MPA 752

BUDGETING AND PUBLIC FINANCE MANAGEMENT

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CONTENTS **PAGE**

MODULE 1

UNIT 1 BUDGETING AND BUDGETARY CONTROL DEFINITION AND MEANING OF BUDGETING

CONTENTS

1.0 INTRODUCTION

Every individual or entity engages in budgeting. Budgeting is as old as man. Budgeting is essentially planning for expenditure as a person, group of persons, companies or even a nation. Jesus Christ used budgeting to explain the cost of being a disciple in Luke 14:28-31. Jesus talked of a man who intended to build a tower and did not sit down to do a budgeting. He got frustrated on the way after laying the foundation. Jesus equally mentioned a king who went to war with his 10,000 soldiers without considering the strength of his opponent, (another king who had heavily armed 20,000 soldiers) and lost the battle.

Even a housewife prepares family budget very well and endeavours to keep within the budget limit.

2.0 OBJECTIVES

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

- Describe what budgeting means
- Explain budgeting from the point of views of individuals, groups or corporate entities.
- Analyze different definitions of budgeting.

3.0 MAIN CONTENT

3.1 Definition and Meaning of Budgeting

Budgeting means different things to different people. Wilder Sky (1964) cited by Omolehiwa (1995) gave definitions and interpretations given to a budget as follow:

1. A plan of work
2. A prediction
3. A link between financial resources and human behaviour to accomplish policy objectives.
4. A means for making choices among alternative expenditures
5. In the government it is a record for preferences that have prevailed the determination of national policy.

However, according to CIMA (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.

3.2 Deductions from the Meaning and Definitions:

An analysis of the definitions shows that a budget is:

a. Essentially a plan quantified in monetary terms to attain a given objective.
b. Prepared and approved
c. Prior to a defined period (the budget period)
d. Usually showing planned income to be generated
e. Expenditure to be incurred
f. Capital to be employed during that period.

Hence, budgeting could be classified into long term and short term budgets. Long term budget of ten years is termed as strategic planning. It sets out long-term goals, the general programme of actions, and the allocation of resources to carry out such actions. Long – term budget communicates long term goals. For example, programme for rural electrification. The long term budget defines the parameters with which managers have to draw short-term plans.

The short term budget defines objectives in concrete and quantitative terms for the firm as it provides guidelines as to how to achieve these objectives. The short term budget covers a period in time, monthly or quarterly break up.

4.0 CONCLUSION

The need for a budget arises due to improvement of control in an organization. It forces managers to be accountable for their decisions. So budget is a plan which is agreed in advance. It must be a plan and not a forecast. A forecast is a prediction of what might happen in the future whereas a budget is a planned outcome, which the firm hopes to achieve. A budget will show the money needed for spending and how this might be raised or sourced. Budgets are based on the objectives of businesses or corporate entities.

Information included in a budget may include revenue, sales, expenses, profit, personal, and cash and capital expenditure. For a state, it could include capital and recurrent expenditure. These variables are known as budget factors which can be given value.

5.0 SUMMARY

In this unit, you have learnt that budgeting is as old as man. It has been explained that budgeting is as good as planning and not a forecast which means prediction. It was also discussed that there are both long-term and short term budgets.

6.0 TUTOR - MARKED ASSIGNMENTS

1. What is budgeting?
2. Differentiate between long term and short term budgeting?
3. Who can make a budget?

7.0 REFERENCES/FURTHER READINGS

Ifurueze Mishark ((2006) *Studies in Management Accounting and Finance*

Otokiti and Awodun: (2001). *Managing Business Finance and Investments*

Pandy, I.M. (Professor of Finance) *Financial Management* (8th Ed)

UNIT 2 BUDGETING/BUDGETARY CONTROL PURPOSES AND ADVANTAGES OF BUDGETING

CONTENTS

1.0 INTRODUCTION

Budgeting is a management tool. Many benefits are derived from budgeting, although it is a means and not an end in itself. It is a feed forward process: it makes an evaluation of the variables likely to affect future operations of the enterprise. Budgeting predicts the future with reasonable precision and removes uncertainty to a greater extent.

2.0 OBJECTIVES

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

- Recall the meaning of budgeting
- Recall the definitions of budgeting
- Name the purposes and advantages of budgeting
- Itemize the benefits of budgeting.

3.0 MAIN CONTENT

3.1 Purposes/ Advantages of Budgeting

According to Professor I.M Pandey in *Financial Management* (8th Edition), the following are the purposes and more significant advantages of budgeting:

Forced Planning

Management is compelled to plan for the future. It looks ahead and becomes more effective and efficient in administering the business operations. The habit of evaluating carefully the problems and related variables before making any decisions by managers is instilled or compelled by the process of budgeting.

Coordinated Operations

Budgeting helps to coordinate, integrate and balance the efforts of various departments in the light of the overall objectives of the enterprise. This results in goal congruency and harmony among the departments.

Performance Evaluation and Control

Budgeting facilitates control by providing definite expectations in the planning phase that can be used as a frame of reference for judging the subsequent performance. Budgeted performance is a more relevant standard for comparison than past performance since past performance is based on historical factors which are constantly changing.

Effective Communicating:

Budgeting improves the quality of communication. The enterprise objective, budget goals, plans, authority and responsibility and procedures to implement plans are clearly written and communicated through budgets to all individuals in the enterprises. This results in better understanding and harmonious relations among managers and subordinates.

Optimum Utilization of Resources – Both Capital and Human

It helps in directing total efforts of the firm into the most profitable channels.

Productivity Improvement

Budgeting increases the morale and so the productivity of the employees by seeking their meaningful participation in the formulation of plans and policies, bringing a harmony between individual and the enterprise objectives and by providing incentives to perform more effectively.

Profit mindedness is developed by budgeting and this in turn promotes cost – consciousness.

Management by exception is an offshoot of budgeting. Management attention is focused on significant matters through budgetary reports. It saves the management time and energy considerably.

Budgeting leads to efficiency as managements' self evaluation is permitted and the progress in attaining enterprise objectives.

3.2 Deductions From The Advantages Of Budgeting

If budgets are carried out in a conscientious and effective manner before, during and after budgets are set, they will offer numerous benefits both to the organization and their employees. Those benefits will include.

Managers are compelled to analyze the activities of the organizations.
The attention of management is drawn from the present to the future.

Management can now anticipate projects or opportunities in time and deal with them effectively.

Reference point for control of actions or decisions decided upon is provided.

4.0 CONCLUSION

Budgeting in the views of Professor Pandey and Dr. Ifurueze is a worthwhile activity which leads to efficiency as managements' self evaluation is permitted and objectives of the enterprise are attained.

More so, management is forced to plan and coordinate operations.

There is increase in the quality of communication and optimum utilization of resources.

5.0 SUMMARY

The process of budgeting guarantees the following advantages not only to the individuals but the organization as a whole:

- Acts as a plan
- Performs a coordinating role
- Creates a framework
- Offers an incentive and
- Provides a control facility

6.0 TUTOR - MARKED ASSIGNMENTS

1. Why is effective communication an advantage in budgeting?

2. Despite performance evaluation and control, what other benefits are there in budgeting.

7.0 REFERENCES/FURTHER READINGS

Lian, Maitland (1996). *Budgeting for Non-Financial Managers*

Ifurueze Mishark (2006). *Studies in Management Accounting and Finance*

PANDY, I.M: *Financial Management* (8th Edition).

UNIT 3 BUDGETING AND BUDGETARY CONTROL: APPROACHES TO BUDGETING

CONTENTS

1.0 INTRODUCTION

In this unit, effort will be made to teach you the different approaches or procedures to budgeting. Considering the fact that you can recall the meaning, definition and even the benefits of budgeting studied in the previous units, this unit will be easy to grasp.

The budgetary procedures which take place within businesses will vary from one organization to another. However, most firms will follow a similar series of steps as shown in the diagram or flowchart.

2.0 OBJECTIVES

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

- Name and recall the basic advantages of budgeting.
- Itemize from sales forecast compiled to corrective action carried out.
- Explain the activities of the budget committees in any given organization.

3.0 MAIN CONTENT

3.1 Procedures to Budgeting

The way in which a budget might be prepared is procedural. It is a step-by-step process. The initial step is to decide upon a budget period and state the objectives, which are to be achieved. The budget period may vary according to the type of budget but one month or one year is usually normal.
According to Lain Maitland (1996), the following sequence is typical in most organizations: Compilation of sales forecast. It should be noted that there are differences between a forecast and a budget. They may look the same to all intents and purposes, a forecast sets out what is likely to happen, be required or whatever. Whereas, a budget states what should occur or else!

A sales forecast is drawn up by the manager and his team. They predict what the sales will probably be over the coming months and year, as appropriate. The sales forecast is the first to be compiled simply because majority of firms base their activities and planned expenditure around their anticipated revenues.

The drafting of the production forecast is the next step to be taken into account as it is based on the preceding sales budget forecast. Production capacity, which is the maximum amount that can be produced by a firm over a given period.

This is assessed and undertaken by the production manager and his colleagues. The production levels will be set in relation to estimated sales, whilst taking note of opening stocks and the required closing stock levels which may need to be higher or lower than at the outset. From these figures, direct materials, direct labours and factory overheads can be worked out and allocated as relevant.

The next level is the capital expenditure forecast. This implies that some items may have to be purchased because of exhausted existing equipment, changing technology and the like, with others being offloaded as appropriate. This decision is taken by the finance director or whoever, drawing on the information provided by the sales, production and other departmental managers within the organization.

The drawing of departmental forecast is the next in sequences. With relevant information from the sales and production budget forecasts being made available as necessary, additional budgets will be composed, setting down the revenues and the expenditures within the remaining departments- purchasing, marketing, finance, administration, personnel, distribution etc. These will be put together by the departmental heads/managers and their teams, typically working in close cooperation, with each other. Key data concerning capital goods will be passed to the finance department, or whoever is responsible for creating that capital expenditure budget.

Budget committee receives forecasts in order to vet and consequently approve or amend them. They also draw up a cash budget, budgeted profit and loss account and a budgeted balance sheet. The composition of this committee will vary according to individual circumstances and might be chaired by the finance director or whoever has ultimate responsibility for budgeting within the firm. The various departmental heads who compiled the forecast may act as members.

Master budget is set up by the budget committee, based on information acquired and assessed.

This is a tough and protracted task as it is improbable that all the forecasts will instantly gel together well and adjustments will have to be made to them. It is likely that the finance director or who ever has overall charge will have the last words in the decision making process.

The individual budgets are confirmed by the budget committee as agreement is reached on the master budget. The sales, production, capital expenditure and departmental ones can be established and confirmed by the appropriate departments.

The variation reports are regularly completed in order to adhere as much as possible to the budgets that have been set. A variation report simply records the estimated and actual revenues and, or expenditures which any variances noted along side of them-have to be filled in when major differences exist. Typically in excess of 10%.

Identification of corrective action as noticeable and potentially troublesome variances will be brought to the attention of the departmental manager. He identifies the corrective action needed to remedy the matter. It could be delayed payments, chase up outstanding debts, or whatever to improve poor cash flow situation.

At the end, corrective actions are carried out as identified. Those variances that cannot be remedied and which may have substantial knock-on effects on this and other budgets will need to be passed upwards so that adjustments and allowances can be made.

3.2 Deductions from the Procedures

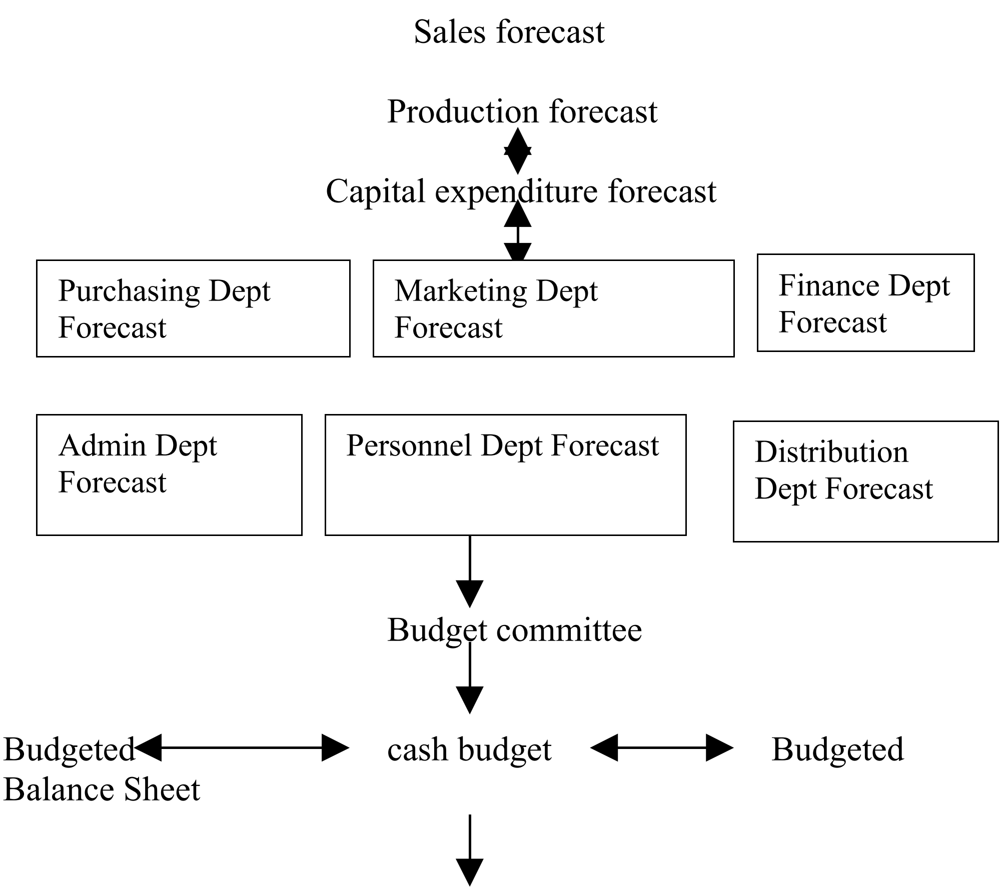
The sequences in which budgets are approached include the following: sales forecast compiled:

- Production forecast drafted
- Capital expenditure forecast composed
- Departmental forecasts drawn up.
- Budget committee receive forecast
- Budget committee confirms individual budgets
- Variation reports completed regularly.
- Corrective action identified
- Corrective action carried out.

4.0 CONCLUSION

It is normal to have a budget of either one month or one year. This is preceded by the intended objectives of the budget which have to be achieved at the end of the day. The preparation of budgets is procedural and is a step by step activity which must follow a sequence as highlighted above.

5.0 A SUMMARY OF THE PROCEDURES



Profit +Lost Acct.

Variation Report

↓

Corrective Action Identified

↓

Corrective Action Taken

6.0 TUTOR - MARKED ASSIGNMENTS

1. What are the sequences or procedures identified between sales forecast and corrective action carried out
2. Which manager heads the budget committee and why?
3. How long do most budgets last?

7.0 REFERENCES/FURTHER READING

Lain, Maitland: (1996).Budgeting for Non – *Financial Manager*.

Ifurueze Mishark: (2006). *Studies in Management Accounting and Finance*.

MODULE 2

UNIT 1 TYPES OF BUDGETS IN THE PRIVATE SECTOR: SALES, RAW MATERIAL PURCHASE AND RAW MATERIALS UTILIZATION BUDGETS

CONTENTS

1.0 INTRODUCTION

As Financial Plans that set out anticipated revenues / and or estimated expenditure over a period of time, typically one year, budget has types. This unit attempts to discuss three types: the sales, the raw materials purchase and raw materials utilization budgets

2.0 OBJECTIVES

At the end of this unit, the students should be able to explain the following:

- Recall the prominent procedures of budgeting
- The sales budget as a foremost type of budget
- The raw materials purchase budget as essential for production
- The details of raw materials utilization budget

3.0 MAIN CONTENT

3.1 The Sales Budgets

Is the foundation on which other budgets are made; it is a detailed plan of sales made by a firm or expected by a firm over a given period, say, a year and sub-divided over a shorter period usually of one month's duration each. The sales budget represents the starting point in any budgeting process because it is the only budget that estimates revenue to be generated in a period. It serves as a coordinator and a pre-requisite for other budgets.

The mechanism of sales budget involves the following:

1. Making a quantity decision which decides the quantity of goods to be produced based on consumer demand over the years.
2. Making a price decision which determines the standard unit price of products after due consideration of production mark up.
3. Making the revenue decision for the period using the following traditional methods:

    a. Committee opinion method
    b. Sales force method and
    c. Statistical method.

3.2 Raw Materials Purchase Budget

This is a detailed plan showing the purchase or materials needed for production in a given period, showing all necessary adjustments made for normal losses in the production process. It is mathematically determined as material usage plus minimum closing stock minus closing stock of raw materials.

3.3 Raw Materials Utilization Budget

Shows a detailed plan of the quantity of raw materials required for a given level of production in a defined period. It is determined by multiplying the budgeted production units by the material mix.

3.4 Deductions from the Main Content

The sales budget is the starting point of every budget because of its detailing of the revenue to be generated by a given organization.

Production budgets are made up of two types – the raw materials purchase and the raw materials usage or utilization budgets.

4.0 CONCLUSION

For a meaningful budget, there has to be sales budget, detailed with its estimated revenue in order to facilitate other aspects of budgeting.

The raw materials purchase budget gives details of materials needed for production in a given period and shows the necessary adjustments made for normal losses in production.

The raw materials utilization budget takes into cognizance the plan of the quantity of raw materials need for a level of production for a given period.

5.0 SUMMARY

Sales budget is a sine qua non to any budgeting due to its revenue generating attribute in budgeting.

Raw materials purchase budget is also prominent as no firm can produce without consideration for necessary input.

The place of raw materials utilization is important due to the detailed plan of the quantity of materials required for a given level of production in a stipulated period.

6.0 TUTOR - MARKED ASSIGNMENTS

1. Discuss the relevance of sales budgets in any given budgeting exercise.
2. Differentiate between raw materials purchase and raw materials utilization budgets in any organization.

7.0 REFERENCES/FURTHER READINGS

Ifurueze, Mishark ((2006). Studies in Management. *Accounting and Finance*.

Lain, Maitland: (1996). *Budgeting for Non-Financial Managers*.

UNIT 2 TYPES OF BUDGETS IN THE PRIVATE SECTOR: PRODUCTION, LABOUR AND OVERHEAD BUDGETS

CONTENTS

1.0 INTRODUCTION

This unit introduces three other types of budget. These include: Production, Labour and Overhead budgets. Effort will be made to give a precise explanation of these types through detailed analysis

2.0 OBJECTIVES

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

- Recall sales, raw materials purchase and raw materials utilization budgets
- Explain the meaning of production budget
- Discuss the labour budget
- Analyze the overhead type of budget.

3.0 MAIN CONTENT

3.1 The Production Budget

Specifies the various quantities of goods to be produced throughout the period in question, as well as the cost of the direct materials, direct labour and factory overheads involved in producing these amounts. Direct materials are those raw items and components parts which are incorporated into the finished goods. Direct labour refers to that part of the workforce, which actually produce the goods. Factory overheads are those other production expenses like indirect materials, indirect labour and heat, light and power.

3.2 Labour Cost Utilization Budget

Is an estimated or cost of the services of employees whose efforts may be directly traced to specific product unit or job centre. This type of budget helps to determine the quantity of the labour and the amount required to satisfy its budgeted level of production directly.

Example: The budgeted production in Baba Agwa PLC is 8 500 chits. It takes the factory worker 3 ½ hours to achieve a unit of the product. The company has policy of paying N4.00 per hour of work done.

Prepare a labour cost budget for the period.

Solution

Baba AGWA PLC Labour cost budget for the year 1995 budgeted production units is 8500 units Labour hour required

8500 X 3 ½ hours = 29, 750 applying wage rate:

₦4 X 29750 hrs = labour cost ₦119,000

3.3 Overhead Budget

Involves budgeting for all indirect expenses, e.g. indirect materials or labour and other cost supporting services incidental to the production process which cannot be traceable to a particular job center or product.

Examples are expenses, repairs, power and heating and depreciation. Manufacturing over head budget is an aggregation of all the various manufacturing overheads and fixed overheads budgeted to be incurred during the production period.

4.0 CONCLUSION

Production budget indicates the various quantities of goods to be produced throughout the period in question as well as the cost of the direct materials, direct labour and factory overheads involved in the production of the quantity.

Labour cost utilization budget discusses the services of the employees whose efforts may be traced to specific product unit.

And overhead involves budgeting for all indirect expenses and other cost supporting services

5.0 SUMMARY

In these three types of budgets, it will be realized that production budget is all embracing. Labour and overhead budgets are all subsets to production budgets.

6.0 TUTOR - MARKED ASSIGNMENTS

1. Production budget embraces labour and overhead budgets. Discuss.
2. Overhead budget can be said to be a hiding place for fraudulent activities! How true is this assertion?

7.0 REFERENCES/FURTHER READINGS

Lain, Maitland: (1996).Budgeting for Non– *Financial Managers*.

Ifurueze, Mishark: (2006). *Studies in Management Accounting and Finance*

UNIT 3 TYPES OF BUDGETS IN THE PRIVATE SECTOR: CASH AND FLEXIBLE BUDGETS

CONTENTS

1.0 INTRODUCTION

In this unit, students will be exposed to more types of budgets and budgeting. These are cash and flexible budgets.

2.0 OBJECTIVES

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

- Recall and discuss production, Labour and Overhead budgets
- Explain cash budgets
- Analyze flexible budget.

3.0 MAIN CONTENT

3.1 A Cash Budget

Is a statement of planned cash receipts and disbursements? It is a financial statement stating cash inflows and outflows for a particular period with a view to highlighting the cash implications of any venture by identifying the problems that could arise; allowing management the opportunity to nip such a problem in the bud.

A cash budget is important in the following ways:

- The availability of cash when required is determined
- The short-term and long term need of capital is promptly estimated
- It helps to establish any cash shortage that may arise and the financial arrangement needed to cover for the shortfall.

In the cash budget: it is expected to locate the following from where receipts of cash may come from.

i. Cash sales
ii. Payment by debtors (credit sales)
iii. Sale of fixed assets
iv. The issue of new shares or loan stock
v. The receipt of interest and or dividends from investments outside the business.
vi. Payroll cost or other operational expenses.
vii. Purchase of capital
viii. Payment of interest, dividend or taxation.

3.2 Flexible Budget

The flexible budget according to CIMA (Chartered Institute of Management Accountants) is one which by recognizing the difference in behaviour between fixed and variables costs in relation to fluctuations in outputs turnover or other variables factors such as number of employees is designed to change appropriately with such fluctuations.

Hence, the flexible budget is structured to change or fluctuate in output. It is a series of budgets designed to change in relation to the level of activity attained for various levels of activity. The knowledge of cost behaviours is a determinant as it is prepared for a range of meaningful production.

The following steps are followed in preparing flexible budgets:

a. Different levels of activity are determined for all the cost ranges
b. At the different levels, fixed costs are expected to be fixed unless in exceptional areas where the plant size changes.
c. All variable cost, elements will vary at each activity level

3.3 Deductions from the Main Content

A cash budget is a financial statement stipulating cash inflows and outflows for a given period. It highlights the implications of any venture in an organization in order to keep the management on their toes.

Flexible budget is a series of budgets designed to change in relation to the level of activity attained, it is prepared for a range of meaningful production due to knowledge of cost behaviour.

4.0 CONCLUSION

A cash budget is essential for indicating the availability of cash when required in an organization. Any cash shortage that may arise is established and prompt financial intervention is undertaken by management.

Flexible budget on the other hand recognizes difference in behaviour between fixed and variable cost in relation to fluctuations in output, turnover or other variable factors.

5.0 SUMMARY

Cash budget is a financial statement expressing the inflows and outflow of cash in a firm for a given period. It determines the availability or otherwise of cash and so prepares management for prompt actions.

On the other hand, flexible budget is structured to change or fluctuate in output. In preparing this, different levels of activity are determined for all the cost ranges. At those levels, fixed cost remains while all variable cost elements vary at each activity.

6.0 TUTOR-MARKED ASSIGNMENTS

1. Why is cash budget very important in any organization?
2. Explain why flexible budgets are not rigid?

7.0 REFERENCES/FURTHER READINGS

Lian, Maitland (1996). Budgeting for Non-*Financial Managers*

Ifurueze, Mishark Esq. (2006). Studies in Management *Accounting and Finance*
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UNIT 4 TYPES OF BUDGETS IN THE PRIVATE SECTOR: MASTER BUDGET

CONTENTS

1.0 INTRODUCTION

In this unit, students will be exposed to the mother of all budgets, the master budget. Details will be given as to why it summarizes all other budgets types.

2.0 OBJECTIVES

At the end of this study, the students should be able to:

- Recall the meaning of cash and flexible budget as discussed in the last unit.
- Name the different types of budgeting studied.
- Explain the meaning of master budget with clear explanations.
- Discuss why master budget is all embracing.

3.0 MAIN CONTENT

3.1 The Master Budget

Represents a summary of all functional or operating budgets of an organization. It includes the sales materials, labour overhead and other financial budgets. It coordinates the revenue expenditure, equipment, capital and other classes of budgets.

In most cases, the master budget is always referred to as the profit and loss account and the balance sheet budget. In effect, the master budget pulls all budgets together, to produce three key documents – a cash budget, a budgeted profit and loss account and a budgeted balance sheet.

A cash budget set down the ongoing cash position of a firm by recording anticipated cash inflows and outflows during the relevant period of time.

A budgeted profit and loss account show firms sales revenue over the period in question and all relevant costs incurred in order to generate the revenue, leaving a profit or a loss on trading activities.

A budgeted balance sheet sets out the firm‘s assets such as equipment, machinery and stocks of raw materials, plus its liabilities like debts to suppliers as at the end of the period.

The following are the steps involved in preparing a master budget.

- Revenue or sales budget
- Production budget
- Direct materials budget
- Direct labour budget
- Factory overhead budget
- Ending inventory budget
- Cost-of-goods-sold budget
- Selling and administration budget
- Budgeted income statement

3.2 Deductions from the Main Content: Master Budgets

The Master budget summarizes all functional budgets of a firm. It is made of three broad subsets or key documents. They are the cash budget which exposes the ongoing cash position of the organization, the budgeted profit and loss account which discusses a company’s sales revenue during a given period and all necessary costs incurred while generating the revenue, leaving a profit or a loss and the budgeted balance sheet which outlines the firms’ assets and liabilities.

4.0 CONCLUSION

The major components of the master budget include the following: sales or revenue, production cost, direct materials, direct labour, factory overhead, ending inventory, costs of goods sold, selling and administration costs and budgeted / income statement (which is made up of sales revenue, cost of goods – sold and selling and administration costs).

5.0 SUMMARY

This unit has discussed the master budget as a summary of operating budgets of an organization. No wonder it is always referred to as the profit and loss account and the balance sheet budget. 2.1 make this clearer.

6.0 TUTOR - MARKED ASSIGNMENTS

1. What constitutes a master budget of a company?
2. Why the master budget is called the profit and loss account and the balance sheet budget?

7.0 REFERENCES/FURTHER READING S

Ifurueze, Mishark (2006). Studies in Management *Accounting and Finance.*

Lain, Maitland (1996).Budgeting for *Non-Financial Managers*.

MODULE 3

UNIT 1 REPARATION OF BUDGETS IN THE PUBLIC SECTOR: BUDGETING SYSTEM IN A DEMOCRATIC STATE

CONTENTS

1.0 INTRODUCTION

Budgeting by a government has been considered a significant and statutory responsibility of the executives. Budgeting however involves the preparation and implementation of budget in a given establishment. It is a financial and, or quantitative statement prepared and approved prior to a defined period of time usually showing anticipated revenue or income and expenditure to be incurred in a given accounting period so as to achieve a basic goal for the establishment.

To the government, budget usually serves as:

a. An estimate of revenue and expenditure for a given fiscal year;
b. A guide towards the execution of the year's activities; and
c. An instrument of evaluating performance.

Based on the information above, budget in the public sector is normally used as an effective instrument for the following.

i. As an instrument for economic policy
ii. Instrument for effective management
iii. Instrument for evaluating performance

2.0 OBJECTIVES

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

- Recall budgeting in the private sector
- Explain budgeting in the public sector
- Narrate the processes of budgeting in a democratic state
- Identify the stages of approval of budgets in the public sector.

3.0 MAIN CONTENT

3.1 Budgetary Process in a Democratic State

The preparation and approval of the Annual budgets are essentially the duties of the Executive and the legislature respectively. Statutorily, a provision of section 81 of the 1999 constitution of the Federal Republic of Nigeria requires the president of the nation to prepare and present an annual estimate of revenue and expenditure of each fiscal year in a specific format to the National Assembly for approval.

Budget consolidation is normally achieved through the Budgets and Planning Ministry after receiving budget policy from the Budget Department of the Presidency. Budget guidelines are sent by the Ministry of Budgets and Planning in form of Call Circulars to the various Ministries and other government establishments, requesting them to prepare and forward their estimates of revenue and expenditure for the coming year.

On receipt of the Call Circulars by the various ministries and government establishments, departmental budget committees are set up for the preparation of the estimates and then consolidated at the ministry's budget committee level which do the necessary modification and consolidation of the budget before forwarding to the ministry of Budget and Planning by the Chief Accounting Officer of the Accounting unit.

On receipt of the Estimates from each Ministry, the Ministry of Budget and Planning sets up a draft Estimate Committee to review, modify and consolidate the various Estimates submitted by the various Accounting Units.

This will then be forwarded to the president, the chief executive who will now present the budget to the legislature for approval.

3.2 Budget Approval Phases

Approval of budget normally takes three phases, these are:

1. Ministerial phase
2. Executive phase
3. National Assembly or Legislative phase

3.2.1 Ministerial Phase

This is the Phase where the Ministry of Budget and Planning on receipt of the various Estimates sets up a draft Estimate Committee and also invites each Ministry representatives as Accounting Officers to come forward and defend their Estimates. The Ministry does the necessary revision, modification and consolidation of the various budgets. On successful defence of the various Estimates, the consolidated budget will be sent to the President.

3.2.2 Executive Phase

This is the phase of budget approval whereby the President receives the estimate and then presents such to the Council of Ministers for proper deliberation and approval. The President transmits such budget to the National Assembly for final approval.

3.2.3 Legislative or National Assembly Phase

This is the third and final Phase of Budget approval in Nigeria. Here the President presents the Budget to the lower and upper houses of Assembly (Federal House of Representatives and the Senate in a joint session. This is called Budget Session at which there are standing committees of the two houses. Whenever there are discrepancies or conflicts, a Finance Committee will be set up for necessary adjustments, modifications; reduction etc and their final decisions will be valid.

The two houses will then later meet to approve the budget after which the President will give his assent and the Budget, from a draft Estimate will be converted into appropriate bills which later become an

Appropriation Act. Hence, an Appropriation Act refers to the approved Budget.

3.3 Deductions from the Main Content

The President is empowered by the Constitution of the Federal Republic of Nigeria 1999, Section 81 to prepare and present an Annual Budget in a specific format to the National Assembly for approval.

Budget Department of the Presidency initiates budget policy which is sent to the ministry of budget and planning for consolidation.

The guidelines are given to the various ministries in form of Call Circulars for action in the various ministries.

What is sent to the Ministry of Budget and Planning is further reviewed, revised and modified by the Draft Estimate Committee before transmission to the President who would present same to the National Assembly for approval.

There are three Phases of approval which include the Ministerial, the Executive and the National Assembly or Legislative Phases.

4.0 CONCLUSION

It should be noted that government activities are normally financed by Budgets which are therefore required to be approved by the Legislative arm of the government. Consequently, budgets as being used in the private sector are also used in the public sector for the following reasons:

i. Planning
ii. Control
iii. Coordination and Allocation of Resources
iv. Motivation
v. Authorization of Action
vi. Communication and organization of government policies
vii. Evaluation of performances
viii. Decision making etc.

5.0 SUMMARY

Section 81 of the 1999 Constitution of Nigeria empowers the President to present an Annual Budget. This is prepared through the Budgets Department in the Presidency to the Ministry of Budget and Planning, via the different ministries, parastatals, extra-ministerial arms and back to the President for presentation to the National Assembly in a joint Budget Session.

The phases of approval of budget include the ministerial, the Executive and the National Assembly Phases.

6.0 TUTOR - MARKED ASSIGNMENTS

1. What does budget in the public sector entail?
2. Explain the process of preparation of budgets in a democratic state?
3. What are the phases of budget approval? Discuss them.

7.0 REFERENCES/FURTHER READINGS

Rotimi, Ajibola: (2005). Public Finances – *Principles and Practice*.

Uremadu S. O: (2000). Modern Public Finance – *Theory and Practice*.

Allen, Schick: (1980). *Perspectives on Budgeting*

UNIT 2 METHODS OF BUDGETING: TRADITIONAL OR INCREMENTAL AND ZERO- BASE BUDGETING

CONTENTS

1.0 INTRODUCTION

In this unit, we shall explain the methods of Budgeting in the Public Sector, considering the fact that Budgeting is such a universal and essential activity of governments. Though, a budget wears many faces.

For an Accountant, Budget is a means of tracking government finances;

For an Economist, it is a means of manipulating revenue and expenditure to influence the production of goods and services.

A Political Scientist's budget is one in which some people pay so that others may benefits;

A Public Administrator's budget is a source of funding for government agencies and programme.

This unit considers traditional or incremental budgeting system (IBS) and Zero Base Budgeting (ZBB). We shall explain them fully and cite the advantages and disadvantages of each of them.

2.0 OBJECTIVES

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

- Recall the roles of the Executive, the Ministers and Legislature in budgeting and budget approval.
- Explain the meaning of traditional method of budgeting.

- Discuss the Zero Based Budgeting
- Give the advantages and disadvantages of each type.

3.0 MAIN CONTENT

3.1 The Traditional or Incremental Budgeting System

This is also called line items budgeting system. It is also an input approach to budgeting. It is a budgeting system which involves the utilization of the previous period budgets thereby increasing it by a specific percentage (%) to arrive at a new Estimate with full consideration of economic trends, inflation and fund availability. In this type of budget, attention is directed towards changes that occur between existing appropriations and proposed expenditures. Such a progress accepts existing base and examine only the increments, which extends the only budgeting programme in the future. Only the desired increments are subsequently analyzed. This method of budgeting is good for recurrent expenditure, thus the proposed year's budget can be calculated as follows:

Next year's budget = this is year budget X inflation factor + cost of new activity.

The Advantages in This Method Include The Following.

- It is adequate and good for recurrent expenditure,
- It ensured compliance with appropriation standards,
- It has simplicity of operation,
- It is suitable for Nigerian development.

The Disadvantages of This Budgeting Include The Following

i. Past inconsistencies and errors are carried forward.
ii. It concentrates on costs and expenditures, which are inputs rather than outputs.
iii. It funds programmes of low or expired usefulness on overgenerous scales.
iv. It fails to fund new programmes of high priority on sufficiently generous scales.
v. It results on a continual growth in budget totals related to cost inflation.
vi. It limits public understanding of government activities.
vii. It fails to clarify cost of alternative methods of achieving programmes objectives.

viii. It examines the momental changes in greater details than the budget as a whole.
ix. It leads to inefficiency
x. Lack of accountability may result.

3.2 The Zero Bases Budgeting (ZBB) Method

This is used in conjunction with any other type of Budgeting. Its development arises from the criticism of the Traditional Budgetary System. It is an approach to Budgetary Planning which rejects the customary views of the Incrementalist. It is a systematic approach / process by which management takes the careful examination of the basis for allocating resources in accordance with the formation of budget requirements and programme planning. It is a budgeting system which requires every provisional head, manager, etc to justify his entire budget from the scratch (Zero Base). Any item that cannot be justified will automatically be eliminated. The Manager shall ignore what had been done in the past and shall attempt to justify the futurist items. ZBB is a cost benefit approach to budgeting, which ensures value for money activities. It however involves the use of decision packages.

According to Cornelius E. Tienny in *Handbook of Federal Accounting Practices*, the goals of ZBB as summarized by the office of Management and Budget (OMB) in USA are as follows:

a. To examine the need for an accomplishment and effectiveness of existing government programmes as if they were proposed for the first time.
b. To allow proposed new programme to compete for resources on a more equal footing with existing programmes
c. To focus budget justifications on the evaluation of discrete elements and programmes or activities of each decision unit aid.
d. To secure extensive management involvement at all levels in the budget process.

Generally speaking, ZBB consists of the following important stages/ procedures:

i. Identification of Decision Unit
   This is the smallest unit where decisions are made.
ii. Development of Decision Packages
   These consist of accumulation of decision units. It is a proforma documentation used in describing decision units and their cost of operation.
iii. Evaluation and Banking of Decision Packages.

iv. Determination of cut-off points using a realistic cut-off procedure.
v. Allocation of resources or consolidation of budgeting justification of resources.
vi. Implementation, monitoring and re-evaluation.

The Advantages of This Budgeting Include:

- It avoids the problem of incrementation
- It allows for value-for-money approach
- There is efficient resources allocation.
- It is futuristic - It focuses on future rather than on past activities.
- It allows for the participation of individual organs of decision making unit.
- It provides a yardstick for measurement of performance.
- It acts as a tool of change, which is beneficial to the nation.
- Wasteful spending is reduced
- Important project can continue to obtain improved funding.
- It is good for Capital Expenditures.

The Disadvantages of ZBB Includes:

1. Cost is very high
2. There is problem of identifying a suitable decision unit.
3. There is high volume of paper work in the system.
4. There is problem of producing suitable decision packages
5. It may cause a shift in resources allocation
6. Lack of accurate, sufficient and reliable data.
7. There is lack of qualified and competent personnel.
8. Switching to ZBB may require a modification of the system, which may necessitate a general review, overhauling, adding to or scrapping of activities, functions etc.
9. Bureaucracy may undermine its effectiveness

3.3 Deductions From the Main Contents

Traditional or Incremental Budgeting System is the type of Budgeting which involves the utilization of the previous periods budgets thereby increasing it by a specific percentage; considering the economic trends, inflations and fund availability, a new estimate is arrived at.

The proposed year's budget = this year's budget X inflation factor + cost of new activity.

This is simple to operate and suitable for Nigeria's development as appropriation standards are complied with.

On the other hand, the Zero Based Budgeting System which is a systematic process as management takes careful examination of the basis for allocating resources in accordance with the formation of budget requirements and Programme Planning. Every provisional head or manager must justify his entire budget from the scratch (Zero Base).

This method avoids the problem of incrementation and makes room for value-for-money approach wasteful. Spending is reduced and there is room for the participation of individual organs of the decision unit.

4.0 CONCLUSION

This unit has described the concepts of traditional or incremental budgeting system alongside with the Zero-Based Method. Their advantages and disadvantages are highlighted. The procedure for the Zero-Based Budgeting is also systematically explained.

5.0 SUMMARY

Incremental Budgeting System accepts the existing base and estimates only for the targeted year, taking the economic factors (inflation, availability of funds etc) into view. The shortcomings of this method are many. Past inconsistencies and errors are carried forward as it limits public understanding of government activities. It also leads to inefficiency and shield lack of accountability.

Zero Based Budgeting Method leads to the justification of every item in the estimate otherwise; such an item is automatically eliminated.

This is a cost benefit approach to budgeting, which ensures value for money activities. There are also some low points which include the high cost of preparation, lack of accurate, sufficient and reliable data along side with negative influence of bureaucracy on its effectiveness.

6.0 TUTOR-MARKED ASSIGNMENTS

1. What are the shortcomings of the Traditional Budgeting System?
2. Explain the Incremental Budgeting System in the public sector.
3. What does Zero-Based Budgeting mean?
4. Highlight the advantages of this (ZBB) method of budgeting to the Nigerian public sector

5. Itemize the procedures for preparing the Zero Based System of Budgeting

7.0 REFERENCES/FURTHER READINGS

Rotimi, Ajibola : *Public Finance Principle And Practice*

Oremadu S.O: Modern Public Finance, *Theory and Practice*

Golemblem, Sidi Rabin: *Public Budgeting and Finance*.

UNIT 3 PLANNING, PROGRAMMING BUDGETING SYSTEM (PPBS) AND PROGRAMME AND PERFORMANCE BUDGETING SYSTEM

CONTENTS

1.0 INTRODUCTION

In this unit, we shall discuss additional methods of budgeting - Planning, Programming Budgeting and Programme and Performance Budgeting Systems. We shall give detailed explanation and cite their high points and low points in the public sector finances.

2.0 OBJECTIVES

At the end of this unit, the students are expected to:

- Recall the first two methods of budgeting discussed in the previous unit.
- Explain in simple terms the meaning of Planning, Programming Budgeting and Programme and Performance Budgeting Systems.
- Itemize the pros and cons of the two budgeting methods
- Analyze the features of these methods of budgeting in the public sector.

3.0 MAIN CONTENT

3.1 Planning, Programming Budgeting System:

This provides regular procedures for reviewing goals and objective, for selecting and planning programmes over a period of years in terms of output and resources. It also facilitates the allocations of resources between programme and their implementation, processes and control.

Therefore, the key characteristics of PPBS is that objectives and programmes costs are formulated over a period of years within the context of a medium term plan, thus permitting a longer financial perspective than Traditional Budgeting would allow.

In such a plan, the continuity of projects, the extent of commitment, and the future financial consequences of current expenditures, can be recognized.

It must be noted that those who formulate plans are forces to consider the full financial implications of their policies.

The Features/Elements of PPBS Include The Following

a. Identification of goals and objectives in each major area of governmental activity.
b. Analysis of the output of a given programme in terms of its objectives.
c. Measurement of total programme cost not just for one but for at least several years ahead.
d. Formulation of objectives and programmes extending beyond the single year of the annual budgets
e. Analysis of alternatives to find the most effective means reading basic programme objectives.

The High Points of PPBS are:

i. It provides information on the objectives of the organization
ii. It cuts across conventional lines of responsibility and departmental structures by drawing together the activities that are directed towards a particular objective
iii. It exposes programme that are over lapping or contradictory in terms of achieving objectives.
iv. It concentrates on long term effects.
v. It provides information on the impacts that the existing and alternative programmes will have an objective, and the associated programme costs.
iv. It enables resources allocation choices to be made on the basis of benefits/cost relationship.
vi. It promotes rational decisions.

The Low Points of PPBS Are:

i. It requires skilled manpower which is not available in most of the developing countries.
ii. It is capital intensive in nature and requires the use of computers which may not be available.
iii. It requires excellent statistical sources and data storage which are not available in most of the developing countries.
iv. It is costly and time consuming
v. Many activities are of multi-purpose nature and it is always difficult to determine how the costs of such activities should be allocated to a particular output categories.

3.2 Programme and Performance Budgeting System

Is the budgeting type in which the input of resources is related to the output of service/product? It can also be described as one, which represents the purposes and objectives for which funds are requested. It can also be described as a method that emphasizes the thing which government buys.

This budgeting system was first adopted by the Federal Government of Nigeria in 1981 and was later abandoned.

The features of Programme and Performance Budget include the following:

a. Classification of budgets in terms of functions, programme and activities;
b. Measurement of work or output provided by each activity;
c. Expression of the budget in a way which allows a direct comparison between cost of funds and the work to be performed for each programme or activity;
d. Monitoring of actual against budgeted cost and performance.

There Are Advantages in This Budgeting Style and They Are:

a. The goals, sub-goals, objectives and activities are identified.
b. Monitoring of projects is possible by the National Assembly members
c. Fund allocated will always be spent on what it was meant for since measurement of work done is possible.
d. It eliminates double allocation.
e. It increases efficiency of work performed.

The Other Side of the Budgeting System Includes:

a. It requires much paper work and it is time consuming
b. It requires skilled manpower which at present is not adequately available in the developing countries.

3.3 Deductions From the Main Content

Planning, Programming Budgeting System is that style that provides regular procedures for reviewing goals and objectives, for selecting and planning programming over a period of years in terms of output and resources. It enables resources allocation choices to be made on the basis of benefit/cost relationship.

The programme and performance budgeting insists that allocation of funds should be related to what is intended to be achieved. The essence of this method of budgeting is that results to be achieved should override considerations of expenditure to be incurred. The goals, sub goals, objectives and activities are identified as there is possibility of monitoring of projects by the National Assembly members. Efficiency of work performed is increased.

4.0 CONCLUSION

This unit has discussed the features, advantages and disadvantages of planning, programming budgeting system and that of programme and performance budgeting system.

5.0 SUMMARY

Planning and programming budgeting system puts into consideration costs and benefits before deciding on which project to focus attention. Hence, the decision maker should have available the fullest possible knowledge of the results of alternative courses of action open to him.

The programme budgeting assigns costs to programme in order for government to make more rational and efficient budgeting. Here, budgeting is made for a specific programme – Tarring of Onitsha-Owerri Expressway.

6.0 TUTOR MARKED ASSIGNMENTS

1. What are the high points of planning, programming budgeting system in any economy?
2. What disadvantages are in programming and performance budgeting?

7.0 REFERENCES/FURTHER READINGS

Daniel, A.I – (1996). *Pubic Sector Accounting*

Uremadu, S.O Modern Public Finance (*Theory and Practice*)

Rotimi, Ajibola – (2003). *Public Finance Principles and Practice*

UNIT 4 METHODS OF BUDGETING: CONTINUOUS OR ROLLING BUDGET

CONTENTS

1.0 INTRODUCTION

In this unit, students will be exposed to another type or method of budgeting which is not as popular as those earlier discussed in other units. This is the Rolling or Continuous budgeting method or system.

2.0 OBJECTIVES

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

- Recall the four types of budgeting discussed in the other units
- Explain the meaning of Rolling or Continuous budgeting system.
- Highlight the advantages and disadvantages of the Continuous or Rolling budgeting system.

3.0 MAIN CONTENT

3.1 Rolling or Continuous Budgeting

(Chartered Institute of Management Accountants) CIMA The defines a Rolling Budget as the continuous updating of a short term budget by adding say, a further month or quarter months, and deducting the earliest month or quarter months so that the budget will reflect current conditions.

It is a system that involves the continuous updating of budget through review of actual results of a specific period in the budget, and determining a budget for the corresponding time or period.

There are advantages in this method of budgeting. They are:

i. It reduces the elements of uncertainty in the plan that might be caused by inflation.
ii. It produces the most realistic budget figure.

There is a disadvantage that cannot be ignored. It consumes much time and even manpower as the budget needs to be reviewed regularly.

3.2 Deductions from the Main Content

The rolling budget involves updating of budgets through reviewing of actual results of a specific period in the budget. A budget is then determined for the corresponding time. The most realistic budget figure is produced through this method.

4.0 CONCLUSION

The meaning, advantages and the disadvantages of rolling budget have been discussed meaningfully in the unit.

5.0 SUMMARY

The Rolling budget produces a realistic budget figure due to the periodic and continuous review. Issues of uncertainty resulting from inflation are quickly dictated and checked.

6.0 TUTOR - MARKED ASSIGNMENTS

1. Recall the four other methods of budgeting earlier discussed.
2. What is Rolling Budget?

7.0 REFERENCES/FURTHER READINGS

Daniel, A.I – (1996). *Pubic Sector Accounting*

Uremadu, S.O - Modern Public Finance (*Theory and Practice*)

Rotimi, Ajibola – (2003). *Public Finance Principles and Practice*

MODULE 4

UNIT 1 BUDGETARY ISSUES IN PUBLIC FINANCE: BUDGETARY CONTROL

CONTENTS

1.0 INTRODUCTION

In this unit, we shall explain the essence of budgetary control in public finance. It should be noted that budgeting is one of the primary devices for accomplishing control in organization. This is because budgets are used to plan and monitor all aspects of business activities in any enterprise. Costs are controlled, responsibilities are assigned, decisions and even departments are coordinated through budgets.

2.0 OBJECTIVES

At the end of the unit, students should be able to:

- Recall budgeting methods in the previous modules / units.
- Define budgetary control.
- Itemize the steps in budgetary control
- Discuss the functions of budgetary control in the public finance
- Analyze the features of budgetary control.

3.0 MAIN CONTENT

3.1 Budgetary Control

Budgetary Control is defined by CIMA (Chartered Institute of Management Accountants) as "the establishment of the budgets relating to the responsibilities of the executive to meet the objective of an organization and the continuous comparison of actual with budgeted estimates so that, if remedial action 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".

Hence, the following facts arising from the above definitions should be of note:

a. It is a management technique used to plan, execute and control operations and activities aimed at achieving set targets within a stipulated time frame.
b. It is a review of planned estimates against actual results to achieve performance evaluation
c. It ensures that actual results are positively in accordance with the overall financial and policy objectives of an establishment.
d. It is a continuous process which reviews and adjusts budgetary target during a particular period.

There are steps involved in budgetary control. They include:

i. Preparation of a budget or a detailed action plan;
ii. Identification of responsibility centers in the organization to execute or carry out specific activities or operations forming part of the action;
iii. Adaptation of mutually agreed targets of achievements or outputs to serve as milestones or other indicators of progress in the actions plan in financial and physical terms;
iv. A system for periodical monitoring of performance or activities of every segment or responsibility center involved;
v. Careful comparison of the actual performance and outcome with the corresponding parts of the plan;
vi. Assessment of deviations and variances in actual performance and activities in relation to the plan and identification of causes of such a deviation;

vii. Initiation of corrective action aimed at ensuring that the planned activities and actions are adhered to as far as possible.

It then 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 and culminating in corrective action.

Its main purpose is to enable management to plan and carry out projects, operation or activities with effectiveness and efficiency in the use of resources.

The concept of control in budgeting cannot be overemphasized particularly in terms of cost efficiency and cost effectiveness. The concept encompasses the functions of:

- Fund control
- Expenditure control
- Revenue control
- Payment or Disbursement control
- Cash control
- Cost control
- Cash or payroll control.

Budgetary control is important in the following ways:

a. It increases efficiency as individual accounting officer knows that he will be accountable for the fund allocated to his unit and his performance will be evaluated visa-a-vis his output.
b. It reveals inefficiency of some managers/accounting officers' as such corrective measures will be taken.
c. It reduces greater losses since it is a continuous measuring of actual and budgeted positions and as such the loopholes will be blocked
d. The causes of variances between the budgeted and actual are known and necessarily steps taken to forestall the occurrences.
e. It reduces over-expenditure on the part of the spending officers.

There are features that cannot be ignored as they are essential in budgetary control. They include the following:

a. Relevance and Timeliness: If budgetary control system is to work properly, the information sent to the officer concerned must be relevant and timely.

b. **Controllable and Non-Controllable Items**: In order to carry out the budgetary control of an organization or an aspect in the organization, the controllable and non-controllable items should be clearly distinguished between the variables that are directly controllable and non-controllable.

c. **Budget Figure**: For any meaningful budgetary control, it must include the budget figure not only for the whole year but also for the appropriate proportion of the year.

d. **Adequate Information**: Before a good budgetary control can be carried out there must be adequate information which must be understandable and contain the right amount of details.

e. **Proper Books**: The Statement and Accounts prepared at the end of a period give an idea of the activities / flow of funds. Therefore, for the purposes of budgetary control proper books of Account must be maintained.

f. **Regular Checks**: Monitoring is a continuous surveillance at the implementation of a project or a programme. It seeks to ensure that various activities are carried out according to the budget and programme progresses according to the plan. Therefore surprise checks should always be carried out at any time of the year.

g. **Internal Control**: This is defined as "the whole system of controls, financial and otherwise established by the management in order to carry on the business of the enterprise in an orderly and efficient manner, ensure adherence to management policies, safeguard the assets and secure as far as possible the completeness and accuracy of the records (ICMA). Therefore, internal control can be broadly sub-divided into three groups of control–Administrative, Accounting and Internal Audit controls.

h. **Disclosure of Committed Balances**: In the Ministries and Extra Ministerial Departments, cash / commitment basis has been the accounting basis in use. Here, only the cash received and cash payments are recorded. It is therefore important for an effective budgetary control; the committed balance in the vote book should be disclosed.

3.2 Deductions from the Main Content – Budgetary control

Budgetary Control is a technique encompassing the entire process, starting from the preparation of the budget or the action plan, covering monitoring and review and culminating in corrective action.

It encourages cost efficiency and cost effectiveness.
It reveals inefficiency of some Managers / Accounting Officers as corrective measures are continuously taken.

Over- expenditure is reduced to the barest minimum on the part of the spending officers.

The essential features in budgetary control are:

Relevance and timeliness, controllable and non controllable items, budget figures, adequate information, proper books, internal control, regular checks etc.

4.0 CONCLUSION

In this unit, budgetary control has been explained; the advantages, features and steps are highlighted

5.0 SUMMARY

Budgetary control is a management technique used to plan, execute and control operations and activities aimed at achieving set targets in a stipulated time frame.

There are seven steps involved in budgetary control. The system controls funds, expenditure, payment or disbursement cash, cost and payroll.

6.0 TUTOR – MARKED ASSIGNMENTS

1. What are the features of budgetary control
2. In what ways are budgetary control important

7.0 REFERENCES/FURTHER READINGS

Daniel, G.I: (1996). *Public Sector Accounting*

Koontz et al: *Management*.

UNIT 2 WEAKNESSES OF BUDGETS

CONTENTS

1.0 INTRODUCTION

Budgeting is a systemic approach to the solution of problems. But it is not fool–proof as it suffers from certain problems and limitations. The major problems in developing a budgeting system include the following:

- Seeking the support and involvement of all levels of management.
- Developing meaningful forecasts and plans, especially the sales plan.
- Educating all individuals to be involved in the budgeting process and gaining their full participation.
- Establishing realistic objectives policies, procedures and standard of desired performance.
- Maintaining effective follow-up procedures and adapting the budgeting system whenever the circumstances change.

2.0 OBJECTIVES

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

- Recall the essence of budgetary control in any system
- Itemise areas of danger in any given budget..
- Explain those limitations inherent in well planned budgets.
- Discuss how management judgment, goal conflict, unrealistic targets etc have constituted a nuisance to budgeting.

3.0 MAIN CONTENT

3.1 Weaknesses, Dangers in Budgeting

As a device to solving managerial problems in using budgeting system, the following limitations must be considered by management:

Management Judgment

Budgeting is not an exact science as its success is dependent on the precision of estimates. These are based on facts and managerial judgment which can sometimes suffer from subjectivism and personal biases. The adequacy of budgeting therefore depends on the adequacy of managerial judgment.

Continuous Adaptation

The installation of a perfect system of budgeting is not possible in a short period. As business conditions change rapidly, budgeting programme should be continuously adapted. Budgeting has to be a continuous exercise since it is a dynamic exercise / process.

Management should not be impatient but keep trying various techniques and procedures in developing and using the budgeting system. Ultimately, they will achieve the success and reap the benefits of budgeting.

Implementation

A skillfully prepared budgetary programme will not itself improve the management of an enterprise unless it is properly implemented. For the success of the budgetary programme it is necessary that it is understood by all and that the managers and subordinates put concerted effort for accomplishing the budget goals. All persons in the enterprise must have full involvement in the preparation and execution of budgets; otherwise, budgeting will not be effective.

Management Complacency

Budgeting is a management tool that details a way of managing and not the act of management itself. The presence of budgetary system should not make management complacent. To get the best results of managing, management should use budgeting with intelligence and foresight along with other managerial techniques. Budgeting assists management but cannot replace management.

Unnecessary Details

Budgeting will be ineffective and expensive if it is unnecessarily detailed and complicated. A budget should be precise in format and simple to understand. It should be flexible and not rigid in application.

Goal Conflict

The purpose of budgeting will be defeated if carelessly set budget goals conflict with enterprise objectives. This confuses means with the end result. Budget goals are the definite targets to achieve the overall enterprise objective. They must be in harmony with the enterprise aims.

Evaluation Deficiencies

Budgeting will hide inefficiencies instead of revealing them, if a proper evaluation system is lacking. There should be a continuous evaluation of the actual performance on regular basis too, standards should be re-examined.

Unrealistic Targets

Budgeting will lower morale and productivity if unrealistic targets are set and if it is used as pressure tactic. It could be used as a pressure device but its extent must be carefully determined.

3.2 Deductions from the Main Content: Weaknesses of Budgets

The following are the limitations in budgeting that must be quickly tackled by management in solving managerial problems.

Management judgment should be devoid of subjectivism and biases for an adequate managerial judgment.

There should be continuous adaptation to the rapidly changing programme.

All hands must be on deck in terms of implementation of budget.

There should not be complacency in budgeting management, instead, intelligence, foresight and management styles are applied.

There should be no unnecessary details and unrealistic targets.

4.0 CONCLUSION

In the unit, the limitations and weaknesses of budgets have been highlighted. The areas of worry have been itemized and explained.

5.0 SUMMARY

The unit has given detailed insight into the limitations or weaknesses of budgeting. The points trashed include: management judgment, continuous adaptation implementation, management complacency, unnecessary details, goal conflicts, evaluation deficiency and unrealistic targets.

6.0 TUTOR - MARKED ASSIGNMENT

What are the areas of danger in any given budget?

7.0 REFERENCES/FURTHER READINGS

Pandey, I.M *Financial Management*

Otokiti et al. *Managing Business Finance & Investment*

UNIT 3 DEVELOPMENT PLAN: MEANING, RATIONALE AND FEATURES

CONTENTS

1.0 INTRODUCTION

According to Jawaharial Nehru "Planning is the exercise of the intelligent to deal with facts and situations as they are, and find a way to solve problems".

Planning can be defined as a process and procedures of determining the goals and objectives of a company and designing strategies to achieve them. Forecasting usually preceeds planning and it involves environmental scanning and evaluation in planning, Concrete objective have to be drawn up and planning efforts have to be geared towards the achievement of set objectives. A good planning usually leads to efficient control. Planning can either be tactical, operational or strategic and can also be short term or long term, depending on the time horizon.

2.0 OBJECTIVES

At the end of the unit, students should be able to:

- Discuss the weaknesses and limitations of budgets.
- Explain the meaning of Economic and Development Plans.
- Define the term planning
- Itemize the features of a development plan
- Mention the rationale for development plan

3.0 MAIN CONTENT

3.1 Meaning, Features and Rationale of Development Planning

Economic Planning is a conscious governmental effort to influence, direct and in some cases, control changes in the principal economic variables (consumption, investment, savings, export, import etc) of a certain country or region over the course of time in order to achieve a predetermined set of objectives.

The essence of economic planning is summed up in the notion of governmental influence, direction and control.

Perspective planning is a planning process that examines the long term development options opening to an economy. It involves the selection of best options with a view to achieving desired objectives in the near future.

Therefore, development plan is a deliberate governmental strategy for achieving well defined national goals over a given period of time.

It is a proposal for mobilizing and utilizing resources (domestic and foreign) to achieve economic growth and development. A development plan has been considered a more fruitful strategy of modern development in that it is used in setting and prescribing targets for productions infrastructure, employment, foreign trade etc; especially in the public sector.

A development plan takes a comprehensive view of the national economy in order to work out coordinated and consistent public policies and programme.

A well defined development plan has the following features:

i. It is comprehensive in that it takes a holistic view of the global economy, incorporating both the private and public sectors.
ii. It involves elements of macro economic forecasting, making projection of expected movements of the economy.
iii. Development plan entails a more systematic project evaluation in terms of social cost and benefits. It ensures that a project is executed if the benefits outweigh the cost.
iv. Development plan aims at deliberately influencing the private sector towards national goals and objective
v. It attempts to define policy objectives based on the political views and goals of the government for future development of the economy.

It usually necessitates the establishment of additional institutional machinery for efficient planning.

It covers a long period of time e.g. five years, but supplemented by annual plans.

The rationale for development plan includes the following:

a. Inefficiency of Market Mechanism

The failure of market system to efficiently allocate resources in an economy necessitates the existence of government intervention in the area of development plan.

b. Economic Growth

This refers to the increase in the volume of goods and service produced over time. Government's conscious effort and planning is needed to achieve a particular developmental target at a future time.

c. Indigenization of the Economy

Development plan promotes indigenization of the economy and so reduces foreign domination as much as possible. This is because a foreign dependent economy is open to shocks and imbalances from foreign countries.

d. Foreign Aid

The formulation of detailed development plan with specific sectoral output as well as carefully designed project is a necessary condition for mobilization of international financial support.

e. Favourable Balance of Payment

Development plan is prepared to achieve favourable balance of payment by setting a target import that will guarantee surplus in the balance of payment account.

f. Resource Mobilization:

An efficient resource allocation and equitable distribution of income can be achieved through a well articulated and formulated development plan. For instance, rural banking is aimed at enhancing the living conditions of the rural dwellers.

g. National Unity

A detailed and comprehensive development plan can bring people together and mobilize popular support for nation building. For instance, poverty alleviation programme

h. Socio-economic Development

Government embarks on development planning in order to promote changes and adaptation to socio-economic situations by effecting some institutions and structural changes in the economy

3.2 Deductions from the Main Content

A development plan takes comprehensive view of the national economy in order to work out a coordinated and consistent public policies and programmes.

It entails a more systematic project evaluation, in terms of social cost and benefit. Additional institutional machinery for efficient planning is necessitated by development plan. The private sector is influenced toward national goals and objectives by the important development plan. The importance of development plan include, among others: It attracts foreign assistance, Aids and necessitates economic growth.

Resources are mobilized through such projects as rural banking in order to enhance rural dwellers' living standard.

Socio – Economic development is effected by affecting some institutional and structural changes in the economy.

4.0 CONCLUSION

In this unit, the meaning of not only Development plan, Economic plan but even Planning has been clearly explained. The feature and rationale behind development plan has also been highlighted.

5.0 SUMMARY

Economic plan is a specification of quantitative economic targets to be reached in a given period in time. Economic plan is comprehensive when targets are set to cover all aspects of the national economy while partial economic plan covers only a part of the national economy such as industry, agriculture, public sector, private sector etc.

While Development Plan is a deliberate governmental strategy for achieving defined national goals. The basic attributes of a well defined Development Plan are articulated in seven points.

The eight point rationale for Development Plan are clearly stated and explained.

6.0 TUTOR-MARKED ASSIGNMENTS

1. Differentiate between Economic and Development plan in the economy
2. What is Development Plan?

7.0 REFERENCES/FURTHER READINGS

Rotimi, Ajibola: (2005). *Public Finance Principles and Practice*

Uremadu, S. O: *Public Finance Principles and Practice*

UNIT 4 DEVELOPMENT PLANNING IN NIGERIA

CONTENTS

1.0 INTRODUCTION

It was after the Second World War that modern economic planning took place in Nigeria. For many countries comprehensive national development plans were drawn up only after political independence.

It was in 1946 that Development planning started in Nigeria following the initiative of the secretary of state for the colonies. It was then the ten years plan of development and welfare (1946- 1956) came into being. Under this plan nearly ₦112 million was spent on development about half of which was provided in the form of grants from the United Kingdom.

Following the creation of region in 1954, separate development programmes were prepared for the federal, western, eastern and northern regions for the years 1955 – 60. Economic Development Plans were later revised and extended to cover 1960 – 62, at an estimated total cost of ₦328 million, although, actual expenditure amounted to only ₦170 million during the first five years.

2.0 OBJECTIVES

At the end of the unit, students should be able to:

- Recall the meaning of Economic and Development plans.
- Discuss the development plans before independence of Nigeria
- Explain the first two development plans after independence.
- Describe the circumstance that led to the 3rd and 4th National Development plans.

3.0 MAIN CONTENT

3.1 Development Planning In Nigeria

Since Independence in 1960 Nigeria has formulated and implemented three comprehensive National Development plans and a 4th was adopted in 1981.

3.2 First National Development Plan 1962 – 1968

Under the plan which was launched in June 1962, the GDP was expected to grow at approximately 4% a year. The total planned investment expenditure was ₦2366 million, of which ₦1386 million was to be carried out in the public sector. The highest priorities were given to Agriculture, Industry and the training of high level and intermediate Man power.

Most of the planned goals were actually exceeded due to the performance of the private sector. For example, a growth rate of 4% approximately was planned but 6% rate of growth per annum was achieved. Total public investment expenditure amounted only to ₦798 million or 50.3% of the planned figure. Many of the goals of the public sector were not achieved owing to the outbreak of the political crisis in 1965, and the civil war in 1967. The following are some of the major projects successfully completed by the government. An oil refinery, a paper mill and a sugar mill; the Nigeria Dam, the Niger Bridge, Ports Extension and the construction of trunk roads, a security and minting plant.

3.2.1 Second National Development Plan 1970-1974

The plan was aimed in part at the reconstruction of facilities destroyed or damaged during the civil war, 1967-1970. Its five principal objectives were to establish:

i. A united, strong and self-reliant nation
ii. A great and dynamic economy
iii. A just and egalitarian society.
iv. A land of bright and full opportunities for all citizens.
v. A free and democratize society.

GDP was expected to grow at the average rate of 6.6% p.a during the period of the plan. Total investment was originally estimated at 3192 million but later revised to ₦3203 million as a result of increase in foreign exchange available. The amount of ₦671 million of gross fixed investment was to be carried out by the public sector and the main priorities were Agriculture, Industry Transportation and Manpower development.

Actual development expenditure fell considerably below their planned levels because of:

a. Poor project preparation
b. Difficulties with the ability of the economies absorb high levels of investment (weak absorptive capacity).
c. Weaknesses in manpower planning and development.
d. Shortage of construction materials and difficulties due to other domestic bottlenecks.

Because of the difficulties and shortfalls experienced in the plan implementation, the plan was extended by one year to 1974/75. This was to allow for completion of projects and better preparation of the third National Development plan, especially in view of increased government financial resources expected from the petroleum sector.

3.2.2 Third National Development Plan 1975-80

This plan, covering five years was launched in April 1, 1975 (1975/76 – 1979/80). The basic objectives of the plan were:

a. To expand and diversify the productive capacity of the economy
b. To restore stability. To promote a more equitable distribution of the national income.

Within these general objectives, emphasis was on transport and communications, manufacturing and crafts and general administration.

The revised public sector investment programme was to be financed from recurrent budget surplus (government savings), domestic borrowing mostly from the banking system and loans from the international financial markets.

Government investment expenditure totalled N1760 million during the first three years (**1975/76, 1976/77 and 1977/78)** of the plan; thus actual investment spending exceeded the level anticipated under the revised public investment programme. There are strong indications however that government investment outlays may have declined in the last two years of the plan. This coupled with the rising rate of inflation, may have resulted in substantial shortfalls in the implementation of the plan, especially in physical terms.

Though, the plan was originally expected to terminate on 31st March 1980, its life span was extended by nine months to 31st December, 1980.

3.2.3 The Fourth National Development Plan 1981 – 85

This plan ran from January 1981 to December 1985. The participation of the local government authorities featured for the first time. The overriding aim was to bring about improvements in the living conditions of the people. The following specific objectives were set out in the plan.

- Increase in the real income of the average citizen;
- Increase even distribution of income among individuals and socio-economic groups;
- Reduction in the level of unemployment and under-employment;
- Increase in the supply of skilled manpower;
- Reduction of dependence of the economy on narrow range of activities;
- Increase participation by citizens in the ownership and management of productive enterprises;
- Greater self-reliance; that is increased dependence in the country's own resources in seeking to achieve the various objectives of the society. This also implies increased effort to achieve the most use of human and material resources;
- Development of technology;
- Increased productivity;
- The promotion of a new national orientation towards greater discipline, better attitude to work and cleaner environment.

Of the total of ₦82 billion investments envisaged under the plan, the share of the public sector was expected to be ₦70.5 Billion or 85.9%. The balance of ₦11.5 Billion or 14.1% was reserved for the private sector.

The priority list included agricultural production and processing, education, manpower development, strengthening of economic infrastructure – power and water supply, telecommunication, housing and health development.

3.3 Deductions from the Main Content

Nigeria has formulated and implemented 4(four) types of Development Plans between 1962 and 1985.

Amongst the items and programmes to be improved upon, Agriculture was on the top, all through. Other items of importance include: Education, Manpower, Industry, Transport and Communications etc.

In the first Development Phase, the projects that were successfully completed are – an oil refinery, a paper mill, sugar mill, the Nigeria Dam, the Niger Bridge, Port extension, and construction of trunk roads, a security and minting plant.

The second development phase was originally aimed at reconstruction of facilities destroyed or damaged during the civil war 1967 – 1970. This was not fully realized as there were shortfalls and difficulties which led to a one year extension.

The third which lasted from 1975 to 1980. Emphasis was on transport and communications, manufacturing and crafts and general administration.

The fourth National Development Plan lasted between 1981 – 1985 and the overriding interest was to bring about improvement in the living conditions of the people.

The total investment of ₦82 Billion was envisaged as the Public was to take ₦70.5 Billion while the private sector was to have ₦11.5billion.

4.0 CONCLUSION

In this unit, effort has been made to discuss fully the Nigerian National Development Plan. Each of the four national plans was fully enumerated. Prior to the era of independence in 1960, there were two separate development plans under the colonialists. The entire era, general objectives and specific ones are properly highlighted with their highpoints.

5.0 SUMMARY

Nigeria had two Development Plans during the Colonial Era. In the wake of her Independence in 1960 plans for development commenced as follows:

1st Development Plan – 1962 – 68
2nd Development Plan – 1970 – 74
3rd Development Plan – 1975 – 80
4th Development Plan – 1981 – 85.

6.0 TUTOR - MARKED ASSIGNMENTS

1. What do you understand by development plan in Nigeria?
2. Outline the main objectives of 2nd National Development Plan?

7.0 REFERENCES/FURTHER READINGS

Rotimi, Ajibola: (2005), (2005). *Public Finance Principles and Practice*

Daniel, G. I: (1996). *Public Sector Accounting*

MODULE 5

UNIT 1 PUBLIC REVENUE AND EXPENDITURE: SOURCES OF PUBLIC FINANCE

CONTENTS

1.0 INTRODUCTION

Public finance refers to all activities of government in generating and allocating (spending) revenue towards ensuring efficiency of the state and general well-being of the people. It is the financial operation of public treasury and its implication. Professor Dalton says that Public Finance is concerned with the Income and Expenditure measures of the Public Budget authorities together with the adjustment of one to the other.

2.0 OBJECTIVES

At the end this unit, students should be able to:

- Define public finance
- Itemize sources of Revenue in the Public Sector
- Point out what the make-ups of the oil classifications are
- Explain the constituents of the non-oil revenue.

3.0 MAIN CONTENT

3.1 Sources of Public Finance

Public revenue can be defined as income generated by the Public Sector from various services rendered. In other words, it could mean a portion of total funds required by government for the purpose of financing its activities. A high proportion of government revenues come from fees, fines, rent, royalty, taxes, income from government investments, rates, license etc.

In the views of G.I Daniel (*Public Sector Accounting*, 1999), the government must earn some money in order to sustain itself and perform its duties to the nation through some fiscal measures.

The money required by government to perform its duty must be obtained from a source and utilized on Recurrent and capital Expenditure.

Therefore, revenue to the government is very important because without the fund, the government would not be able to fulfill, its obligations to the public.

There are two main sources of Government Revenue: Oil Revenue and Non-oil Revenue.

3.2 Oil Revenue

This source consists of Royalties, Petroleum Profit, Rent, NNPC earnings from direct sales proceeds of selling crude oil to domestic market, penalty for gas flared, pipeline licenses, oil subsidy and other fees.

3.2.1 Non Oil Revenue

These are indirect taxes, import duties, Export Duties, Direct tax, company income tax fees, and value added tax (VAT).

The revenue derived from various sources are classified into various heads and sub- heads. The heads stand for the main sources of revenue while the sub-heads stand for sub-source under the main source.

4.0 CONCLUSION

Diagrammatic Representation of Public Revenue

Oil Revenue	Non Oil Revenue	Independent
* NNPC Earnings	* Import Duties	* Revenue Sources
* Petroleum Profit	* Export Duties	* Fines
* Tax	* Excise duties	* Fees
* Royalty	* Stamp duties	* Rates
	* VAT	* License
	* Personal Income Tax	* Income from Govt. Investment
	* Corporate Tax	
	* Capital Gain Tax	
	* Capital Transfer tax	

5.0 SUMMARY

Public Revenue Tree

This is a graphical description of public revenue according to their classifications or grouping.

PUBLIC REVENUE

A. OIL CLASSIFICATION | B. TAX CLASSIFICATION

A. OIL CLASSIFICATION OF PUBLIC REVENUE

PUBLIC REVENUE

OIL
NNPC Earning Royalties
from Crude Oil Petroleum
Profit Tax

NON OIL

TAX REVENUE

Import Duties

Export Duties

Excise Duties

Value Added Tax

Company Income Tax

Personal Income Tax

Capital Gain Tax

Capital Transfer Tax

INDEPENDENT
Revenue
Rent
Rate
Fines
Fees
Licenses
Income from
Business
Activities

B. TAX CLASSIFICATION OF PUBLIC REVENUE

PUBLIC REVENUE

DIRECT TAX
Personal Income Tax
Company Income Tax
Petroleum Profit tax
Capital Gain Tax
Capital Transfer Tax

INDIRECT TAX
Import Duties
Export Duties
Excise Duties
Value Added Tax
Licenses

NON-TAX REVENUE
Fines
Fees
Rates
Rent
Income From Business
Activities

6.0 TUTOR - MARKED ASSIGNMENTS

1. Explain the meaning of public finance?
2. What constitutes the oil revenue source of funds?
3. Itemize the source of funds in the non-oil sector?

7.0 REFERENCES/FURTHER READINGS

Daniel,G.I: *Public Sector Accounting*

Rotimi, Ajibola: *Public Finance Principles and Practices*.

UNIT 2 PUBLIC EXPENDITURE – MEANING AND REASONS

CONTENTS

1.0 INTRODUCTION

In this unit, we shall discuss fully issues in public expenditure. We shall start with the meaning of public expenditure and later reasons for increase in public expenditure shall be analyzed.

2.0 OBJECTIVES

At the end of the unit, the students should be able to:

- Recall the sources of public finance in Nigeria.
- Explain the meaning of public expenditure.
- Mention the reasons for public expenditure.

3.0 MAIN CONTENT

3.1 Public Expenditure

Public expenditure refers to the expenses which the government incurs for maintaining itself and the economy as a whole. It is the cost incurred by the public sector in order to achieve specific objectives.

Public expenditure can also be defined as the expenses incurred by the government in the course of performing its operations. It includes: salaries and wages of civil and public servants, road construction, defense, maintenance of laws and order, public infrastructure, e t c.

3.2 Reasons for Increase in Public Expenditure

1. Increase in area and population. The physical boundaries of the state have been widened. The population figure has considerably gone up and government has to cater for the needs of people scattered over a much wider area;
2. Growth of state functions: As the classical doctrine of Laissez faire gave way to Keynesian economics, the role of the government gradually expanded from that of maintenance of law and order, to a welfare state. Government expenditure items therefore expanded from the maintenance of the police and state bureaucracy to include the provision of basic needs and public infrastructure;
3. Higher price level and rising cost of public services. There have been rise in the cost of essential commodities all over the place. In the good old days, Lux soap was sold for 50k but now, it is ₦50.00. Government therefore has to source for higher amount of money to pay for commodities and services purchased;
4. Provision of Public Utility services (water, electricity and transport). These are best provided by the state or local government authority due to cost;
5. Expansion in social services (Education, Health etc) this has led to the establishment of schools, colleges and universities in very large numbers. Other measures like environmental sanitation exercise and clearing of slums in our surrounding are productive investments as they lead to increase in income and employment;
6. Technological changes: These call for larger or new production in the public sector and these improvements in techniques are best exploited by government since life of the people are improved upon;
7. Defective financial and civil administration: Duplication and unnecessary multiplication of government agencies is very common. Wrong allocation of resources and functions also lead to extravagance;
8. Requirements of full employment: The public expenditure naturally shoots up as governments launch ambitious scheme in order to provide full employment for the teaming population;
9. Increasing cost of servicing debt: This result from the existence of deficit budgeting and balance of payment deficit. Debts have to be paid and there is need for repayment schedule which increases public expenditure.
10. Inflation: Increase in price of inputs and other goods purchased by public sector have resulted in increase in public expenditure.

4.0 CONCLUSION

The issues raised have explained the meaning of public expenditure and reasons for their increase in any given state.

5.0 SUMMARY

Public expenditures refer to expenses incurred by the government in the course of performing its day to day operations.

The dynamism of the state, its affair and environment has led to increase in public expenditure. Provision of public utilities (water, electricity and transport). Technological changes, expansion in social services, inflation, etc lead to increase in public expenditure

6.0 TUTOR-MARKED ASSIGNMENTS

1. What is the meaning of Public Expenditure?
2. Are technological changes and inflation the only reasons for increase in Public Expenditure?
3. Name ten and discuss four reasons why government expenditure keeps increasing.

7.0 REFERENCES/FURTHER READINGS

Rotimi, Ajibola : Public Finance (*Principles and Practice*)

Daniel,G.I: *Public Sector Accounting.*

UNIT 3 PUBLIC EXPENDITURE: CLASSIFICATIONS AND EFFECTS

CONTENTS

1.0 INTRODUCTION

We shall attempt identifying different classifications of Public Expenditure. The effect of Public Expenditure will also be discussed in this unit.

2.0 OBJECTIVES

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

- Recall the meaning and reasons for Public Expenditure
- Explain the classification of Public Expenditure
- Expatiate on the effects of embarking on Public Expenditure.

3.0 MAIN CONTENT

In classifying Public Expenditure, we shall consider three different areas, namely, Natural, Object and Functional classifications:

3.1 Natural Classifications

1. Productive versus Unproductive Expenditure: Productive expenditure refers to investment expenditures which boost the productive capacity of the nation. Examples include establishment of projects like NITEL, NEPA, NNPC, NIPOST etc. Unproductive expenditure does not have direct impact on the productive capacity of the nation. For instance, Defence, Police, Judiciary and general maintenance of the nation.

2. Transfer versus non- transfer expenditure: Transfer expenditure are incurred on third party basis in which the recipient has the right as to what and how to spend the resources. e.g students, bursary, scholarship, old people's allowance etc. While non-transfer expenditure refers to those resources actually

spent by the government in producing goods and services for the people e.g expenditure on educations, health, roads etc.

3. Capital versus recurrent expenditure: Capital Expenditures are Expenditures on new projects which have long term benefits e.g. road construction, establishment of mining complexes, electrification, water corporation etc. Recurrent Expenditure considers short term and Recurring item e.g salaries, repairs and maintenance of good roads.

Object Classification

a. Personnel services and benefits
b. Contractual services and suppliers.
c. Acquisition of capital Assets
d. Currents and fixed charges

Economic Functional classification

a. General services
b. Community services
c. Social services
d. Economic services
e. Transfer and other expenditure

3.2 Effects of Public Expenditure

i. Effects on Production: Most public expenditures are productive, directly or indirectly. For instance, the running of commercial enterprises by government is directly productive – railways, state transport corporations etc.

ii. Effects on Distribution: Public Expenditure can have wholesome influence on the distribution of wealth in the community. It can reduce inequalities in income, thereby bridging the gap between the rich and the poor. Government can subsidize goods the production of which is consumed by the poor or lower income group in the society.

iii. Effects on Economic Stabilization: The freer an economy, the greater the degree of fluctuation in terms of price, employment and output. Public Expenditure can be designed as a counter cyclical fiscal measure designed to create effective demand thereby stimulating investment activities.

iv. Effect on Level of Income and Employment: Public Expenditure affects the level of income and employment in the country. This is done according to Keynes, by government through liberal expenditure on public works. This increases income and employment many times more than what is invested (income multiplier).

4.0 CONCLUSION

The unit has discussed the three major classification areas – Natural, object and functional. Each of these sub-groups has been discussed for clearer picture. The effects of public expenditure have also been explained.

5.0 SUMMARY

In the classification formats, three have been identified. They are natural, object and economic functional. In Natural classifications, there are productive and unproductive which differentiates investment on NEPA and the police.

Effects on production establish the benefits of investing in either war or commercial enterprises.

6.0 TUTOR-MARKED ASSIGNMENTS

1. Explain the three formats used in classifying public expenditure?
2. Name three effects of Public Expenditure

7.0 REFERENCES/FURTHER READINGS

Rotimi, Ajibola: Public Finance (*Principles and Practice*).

Daniel,G.I : *Public Sector Accounting*.

UNIT 4 MANAGEMENT OF PUBLIC DEBT – MEANING AND CLASSIFICATIONS

CONTENTS

1.0 INTRODUCTION

In this unit, the meaning and classification of public Debts shall be established. The circumstances and basis for public debt and the main agency for managing the debts shall be explained.

It is of note that the statutory function of central bank involves the raising of money either within or outside the country to finance developmental programmes or balance of payment disequilibrium. The performance of this role gives rise to national debt otherwise called Public debt.

This is distinguished from private debts which consist of obligations to individuals, business firms and non – governmental organizations. Public debt also differs from state or local government debt which usually creates no headlines.

2.0 OBJECTIVES

At the end of the unit, students should be able to:

- Recall the classifications and effects of public expenditure.
- Explain the meaning of Public debt.
- Differentiate public debt from private debt.
- Classify public debts

3.0 MAIN CONTENT

3.1 Meaning of Public Debt

Public or National Debt can be defined as the money owed by the central government to its citizens (domestic public debt) and the overseas governments (external debts). It is the total amount of money owed by the central government of a country to all its various creditors, including private individuals, banks and even the International Monetary Fund (IMF).

Public debt is the total outstanding financial obligations of the government whether acquired or borrowed during a particular period. Hence, it is the liability of the government payable at a future time.

Public debt can also be seen as the money owed by the government to institutions, governments and individuals residents in or outside the economy.

It is a good source of capital formation apart from taxation in a developing economy.

Nigeria has in fact been identified in the "Baker Plan" of 1985 as one of the 15 most heavily indebted among the developing countries who would need to engage in structural economic reforms, adopt the right growth-oriented policies, and attract the much needed fresh funds from external sources, before they could easily get out of their debt problems.

As at December 1986, Nigeria's external debt outstanding amounted to ₦42.2 billion and the debt service ratio during that year was 29.4%. The ratio could have been higher but for the relief given the country by some of her creditors. As at June 2005, the outstanding indebtedness stood at $36.0 billion out of which 28.0 billion is owed to Paris club and the remaining to the World Bank.

Recently, with the oil price hike resulting from the war in Iraq, the Nigerian government has negotiated and reduced her debt profile maximally to a reasonable amount. Thanks to Mrs. Ngozi Okonjo-Iweala, the former Minister for finance of the Federal Republic.

3.2 Classification of Public Debt

The type of public debt reflects the purpose for which the debt was incurred. The following are typical examples:

a. **Internal Debt**: This refers to the money owed to some citizens of the country. It is the money raised within the economy. It is sometimes called Domestic Debt. Repayment is effected in local currency by transferring tax revenue to the creditors.

b. **External Debt**: This refers to the money borrowed by the government of one country from the government or non-governmental institutions of other countries. This follows that the creditor is a foreigner. The repayment is made in currency other than that of the debtor country.

c. **Trade Debt**: This arises when Nigeria trades with other countries and is unable to pay, either partly or wholly, for the goods and services supplied. For example, in the early 1980s, Nigeria's inability to settle her import bills resulted in the accumulation of trade arrears, amounting to N4.4 billion in 1983.

d. **Balance of Payment support Loan**: The overall economic transactions between a country and the rest of the world, classified into current and capital Accounts, and official settlement balance, constitute the balance of payment which may be favourable when it is deficit. However, a persistent unfavourable balance of payment, often referred to as balance of payments disequilibrium, may inform governments decision to seek for balance of payments support loans from institutions such as the International Monetary Fund (I.M.F).

e. **Project – Tied Loans**: Investments which have good potentials and prospects to accelerate economic growth and development, may lead government into contracting project -tied loan. As implied, this type of debt which is for the execution of a particular project is supposed to be self-liquidating.

f. **Loans for Socio-Economic Needs**: The provision of infrastructure, health, education and other social amenities may necessitate borrowing by government to finance them.

g. **Funded Debts**: These are debts for which sinking funds have been provided. They are loans with lesser risk of default as provision has been made for redemption at maturity.

h. **Unfunded Debts**: These are debts without any specific provision for redemption. Therefore unfounded debts carry higher risk of default.

i. **Marketable Debts**: These are loans which are securitized or which can be resold by the existing debt holder to a willing buyer.

j. **Non-marketable Debts**: These are loans issued to particular debt-holder which cannot be resold in the secondary market.

k. **Loan Pooling**: This refers to the acquisition of loans from various sources in order to execute a particular project.

l. **Loan Consolidation**: This refers to the gathering or consolidation of loans before utilization.

4.0 CONCLUSION

Public debt is made up of money owed by the government to institutions, governments and individuals within or outside the economy.

Debts owed to local creditors are called domestic debts while the ones owed the foreign bodies and institutions are called foreign debts.

The purpose for which debt is incurred signifies the type of debt. They are many and include both internal and external debts among others in the list.

5.0 SUMMARY

Public or National debt is defined as money owed by the government to its citizens (domestic debts) and the overseas governments and institutions (external debts).

In developing economies, apart from taxation, public debt is a good source of capital formation.

The following are the classification of public debts: internal, external, trade debt, balance of payment support loan and project-tied loans, funded debts, to mention but a few.

6.0 TUTOR – MARKED ASSIGNMENTS

1. What is the meaning of Public or National Debt?
2. What is the current public debt situation of Nigeria?

7.0 REFERENCES/FURTHER READINGS

Rotimi, Ajibola: *Public Finance principles and Practices*.

Uremadu,S.O: Modern Public Finance (*Theory and Practice*).

UNIT 5 MANAGEMENT OF PUBLIC DEBTS

CONTENTS

1.0 INTRODUCTION

In this unit, the students will be exposed to Debt Management activities. These will be considered at the domestic and external levels.

The Central Bank of Nigeria has set up a department to handle the responsibility of debt management. This role is performed in conjunction with the Federal Ministry of Finance and other agencies.

2.0 OBJECTIVES

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

- Recall the meaning of public debt and its classifications.
- Explain debt management
- Discuss the issues in domestic debt management.
- Mention the involvements in external debt management.

3.0 MAIN CONTENT

3.1 Domestic Debt Management

The Central bank of Nigeria is statutorily entrusted with the function of management of the domestic debts of the Federal government. This involves the following activities

a. Advising government as to the timing of floatation of debt instruments and terms of issue;
b. Advertising the public subscriptions to the issue;

c. Collecting the proceeds of the issues on behalf of the government, supervising the issue of certificates and warrants accounts in respect of receipts and disbursement;

d. Payment of interest and principal on the debts and managing the sinking fund set up to facilitate its redemption.

The bank provides information on regular basis and advises government about the position and implications of domestic debt.

3.2 External Debt Management

This is more intricate and requires careful planning. 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 a judgment on the desirability of contracting further loans.

Nigeria's external debt management strategies have varied from time to time since the early 1980s, when the debt crisis becomes pronounced. However, in February 1988, comprehensive measures were set out with the following policy objectives:

To evolve strategies for increasing foreign exchange earnings thereby reducing the need for external borrowing, to set out the criteria for borrowing from external sources and determine the type of projects for which external loans maybe obtained, to outline the mechanism for servicing external debts of the public and private sectors; to outline the role and responsibilities of the various organs of the Federal and State governments as well as the private sector in the management of external debt.

Consequently, the following guidelines were issued as regards governments borrowing:

1. Economic sector projects should have positive internal rate of return as high as the cost of borrowing;
2. Projects to be financed with external loans should be supported with feasibility studies (which include loans acquisition, deployment and retirement schedule);
3. Social services or infrastructure would be ranked on the basis of their cost / benefit ratios;

4. External loans for private and public sector projects with quick returns could be sourced from the international capital markets

while loans for social services can be sourced from concessional financing institutions;

5. Borrowing by state governments, parastatals and private agencies must receive approval from the Federal Government to ensure that the borrowing conforms to the national objectives. Approval granted to the private agency does not guarantee currency undertaking by the Federal Government;
6. The state governments' borrowing proposals should be submitted to the Ministry of Finance and Economic Development and the Central Bank of Nigeria for consideration before they are incorporated in the final public sector borrowing for the annual budget;
7. State governments and their agencies as well as Federal parastatals should service their debts through the Foreign Exchange Market (FEM) and inform the Federal Ministry of Finance and Economic Development for record purposes. For failure to service their debts, the naira equivalents would be deducted at source before the balance of their statutory allocations are released;
8. As for the private sector, industries that are export oriented should service their debts from their export earnings, while others should utilize the FEM facilities to service their debts.

4.0 CONCLUSION

The unit has highlighted the responsibilities of the Central Bank, Federal Ministry of Finance and Economic Development in terms of debt management.

The central bank is seen to be in the centre of debt management in both domestic and external debts.

5.0 SUMMARY

Debt management has become a major function of the Central Bank of Nigeria, Ministry of Finance and Economic Development and other agencies.

Domestic loans are solely managed by the Central Bank as a statutory responsibility.

Despite advertising for public subscription to the issue, the bank provides information on regular basis and advises government on the position and implications of domestic debts.

More so, the bank is at the centre of the management of External debts. This involves a conscious and carefully planned schedule of loans acquired either for developmental purposes or to support the balance of payments.

Since the 1980s, the external debt management strategies have varied from time to time to avoid further debt crisis. Guidelines are issued and strictly monitored as regards government borrowing.

6.0 TUTOR-MARKED ASSIGNMENTS

1. What is the meaning of debt management?
2. What are the issues in domestic debt management in any economy?
3. Which organization is at the centre of debt management in Nigeria and what are their main instruments of duty?

7.0 REFERENCES/FURTHER READINGS

Uremadu,S.O.: Modern Public Finance (*Theory and Practice*).

Rotimi, Ajibola: *Public Finance: Principles and Practice*.