrinsically linked to the government's budgetary and planning processes and its fiscal and absorptive constraints. These two constraints need to be fully accounted for in the process of costing since they can undermine the implementation of SEEDS. They can prevent both scaling-up and sustaining current level of interventions, therefore making the achievement of MDGs, SEEDS and/or other development targets harder.

Strategies for improving absorptive and fiscal constraints must therefore be integrated in the costing process. Proposed development targets must be technically feasible and efforts to attain them must be fiscally sustainable.

Absorptive and fiscal capacity is not static – they can increase through a number of measures. But initial conditions will determine how far and how fast capacity constraints can be relaxed. Reforms to build human capacity and institutions are crucial element for increasing absorptive capacity. Fiscal capacity for pro-poor spending can be improved through:

- Reallocating public spending from less prioritised expenses,
- Enhancing efficiency in current public spending (with focus on non-discretionary expenses),
- Increasing internally generated revenue (focus on taxes),
- Increasing external funding (focus on scaling-up foreign aid).

2.4 APPROACHES FOR COSTING SEEDS

The most common costing methods are a top-down approach, the bottom-up costing, incremental costing based on past budget allocations and activity based costing, which combines the key features of the first two approaches. The choice of costing method adopted would depend on sector specifics, stage of project cycles, and the sophistication of budgets.

All four methods have their advantages and disadvantages, and in reality costing often includes parts of all four

2.4.1 TOP-DOWN MODEL

The top-down model provides a macro perspective and builds on assumed relationships between economic growth, poverty reduction, productivity and investment/savings ratios. This type of model would typically generate an estimate of the required investments needed to take place if the state is going to attain its SEEDS targets. The top-down model is therefore helpful as a framework to analyse the realism in more detailed costing and to analyse trends.

2.4.2 BOTTOM-UP COSTING

Bottom-up costing builds on thorough sector and sub-sector knowledge and involves sectoral experts. It necessitates field trips, detailed analysis of baseline statistics and state-specific, disaggregated unit costs

For budgeting purposes, a simplified version of the bottom-up approach is preferable since it will involve sector specialists and generate fairly detailed estimates that can be allocated proper budget classification codes, consistent with those used in the

accounting system. This approach is also suitable for capacity building in costing, budgeting and planning. The biggest drawback is that this approach is time consuming and labour intensive and therefore more costly to undertake than the other methods.

Bottom-up costing comprises the following steps

- Sector teams identify and define ambitious but realistic targets for progress, based on SEEDS. Based on these targets, policies and interventions are developed.
- To monitor progress, quantitative targets are established for the long-term, and divided into shorter-term monitorable input indicators. For example, in order to reach the target of universal basic education, input indicators will include numbers of teachers and classrooms, enrolment rates, the pupil-teacher-ratio (PTR), teaching materials, etc.
- Each sector team estimates recurrent and capital costs of each intervention, using disaggregated unit costs, baseline statistics, and transparent and simple cost models.
- In parallel with the sector work, an overall core team takes responsibility for leading an iterative process to maximize synergies, avoid duplications, and ensures cross-sector consistency, resulting in further refinement of cost estimates.
- A financing strategy is developed by matching the estimated costs with available resources and the possibility of increasing the latter. In this way, financing gaps are estimated.

2.4.3 INCREMENTAL COSTING

A third approach is to undertake incremental costing that builds on details of the current budget and assumed ratios for increasing or decreasing activities. This method is less precise than the bottom-up model but more detailed than the top-down method.

Currently, the use of incremental costing has been abused by State planning officials. Financial regulations allow each year's recurrent budget to show an increase of up to 10% without being reviewed in detail. Based on this, officials simply undertake incremental budgeting, i.e. taking last year's budget and adding a little to it. The justification for the extra money and how it relates to any changes in the services offered may not be reviewed at all.

2.4.4 ACTIVITY BASED COSTING

Activity Based Costing combines the features of top-down and bottom-up costing. It brings together all the costs related to one activity, i.e. capital, staff recurrent and other recurrent costs. This makes it possible to calculate the full unit cost for each activity. These are needed for the following:

- Estimate the cost of increasing service outputs;
- Assess the cost to meet a given SEEDS target;
- Evaluate the relative cost of different strategies;
- Identify the potential for efficiency gains;
- Find the correct balance between capital and recurrent expenditure;
- Assess the recurrent implications of capital spending.

For the purpose of taking SEEDS from strategy to action, activity based costing is recommended. Two things are required to prepare the activity based costs for a particular SEEDS target. These are:

- The costs for the current service: capital, personnel and overhead, per unit of output.
- The next year's milestone on the road map to the target in terms of the number of units of output to be delivered.

2.5 TYPES OF COST AND COST BEHAVIOUR

2.5.1 TYPES OF COST

There are different types of costs. It is important to understand these types of cost and take them into account to inform the selection of SEEDS strategies, in order to build realistic and complete budgets for the chosen strategies. The various types of costs are:-

Capital Costs: Costs that relate to the creation of fixed assets, for example, a new school, hospital, roads, utilities, infrastructure, etc.

Recurrent Costs: All other costs which are operational costs of delivering services, for example staff costs, provision for consumables, supplies and expenses, etc.

Within recurrent costs, direct and indirect costs can be distinguished.

Direct Costs: Costs (materials, human resources and expenses) that can be directly linked to the delivery of the service.

Indirect Costs: Costs (materials, human resources and expenses) that are not consumed directly, but are essential to the delivery of the service.

However capital and recurrent costs can further be divided into three elements - materials costs, human resources costs, and expenses. These are further elaborated as follows:

Materials costs cover cost of all materials which are consumed in the delivery of the service (for example, books in a school, treatment chemicals in a water plant, and medicines in a hospital).

Human resources costs cover all the costs of directly employing staff, including salaries, allowances, pension contributions etc (these are often separated in different lines of government budgets, so it is important to ensure that all of the elements are taken into account).

Expenses cover all of the intangible requirements involved in the delivery of the service (for example, maintenance contracts for essential equipment, leases, fees or charges etc).

Unit Costs: Unit cost is the total cost of a unit of input or output (service). For example, on the input side: we can determine the unit cost of a teacher as:-

Salary + allowances + expenses (for example travel costs which are reimbursed) + annual costs of training + administrative overheads relating to the employment contract.

We can then use this cost as a shorthand estimate which can easily be multiplied by the number of teachers to arrive at a reasonable estimate of the total

cost of, for example, employing an additional 100 teachers.

On the output side, although it is a more complex calculation, we can determine the cost of a 'pupil/year' or term or day etc (this is a composite unit cost) by:

- Determining the current total relevant cost e.g. of delivering primary education (direct and indirect, recurrent and capital costs).
- Determining the quantity of service units delivered e.g. the number of 'primary school pupil years'.
- Dividing the current total relevant cost by the quantity of service units delivered will give us an estimate of the current actual cost per primary school pupil/year.

Unit costs are an extremely useful tool in public service planning and budgeting, particularly when existing accounting and information systems are insufficient to provide actual cost information at the operational level. However, they do have their drawbacks and can mislead managers, primarily because they fail to take account of the different types of cost behaviour described below.

By bearing this classification of costs in mind, SEEDS planners and implementers can be more confident that they have included all relevant costs when making comparisons between possible strategies, and that budgets based on this analysis will be more realistic.

The different types of costs are presented in the figure below

Figure 2: Types of Costs

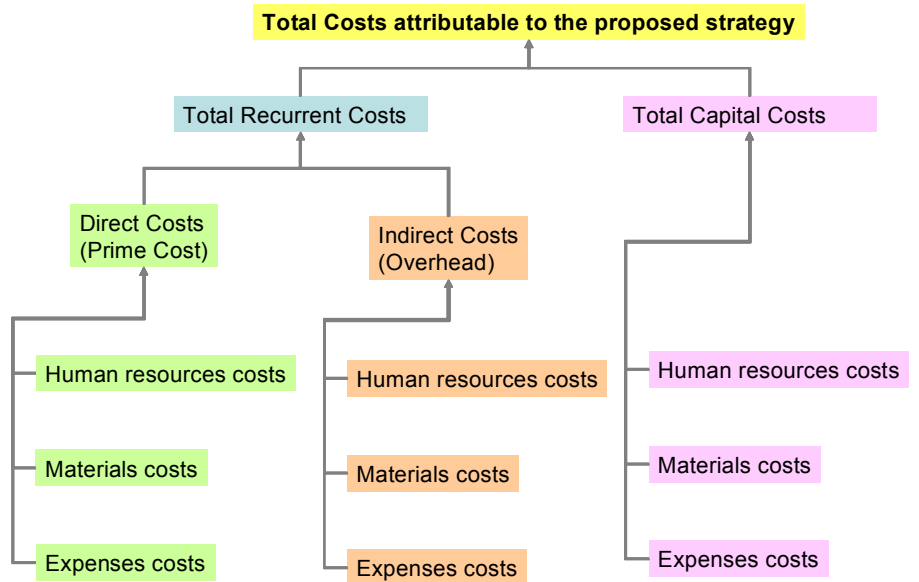
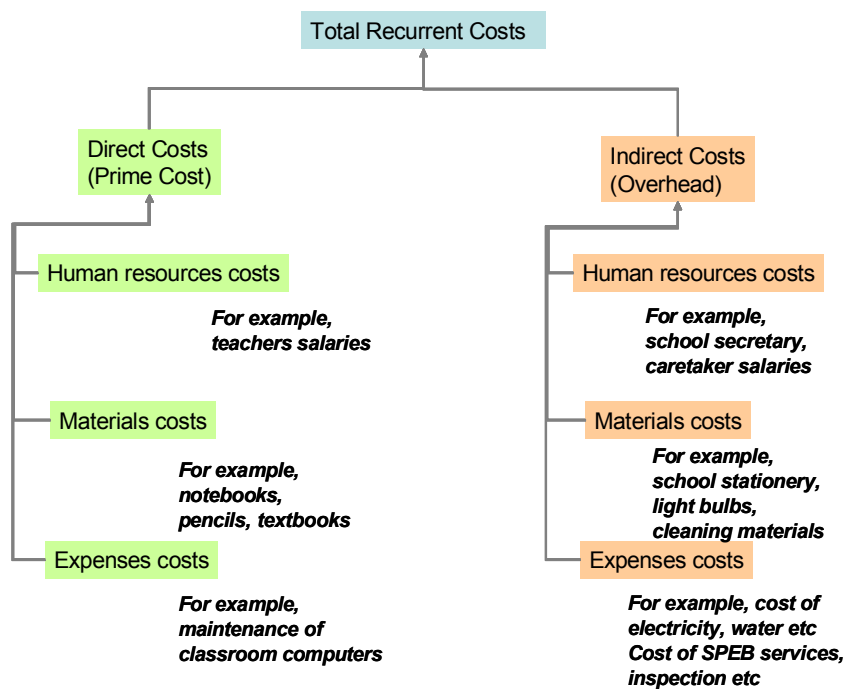


Figure 3: Distinction between Direct and Indirect Costs- A School Example



2.5.2 HOW COSTS BEHAVE

The categorisation of costs into capital costs and direct and indirect recurrent costs is very useful when trying to assess the cost of increasing services. Costs behaviour is considered below:

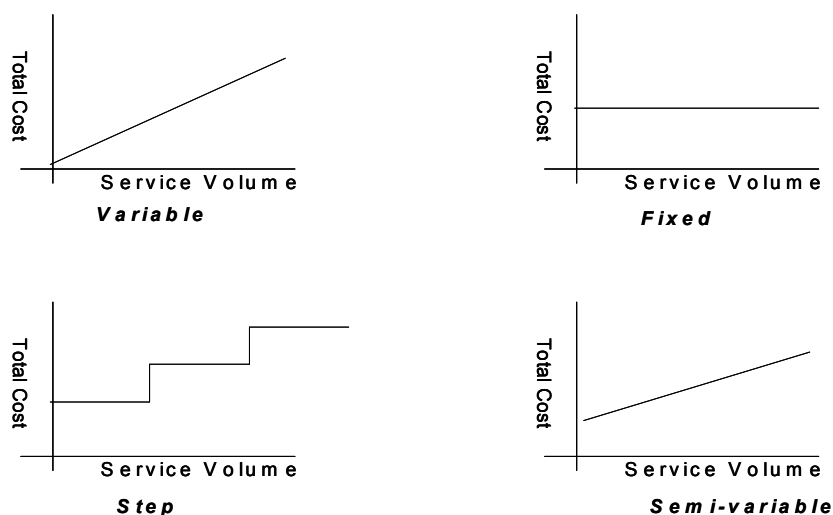
Variable Costs: These are costs that increase directly and in proportion with increasing volumes of service. Generally, only material costs are truly variable (for example, each additional patient treated for malaria will increase the costs of malaria drugs provided).

Fixed Costs: These are costs that do not increase with increasing volumes of service within defined limits. Generally, these will be maintenance-type costs (for example, a school may accommodate between 100 and 500 students before we need to consider acquiring an additional building). In reality, few costs are 'fixed' in the long run.

Step Costs: These are costs that remain fixed over a range of activities. For example, increasing the number of pupils in a class from 10 to 30 will not require an additional teacher. At 31 pupils, we will require an additional full-time teacher, so the cost will rise in a 'step' of one teacher's salary, but will then remain fixed until we reach 60 pupils.

Semi-variable (Mixed) Costs: This occurs where part of the cost is fixed and part is variable. For example some utility charges are made up of a standing charge which does not change regardless of the volume of the utility consumed, and a variable charge which increases with each unit consumed (for example electricity costs).

Figure 4 below illustrates different cost behaviour graphically.



Knowing how costs behave as the volume of service increases enables SEEDS planners to consider the cost implications of varying levels of service increase. For example, the decision as to whether a particular strategy is affordable is related to the scale of service increase being considered. By knowing how each cost behaves, we can calculate the total cost for a variety of 'scenarios' (such as different levels of increase in service volumes) almost as easily as we can calculate the cost for one level. This will then allow SEEDS planners to set a series of milestones (for example, to gradually increase the number of primary education places over a number of years as this can be afforded).

2.6 CAPITAL AND RECURRENT COSTING

A core requirement of the SEEDS framework is to complete a 'reasoned and fully costed strategy'. It is only when all costs are included in estimates that it is possible to determine if policy targets are truly achievable. In addition, costing strategies properly

ensure that the budget includes funds for all costs of projects and programmes.

The current practice in Nigeria emphasises capital investment while recurrent expenditure is seen as unproductive. Activity based Costing (ABC) is a tool for including all costs required to deliver services. It ensures that both capital and recurrent expenditure relating to an investment proposal are fully estimated and captured. The use of ABC reveals that an investment proposal may not involve only capital expenditure. Most capital investments have recurrent cost implications. In fact, in some cases, the implementation of a strategy would involve only recurrent expenditure or more recurrent than capital expenditure.

Estimates of capital and recurrent costs in the budget under the SEEDS framework must be driven by targets and strategies. In order to ensure that a particular SEEDS target is fully achieved, there is need for a commitment to make sufficient funds available to cover the initial capital investment as well as the incremental recurrent cost required to provide the service during the life of the project or programme.

For example, a new hospital project will require making an investment in building a hospital structure as well as recurrent costs to provide staff, medicines, electricity, water, etc. A road project needs annual maintenance. If the best way to raise school attendance is to provide free school lunches and more textbooks or to raise teaching standards by training, only recurrent expenditure is required. A programme to reduce mother and child mortality may not require investments in new clinics and hospitals but only increased recurrent costs, for example, providing more medicine and additional doctors and nurses.

There may be cases in which high levels of recurrent expenditures are not productive. However, this does not imply that SEEDS strategies can be implemented successfully with reduced recurrent estimates in budgets. If a State Government believes that an overall reduction in recurrent expenditure is necessary, a full review of all estimates in the budget will be needed to identify where savings can be made to release resources for the implementation of more SEEDS projects and programmes. There may also be need to analyse the impact capital investments have on recurrent costs, in cases where investments are made to reduce recurrent costs by increasing efficiency.

The costing of SEEDS cannot be undertaken as a separate programme but should be integrated in the State Government's existing operation and budgets. This is to avoid dual budgeting, which distorts the way government works and adds to the impression that development only affects the capital budget.

In line with the Medium-Term Expenditure Framework (MTEF) the costing of capital and recurrent implications of all SEEDS strategies should be undertaken for a three year period, involving multi-year fiscal forecasts and forward expenditure cost estimates on a rolling annual basis. This facilitates the development of realistic macro-economic forecast of the total resource envelope, comprehensive sector ceiling for resources as well as capital and recurrent costs estimates of resources required to meet the objectives of government for a three year period.

2.7 PRIORITISATION OF SEEDS STRATEGIES

Prioritisation is a central part of the process of producing implementable costs of SEEDS strategies. It

involves the allocation of resources between sectors and within sectors. The process of setting targets helps to prioritise the allocation of resources. In general, the focus is on prioritising activities in areas where clear targets have been set rather than in areas that have not been assigned any targets. Therefore, the process for setting targets should be participatory, in order to stimulate broad support for targets that governments can and will be held accountable for. Targets indicate priorities for the allocation of public expenditure, but in the costing process targets must be operationalised into a prioritised and sequenced list of interventions necessary for achieving the targets.

This implies limiting and properly sequencing the set of interventions to those that can most likely be achieved, given capacity and political constraints over the time horizon of SEEDS. Financing constraints need to be recognised, together with an understanding of costs and a willingness to reallocate budgets from lower priority to higher priority sectors and sub-sectors. Cost effectiveness is one of the bases for prioritising, but there are also many other considerations that need to be integrated into decisions on prioritising. It has to be recognised that prioritisation is both a technical and political process, hence the possibility for conflicts.

Experience from some countries where attempts have been made to prioritise the costing of development programmes suggests a multi-criteria approach to priority setting, which ensures that priority setting is transparent and participatory. Performance matrices could be constructed through a series of group discussions with policy makers based on the criteria below:

- Cost-effectiveness;
- Poverty reduction;

- Needs of target groups for services to be provided;
- Budget impact; etc.

Experience has shown that policy makers give high value to interventions that are cost-effective, reduce poverty, target the young, or target people with high need for services to be provided by projects or programmes.

To provide the necessary information for decision-making, SEEDS planners must estimate the costs of the various strategies to be considered. However, the decision on which strategy to adopt will not merely be based on simple comparison of total cost. Alternative strategies will need to be compared using financial as well as non-financial criteria, such as:

- Scoring each possible strategy according to how well it is expected to achieve the target and related objectives. In order to do this, planners must be very clear about all of the criteria against which they wish to assess the possible strategies.
- Comparing the tangible quantitative dimensions – measurable costs and measurable benefits (volumes of service) which each will deliver. This is known as ‘cost effectiveness analysis’. For strategies which largely comprise recurrent costs, then a simple comparison of unit costs may be sufficient for this dimension. Strategies which involve significant capital investment may require more complicated appraisal which reflects the different phasing of costs and benefits (for example, building costs for a new road are ‘upfront’, while benefits will be derived over many years.)
- Making an assessment of the intangible (often social and environmental) costs and benefits. This is generally difficult and expensive to determine, and

would only be included if a full Cost Benefit Analysis is undertaken.

- Considering risks and uncertainties – both the direct risk that the strategy selected may not achieve the target, and indirect risks (for example, if a strategy proposes contracting out the delivery of a service, there is a risk that if the contractor fails, government will no longer have the resources to resume direct delivery)
- Considering affordability: for example in a climate of capital rationing a project which has primarily recurrent costs is more likely to be fundable from the budget than one which has high capital costs. In a climate of recurrent budget restraints, it may be easier to find funds for capital projects. A strategy which is to be implemented over a number of years is likely to be more affordable than one which requires very high volumes of short-term investment.

2.8 PRACTICAL ILLUSTRATION OF COSTING

State Economic Empowerment Development Strategy (SEEDS) 2008 – 2010

Target

- Increase primary school enrolment from 250,000 to 310,000 (Milestones 25,000 in 2008, 20,000 in 2009 and 15,000 in 2010)

Strategies:

- Construction of new primary school blocks, renovation of existing schools blocks (both in urban and rural areas) and school meal for pupil of 3 disadvantaged rural local governments.

Assumptions - Year 2008

1. That the demand for primary school places will increase by 10%
2. 40 pupils per classroom
3. There are 100 blocks requiring renovation
4. 20 additional blocks (5 classrooms per block) are required to meet the 10% target.
5. The estimated primary school population in three rural local government areas is 32,000, of which 18,000 currently go to school. School meals are an effective way of encouraging the remaining 14,000 pupils to attend school

Strategies	Capital Requirement (quantity)	Recurrent – Direct Requirement (quantity)	Recurrent – Indirect Requirement (quantity)
Construction of new school blocks	20 class room blocks (100 class rooms) 4000 class desk and seats	Teachers 120 (1 per class room and additional 20 for 5 new schools) Support staff 15 (per new school)	School running costs Textbooks Maintenance Training of staff
Renovation of existing school blocks	100 class room blocks 15,000 class desk and seats	Additional teachers 200 Additional support staff 60	School running costs Textbooks Maintenance
School meals			32,000 school meals per day for 140 days

COSTING

Type of Cost	Activities	Capital Implications	
		Unit Cost (N)	Cost (N)
Capital			
	20 new class room blocks	5,000,000.00	100,000,000.00
	Renovation of existing class room blocks - 100	1,500,000.00	150,000,000.00
	19,000 new class room desk	3000.00	57,000,000.00
Recurrent Personnel	New Teachers – 320 (Annual Salary)	15,000.00	4,800,000.00
	New Support Staff – 75 (Annual Salary)	10,000.00	750,000.00
	Existing Salary of staff (teachers, Support, Administration, Inspection etc)	Various	205,000,000.00
Recurrent Overhead	School lunch 30,200 X 140 = 4,480,000	200.00	448,000,000.00
	Additional school running costs	Various	50,000,000.00
	Additional textbooks	Various	30,000,000.00
	Additional maintenance costs	Various	10,000,000.00
	Existing Overhead costs		150,000,000.00
Total Costs			1,205,500,000.00

Funding Arrangement:

Local Governments: N206, 500,000.00

State Government: N999, 000,000.00

Currently funding of primary education is a joint responsibility for state and local governments. The above local government covers personnel costs.

SUGGESTED EXERCISES

6. What do you understand by the phrase “a reasoned and fully costed” strategy?
7. List and explain the approaches to costing SEEDS.
8. A STATE FARM EXAMPLE:

As part of SEEDS, Ozone state has set two policy targets: 1, increased food production by 20% within 3 years, 2, reduction in youth unemployment by 30% within 3 years. Higher food production will aid economic growth in the agriculture sector. The state also hopes for a reduction in crime and youth restiveness.

The state has decided the best strategy to achieve these targets is to establish a State Farm which will employ young workers. The projected budget is ₦5.3 million: ₦3.8 million in 2005 and ₦750,000 in each of 2006 and 2007. Ozone state government intends to sell the farm output to increase its Internally Generated Revenue. Revenue in the first year is estimated at ₦1.5 million, which will grow by 20% over the next 3 years.

Alternative strategies to increase food production in the state include:

- Supply of additional equipment and other support to existing farmers, whose average age is 58 years, at a cost of ₦1.8 million.
- Establishment of five Zimbabwe farmers, which will require a total support cost of ₦4.5 million.

The state had considered the qualitative and quantitative factors for all three alternatives before choosing the State Farm strategy. Milestones for the strategy are:

- 20,000 hectares under cultivation by Year 3
- 10,000 young farmers mobilised in Year 1, with 5,000 more in years 2 and 3

- Gross revenues rising from ₦1.5 million in Year 1 to ₦1.8 million in Year 2 and 2.2 million in Year 3
- As standard under the Ministry of Agriculture's Line Item Budget, staff have drawn up the following Development Budget for 2005 with indicative figures for 2006 and 2007.

OZONE STATE DEVELOPMENT BUDGET – Agriculture

Item	Estimated cost (₦)		
	2005	2006	2007
Sensitization of the youth	200,000		
Salaries for the youth engaged	100,000		
Land clearing for cultivation	20,000		
Land preparation for farming	30,000		
Irrigation development	50,000		
Building of 2 farm houses	200,000		
Travelling overseas for debt relief	100,000		
Monitoring of farm activities	15,000		
Renovating existing farm houses	70,000		
Purchase of 3 farm tractors	3,000,000		
Maintenance of farm vehicles	15,000		
Purchase of farm inputs	100,000		
Allowances for super eagles coach	100,000		
Text books for adult farmers	<u>100,000</u>	xxxxxx	xxxxxx
Total	<u>4,100,000</u>	<u>750,000</u>	<u>750,000</u>

At the time of writing, it is reported that one of the tractors purchased in 2005 has been repaired five times in the second month of its purchase and is only managing three days work a week. Although sold to the Ministry as brand new, it is clear that the tractor was second-hand and had been refurbished. Its market value should have been ₦450,000, not the ₦1 million paid by the Ministry. The tractor was only used for 3 days in each week due to its frequent breakdown.

Questions

1. Review the development budget shown in the State Farm Example:
 - a. Identify three costs that are not relevant to the State Farm activity.
 - b. Are there any costs, or revenues, which you think need to be added for an ABC?
 - c. Reorganise the State Farm costs into capital, recurrent (personnel), recurrent (other overhead)
 - d. Using any reasonable criteria, allocate costs to the activities for 2006 and 2007. Is the result in line with figure of Naira 750,000 shown in the table?
2. Looking at the State Farm example, have all the recurrent cost implications of the investment been taken into account? Explain your answer.

MODULE 3 – FUNDING

OUTLINE

- 3.1 Sources of State Government Funds
- 3.2 Revenue Forecasting
- 3.3 Measures for Increasing IGR
- 3.4 Sustainable Debt Management

LEARNING OBJECTIVES

At the end of this module, participants will be able to:

- Identify sources of Funds
- Forecast Realistic Revenue
- Identify measures for improving IGR collections
- Explain sustainable debt management strategies

3.1 SOURCES OF STATE GOVERNMENT FUNDS

SEEDS must be implemented consistently and steadily over its life span. In every one of those years, accurate budgets must be supported by reliable funding, which will depend on accurate forecasts of revenues. If this is not done, some programmes and projects will not get the resources allocated to them in the budget and planned SEEDS activities will not be implemented successfully. It is therefore imperative to know the sources of fund available, as this will form a basis for a reliable forecast, costing and prioritization.

There are three broad sources of State Government funds. The sources are:

- Federation Account Transfers
- Internally Generated Revenue and
- Capital receipts

3.1.1 FEDERATION ACCOUNT TRANSFERS

Federation Account Transfers refer to all categories of revenue accruing from the Federation Account. The two main categories of revenue accruing from the Federation Account are:-

- Statutory Allocation and
- Value Added Tax

However periodically the Federation Account Allocation Committee distributes other funds to states, such as; stabilization fund, ecological fund, proceeds from sale of government enterprises, crude oil reserve, etc.

3.1.2 INTERNALLY GENERATED REVENUE (IGR)

The internally generated revenue (IGR) is made up of tax and non-tax revenue. States classify internally generated revenue under the following headings:-

- Taxes – These include Personal Income Tax (Pay as You Earn and Direct Assessment), Withholding Tax, Capital Gain Tax, Pool Betting & Casino Tax, etc.
- Licences – These include Motor Vehicle licence, Motor Drivers licence, Casino licence, etc.
- Fines and Fees – These include fees for registration of land document, ground rent, registration/renewal of business premises fee, fees for registration/renewal of educational institutions, etc.
- Earnings and sales – These include sale of tender documents, earning on hire of government facility/property, etc.
- Rent on government properties – This includes rent on government properties, etc
- Interest, dividends and repayments – These include interest on bank deposits, dividend accruing from government investment on quoted companies, etc.
- Miscellaneous – These refer to other internally generated revenue not classified under any of the above mentioned headings.

3.1.3 CAPITAL RECEIPTS

Capital receipts are special funds raised by State Governments to finance programmes and projects (particularly capital budget). The major capital receipts of State Governments are:-

- Grants from International Development Partners both multi-lateral agencies (such as UNDP, UNICEF, UNEP, UNESCO, etc) and bilateral agencies (such as DFID, CIDA, USAID, etc).
- Grants and Donations from local organisations
- External Loan/credit from World Bank, African Development Bank, etc,
- Internal Loans and Bonds (short, medium and long term) such as bank overdrafts, treasury bills and certificates, short term commercial loans, development bonds, etc.
- Proceeds from sale of Government Properties.
- Proceeds from Privatisation of state owned enterprises
- Contract financing for large projects and private sector funding and partnerships in the form of Build Operate and transfer (BOT), Build Own Operate and Transfer (BOOT) and Rehabilitate Operate and Transfer (ROT) schemes.

3.2 REVENUE FORECASTING

Forecasting is the prediction of a future event, using past data or outcomes and some economic and social indices. It is not an action plan but a way of saying “if we work hard we can achieve this”, based on past trends and a given set of circumstances.

Forecasting is usually based on market survey reports and therefore it is a prediction of what will happen as a result of a given set of circumstances. It does not involve planning for the allocation of resources. A forecast is not a target by itself but an indication of a possible range of targets. They are general statements of expectation of likely outcome of events given some scenarios. It is an input factor for the production of

annual budgets (and in this circumstance costing of SEEDS)

Revenue forecasting is the process of identifying state revenue requirements for any given period of time. The essence of a forecast is to ensure that adequate provision is made to avoid unpleasant consequences in state government operations such as cash shortages, inability to meet legal obligations, disruption in the implementation of SEEDS, etc.

3.2.1 RELEVANT FACTS ABOUT FORECASTING

There are inescapable facts that must be noted while making a forecast. These facts are:

-
- There is no technique by which the future can be precisely foretold.
- The further into the future one attempt to forecast the harder it is.
- There are statistical techniques for analysing time series, and for establishing correlations, so that forecasts of a dependent variable may be derived from forecasts of the independent variables.
- A forecast is based on certain assumptions, and these assumptions should be clearly stated.

3.2.2 CONSIDERATIONS IN FORECASTING REVENUE

There are three important considerations in the revenue forecasting process. They are as follows:-

Formality: The first consideration addresses the formality of the revenue forecasting process and more explicitly

answers questions as to whether the forecast is formally defined, initiated, regularly reviewed, and documented. In addition, it looks at whether any formal forecasting methods are employed. Formality may be a function of different state legal systems and administrative needs, reflected in state or per capita income differences.

Simplicity: A second important aspect is the simplicity of the forecasting process - how cohesive and centralized the organization of the forecasting process is. This aspect refers to the number of agencies involved in producing the revenue and macro forecasts and the number of competing forecasts produced. A more complex system of forecasting involves multiple agencies or multiple forecasts and this may require the support of a formal system that puts in place rules and regulations for effective coordination. Consequently, one would expect that there will be a positive correlation between simplicity and formality.

Transparency: The last identified aspect of revenue forecasting is transparency. It measures whether or not outside agencies are involved in the forecast, if macroeconomic assumptions have been made public, and the level of detail in the budget document.

3.2.3 FACTORS OF REVENUE FORECASTING

The following factors must be considered when making revenue forecasts:

- Revenue base and coverage
- Analysis of the revenue sources
- Legal framework
- Capacity and human resources needed for revenue generation

- Infrastructure and tools to work with
- Political and legal issues – any legislation pending in the National Assembly that may restrict state government activities.
- Climate or weather conditions – for example some revenue sources may be influenced by climate
- Government policies
- The cost of generating the revenue itself
- Extent of economic, commercial, and other activities in the state
- The cash operating cycle.

3.2.4 PROBLEMS OF FORECASTING REVENUE

There are some problems associated with revenue forecast which include:

-
- Inconsistency in government policies
- Inadequate human capacity
- Inadequate information and working tools.
- Linear function is assumed and a change in activity estimation outside the relevant range is difficult.
- Forecasting uses past data, which can only act as a guide. The expected outcome may or may not occur.
- There are many uncertainties in real life situations:
 - political uncertainties
 - policy changes
 - difficulties in establishing trends which may be used in establishing future events
 - changes in economic environment
- Use of computer technology is not very common

3.2.5 FORECASTING METHODS

There are three major methods of forecasting state government revenue.

Judgmental methods

These are methods most commonly used by state governments in revenue forecasts. Such forecasts are often made as individual judgments, committee agreements or decisions, revenue force estimates, jury of executive opinion, pilot survey, etc.

Experience suggests that the vast majority of forecasting done by states is through judgmental methods without the benefit of technological applications as done by private organisation.

Quantitative methods

The second category is the type on which the majority of the forecasting literature has been focused. There are three sub-categories of these methods. These are:

- Time-series methods. These seek to identify the historical patterns [using time as a reference] and then forecast using a time-based extrapolation of those patterns. For example, smoothing of time-series or autoregressive moving average.
- Explanatory methods. The methods seek to identify the relationships that led to [caused] observed outcomes in the past and then forecast by applying those relationships to the future. For example, regression analysis.
- Monitoring methods. These are not yet in widespread use. The methods try to identify changes in patterns and relationships. They are used primarily to indicate when extrapolation of past

patterns or relationships is not appropriate. For example, multiple regression.

Technological methods

These methods address long-term issues of a technological, societal, economical, or political nature. The four sub-categories here are extrapolative [using historical patterns and relationships as a basis for forecasts], analogy-based [using historical and other analogies to make forecasts], expert-based [using a team of experts], and normative-based [using objectives, goals, and desired outcomes as a basis for forecasting, thereby influencing future events]. Examples of extrapolative methods are time-dependent comparisons, historical analogies, an example of expert based method is Delphi method, while an example of normative method is cross impact matrix.

Technological methods will not be appropriate for revenue forecasting given the level of available manpower, technology and data currently available in the states.

3.3 MEASURES FOR INCREASING INTERNALLY GENERATED REVENUE

Internally Generated Revenue (IGR) remains the only revenue source over which the state governments have control. There are various reasons why states need to review and improve IGR performance. First, while IGR policy and various revenue laws create the potential for raising IGR, the actual amount flowing into the government treasury, to a large extent, depends on the efficiency and effectiveness of the revenue administration. Weaknesses in revenue administration lead to inadequate IGR collections.

Secondly, inadequate IGR collections result in policies and programmes being funded through borrowing that could

lead to an unsustainable increase in public debt or inflation. In the alternative, revenue shortfalls shrink the resource envelope, thus, affecting the government's ability to implement its policies and programmes in SEEDS. Unexpected dips in revenue collections also cause budget cuts that result in major inefficiencies in the public expenditure management.

The average percentage share of IGR in the total revenue of states from 2001 – 2005 was 3.7%. It is only Lagos State that received 50.2% of their total revenue from IGR in 2005. The low proportion of IGR to total revenue in most states was as a result of lack of attention of states to IGR potentials. The state governments' efforts to generate more funds from IGR have been very weak and unfocussed.

The measures required to improve IGR generation may vary from state to state, however the following measures will be necessary for most of the states.

- Organisational and Management measures, and
- Operational Measures

3.3.1 ORGANISATIONAL AND MANAGEMENT MEASURES

States IGR accrue from two main sources, tax and non-tax revenue (i.e. Fines and Fees; Licences; Earnings and Sales; Rent on Government Properties; Interest, Dividend and Repayments). Tax revenue is collected by State Internal Revenue Services (the operational arm of State Board of Internal Revenue). Most of the non-tax revenues are collected by various Ministries, Departments and Agencies of state government.

The organisational measures for enhancing IGR may include the following:-

Autonomous Board of Internal Revenue

The placement of the revenue administration within the government structure has significant implications for its ability to muster political support to push needed legislative changes, implement reforms and take strong enforcement actions against vested interests. It also influences its autonomy in using financial resources, hiring and firing staff and taking operational decisions.

States may consider constituting a Board of Internal Revenue (BIR) that has considerable autonomy, but a status less than a ministry. The top management of the Board may be recruited on fixed term contracts. Management should have significant independence in financial, personnel and operational matters, and be accountable for delivering agreed results. Renewal of contracts of top managers should depend on revenue administration performance.

Strengthen Revenue Efforts of MDAs

Most state governments pay little attention to the revenue generation efforts of their respective MDAs. States should consider creating revenue units within the MDAs. The MDAs should have specific revenue targets. The State Board of Internal Revenue should monitor the performance of the MDAs in meeting their revenue targets.

Staff and Management Strengthening

The states need to strengthen the capacity of managers of Internal Revenue Service (IRS) and MDAs revenue units for setting strategic goals; formulating operational policy; managing financial, human, information and physical resources effectively; supervising, monitoring and evaluating performance; improving coordination; anticipating and resolving operational problems; enforcing internal control systems; preventing corruption; improving mechanisms to

redress revenue payers grievances; and interacting with external stake-holders. Training in general management and change management would be very important

Improving the management of the revenue administration is perhaps one of the most challenging areas. First, management improvements inherently require fundamental changes in the behaviour of managers and staff - their sense of the mission and purpose of revenue administration; their desire to make optimum use of scarce resources to meet organizational objectives; their willingness to pursue powerful tax evaders as well as non tax revenue evaders and withstand the resulting political pressure; their commitment to integrity and revenue service; etc. In many states, inefficient management practices have been the norm and it is often very difficult to change the underlying culture.

Second, in management of financial and human resources, revenue administrations are often constrained by laws and regulations that apply to the civil service as a whole. Thus, in many states revenue administration staff are often part of the general civil service. As a result, there is little flexibility to improve their salaries and incentives. This poses a particularly difficult problem with regard to recruitment and retention of good managers, lawyers, auditors and IT professionals needed to run a modern revenue administration. Also, because of outdated disciplinary rules applicable to civil servants, revenue administrations frequently find it difficult to take prompt action in cases of corruption. States should devise the best approach for addressing these issues.

3.3.2 OPERATIONAL MEASURES

Review and improvement of operational measures should include:

Updating and Consolidating Revenue Data

In some states there may be need to conduct detailed surveys to increase the existing taxpayer base as well as other strategic non-tax revenue base. The state taxpayer and other non-tax revenue records should be updated and captured with basic Information Communication Technology (ICT) equipment. States may engage private sector revenue organisations to perform this function. States may need to adopt a unique Taxpayer Identification Number (TIN) which will be allotted to existing and potential taxpayers. In some countries, appropriate legal provisions have been made to make use of the TIN mandatory in transactions with tax authorities, for obtaining various licenses and permits and for significant economic transactions that have tax implications. This compels potential taxpayers to register with the revenue administration. Field surveys to detect unregistered taxpayers, as well as extensive publicity campaigns have often accompanied these drives to allocate TINs. The TIN forms the basic building block for revenue administration IT systems, as it allows the connection of taxpayers to their returns, payments and major taxable transactions with third parties.

Fostering Voluntary Compliance

Voluntary tax compliance is almost absent in Nigeria. Therefore, encouraging it is a major challenge. This may be achieved through the following:-

- Organising revenue awareness campaigns on television, radio, bill board advertisements, etc. This is to make potential taxpayers and other non-tax revenue payers aware of the general concept of taxation and non-taxes revenue and why they should pay.

- Publishing pamphlets and creating web pages providing information on tax laws (as well as other non-tax revenue laws), rules and procedures and changes thereto; organising seminars and workshops for taxpayers (as well as other non-tax revenue payers), providing assistance to taxpayers in filling up tax returns, looking up their accounts to see how much they owe and clarifying doubts on legal and procedural matters; setting up telephone hot lines to answer questions; etc.
- Simplification of forms, reducing the number of steps required to obtain tax clearance certificates, re-engineering of business processes and introduction of better operating process.
- Performance: Voluntary compliance will be enhanced by performance. If citizens are satisfied with the level of service and infrastructure provided by state government, they will be encouraged to pay their taxes and other non-tax bills willingly.

Improved Efficiency in Revenue Collection and Monitoring

One of the major areas of concern in respect of revenue generation at the state level is the degree of leakages. It is a known fact that there is a wide gap between the amount of revenue collected and what eventually gets to the state government treasury. The difference often finds its way into the revenue collectors' pocket. The collectors design several methods to defraud the state government ranging from printing of revenue receipts to manipulating revenue books and records.

States could circumvent this through the following methods:

- Direct Bank Lodgement System (DBLS)
- Regular monitoring of revenue collection process.

Improvement in Enforcement Mechanism

States need to strengthen enforcement mechanism of the revenue process. The aim is to heighten the risk perception and demonstrate the revenue administration's capacity to detect and punish evasion. This is perhaps still the weakest area in revenue administrations in most states. Most states collect tax from less than 10% of potential tax payers. States may explore the option of designating specific courts to handle revenue matters.

Improving Administrative Appeals Mechanism

The Personal Income Act has provision for states to establish a Tax Appeal Commission, which would act as appellate authority of first instance in respect of disagreement between IRS and potential taxpayers on assessed amounts. The Tax Appeal Commission would provide a mechanism for expeditious disposal of such cases. A good appeal process would also improve voluntary compliance as it increases the taxpayers trust in the fairness of the fairness of the revenue administration.

3.4 SUSTAINABLE DEBT MANAGEMENT

Debt management is an important part of a programme to fund SEEDS. Many states have large liabilities: internal loans, debts to suppliers and contractors, pension liabilities and debts to other levels of government. Paying these liabilities absorbs a large proportion of state revenues that would otherwise be available to fund SEEDS programmes and projects. Sustainable debt management entails an effective debt management strategy, debt negotiation and debt monitoring.

3.4.1 EFFECTIVE DEBT MANAGEMENT STRATEGY

For states to avert the debilitating impact of debt burdens, certain lines of action become imperative. In this direction, the following strategies may be adopted;

Growing out of Debt Possibilities

States can grow out of their debt situation through entrenchment of fiscal discipline. They can achieve this by way of sound public expenditure management and the adoption of improved policies that are expected to increase their revenue. Growing out of debt possibilities will require;

- Avoiding extra-budgetary spending,
- Elimination of virement in all its ramifications,
- Transparency and due process in procurement (i.e. elimination of contract inflation),
- Entrenchment of effective resource utilisation through elimination of waste and leakages,
- Increase IGR
- Avoid borrowing from the banking system to finance recurrent expenditure, and
- Reduce subventions to commercially oriented parastatals

Adoption of Sinking or Amortisation Fund

This involves setting aside certain amounts of money at predetermined dates in a special account. This can be done even before moratorium falls due. Adoption of a sinking fund imposes some measure of financial discipline on managers. Redemption of debts/bonds at maturity can

only be done effectively if the amortisation fund is faithfully operated and managed.

Debt Securitisation

This focuses on restructuring the debt tenor through spreading of debt burden, diversifying ownership holding of debt instruments and lengthening of maturity at an attractive rate of interest. Debts owed to banking system can be converted to medium or long term bond at a rate below the prevailing market rate.

Debt refinancing

Debt refinancing often results from mutual agreement between the creditors and debtors to roll over payments over a certain period under new terms and conditions. Debt refinancing can take several forms including the following;

- Refinancing of existing loans by raising fresh or complimentary funds to meet existing obligations.
- Rescheduling the principal part or total of an existing loan by postponing repayment. This may involve rescheduling the interest payment.

Bond Market Finance

This is another way of financing the state's existing obligations. For example, contractors and pension liabilities can be converted into government development stock. For best practice, consent of the beneficiaries needs to be obtained.

Debt Relief

This debt management strategy reduces the contractual value of debt in terms of present value. It refers to change in

the contractual arrangement to make it more favourable to the debtor. It could be voluntarily initiated by the creditor or as a result of a bargaining process in which threat of delay or default or outright repudiation play a role.

3.4.2 DEBT NEGOTIATION

Negotiation is an important preparatory stage of any sustainable debt management process. The primary objective of a meaningful negotiation is to reconcile conflicting interests in the loan proposal and hence provide an avenue for streamlining both recipient and creditor interests with a view to achieving better loan utilisation

3.4.3 DEBT MONITORING

Effective debt monitoring is essential to sustainable debt management. While this has worked in the western world, it is the undoing of the developing countries. In Nigeria, the level of state government debt is not closely monitored. For example, prior to Nigeria's exit of the Paris Club debt most states did not have comprehensive knowledge of their debt profiles. This was as a result of a lack of proper debt monitoring.

3.4.4 GUIDELINES FOR DEBT MANAGEMENT

Debt management guidelines at the state level require the following:-

- Establish a State Debt Management Unit (with qualified and well trained staff, appropriate facilities and equipment, etc)
- Review, catalogue and account for domestic debt
- Carry out reconciliation of each classification of foreign debt with the Federal Government Debt Management Office (DMO)

FUNDING

- Develop a debt management information system
- Formulate a state debt management strategy in accordance with detailed action plan
- Produce a monthly (or quarterly) debt management information report

SUGGESTED EXERCISES

1. From the knowledge of your state:
 - a. List the major sources of Fund.
 - b. What are the major impediments to realistic revenue forecast? As the Director of Planning in your state how would you resolve these impediments?
 - c. What are the weaknesses in Revenue Administration affecting IGR in your state? Recommend appropriate measures to improve IGR.

Magodo State 2006 Audited Financial summary stated as follows:

A: Pensions Liability of N423, 673,900

B: Contractors liability of N2, 456,987,000

C: Total Bank Loan of N5, 004,008,000 (N3, 400,765,000 will mature

In December, 2007)

D: External loan of N6, 098,567,000

E: Some comments of the Auditor General in the report are as follows:

- i) There are inaccuracies in respect of the liabilities
- (ii) There was no breakdown of the Contractors liability and External loans.

1. Question: Recommend options for managing these debts as well as measures that will resolve the comments of the Auditor General.

PRODUCTIVITY OF PUBLIC RESOURCES

MODULE 4 – PRODUCTIVITY OF PUBLIC RESOURCES

OUTLINE

- 4.1 Introduction
- 4.2 Value for Money of Public Services
- 4.3 Supporting Frameworks

LEARNING OBJECTIVES

At the end of this module, participants will be able to:

- Discuss value for money in service delivery; and
- Explain the supporting frameworks for productivity of public resources

PRODUCTIVITY OF PUBLIC RESOURCES

4.1 INTRODUCTION

State government annual budgets contain SEEDS programmes and projects as well as necessary government spending not within SEEDS. The budget expenditure that is within SEEDS varies in different states according to their development status and priorities. In addition, SEEDS targets of most states are extremely ambitious.

Therefore, states operate under certain level of fiscal constraints. This means that states cannot deliver their SEEDS targets without substantial improvement in productivity in public resources.

Productivity is the relationship between output generated by a production or service system and the input provided to create the output. It is measured as the ratio between output and input. Productivity in public resources will be achieved through:

- Value for Money of Public Services
- Supporting Frameworks

4.2 VALUE FOR MONEY OF PUBLIC SERVICES

Value-for-Money of public service is an objective and systematic examination of evidence for the purpose of providing an independent assessment of the performance of a government organisation, programme, activity, or function. This is to provide information required to improve public accountability and facilitate decision-making.

Value-for-Money includes the assessment of the economy, efficiency and effectiveness of the resources an entity uses to achieve results.

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- Economy refers to acquiring the right resources at the lowest cost, i.e. the measure of input.
- Efficiency entails maximising the useful output from the resources utilised, i.e. the measure of productivity (output/input relationship)
- Effectiveness refers to ensuring that the output from any given activity achieves the desired result, i.e. the measure of outcome and goal achievement.

Value for Money Techniques:-

Management and Systems Review: The purpose of this review is to investigate the ways in which objectives are established, policies implemented and results monitored. The emphasis is on how efficiently this process is carried out rather than reviewing the objectives and policies themselves.

Analysis of Planning and Control Process: This involves exploring such questions as ways of comparing the objectives with the needs of the population and methods of identifying activities that are not meeting objectives. The use of investment appraisal techniques and the methods of monitoring projects against the initial appraisal are relevant at this stage. In addition, methods of reviewing operating results should be studied by analysing control and reporting systems and the extent to which they alert members and officers of the need for action.

Efficiency Assessments: This involves the use of checklists of good practice to build up a detailed knowledge of cost-effective practices, and based on this a process would be developed and debated by the auditors with the operating managers. Another method of doing this is to carry out a number of specific investigations into activities with high unit costs, poor performance measures or suspected poor management in order to determine the reasons for adverse

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performance measures and identify the appropriate remedial action.

Effectiveness Review: This involves a study to determine whether activities are achieving their stated aims. This will involve the auditors discussing with the operating managers and committee members on the details of particular services and requiring answers on why the service is provided, the reasons for the service being organised in the way it is, what alternatives have been considered and why have they been rejected and how performances are being measured.

4.3 SUPPORTING FRAMEWORKS

In addition to value for money in public service delivery there are certain supporting frameworks that need to be in place to achieve productivity of resources. Some of the supporting frameworks are:-

- Baseline statistics and unit costs
- Competent and well motivated work force
- Applicable Technology, facilities and equipment
- Improved Financial Management System with proper sanction mechanism
- Transparency and Due Process in procurement of goods, services and works.
- Improved Budget Classification and Chart of Accounts.
- Undertaking regular value for money audit.

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SUGGESTED EXERCISES

1. In the State Farm example in module 2 exercises:
 - a. Are the unit costs reasonable?
 - b. What should have been done to prevent the problems with the tractors?
2. Discuss the supporting frameworks for productivity of public resources

