COURSE GUIDE

PSM 829
BUDGETING AND BUDGETARY PROCEDURE

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INTRODUCTION

PMS 829 Budgeting and Budgetary Procedure is a two-credit unit course. It is prepared for students offering M.Sc. in Public Sector Management, a programme available in the School of Management Sciences, National Open University of Nigeria.

The course is a useful material in your academic pursuit as well as in your place of work as managers, administrators, and so on.

COURSE CONTENT

The course focuses on budgeting and budgeting procedure in the Public Sector. However, relevant but indirect issues are also discussed to expand your knowledge base on this topic.

COURSE AIM

The main aim of the course is to equip you with adequate information on budgeting and budgetary procedure that will enable you access sufficient knowledge that is applicable to Public Sector Management. Primarily, the course is presented in a form that will aid easy assimilation and application as you invest your time in studying the course material.

COURSE OBJECTIVES

At the end of studying the course material, among other objectives, you should be able to:

- discuss what a budget is
- describe budgeting
- explain budget committee
- describe the functions and responsibilities of a budget committee
- discuss the various responsibility centre
- describe a master budget
- describe and prepare a cash budget
- describe a sales budget
- describe and prepare a production budget
- explain a capital budget
- explain the meaning of a balanced budget
- discuss a balanced budget amendment
- discuss problems associated with balanced budget rule
- state the stages involved in the budgeting process
- discuss the role of budget personnel in budgeting process
- state briefly how budgets are revised

- state briefly the keys to a successful budgeting process
- discuss the method of preparing budgets adopted by the various tiers of government in Nigeria
- state the advantages and disadvantages of the incremental budgeting method
- describe the factors affecting the budgeting system in the public sector
- state the purpose of government accounting
- state the powers of the Accountant-General of the Federation
- state the functions of the Accountant-General of the Federation
- state areas the Auditor-General is expected to give his opinion
- state the powers of the Auditor-General for the Federation
- state some indirect accounting functions performed by the Auditor-General
- describe the executive control over budgeted expenditure
- discuss the legislative control over budgeted expenditure
- discuss the control over budgeted expenditure exercised by the Ministry of Finance
- discuss the treasury control over budgeted expenditure
- discuss the departmental control over budgeted expenditure.

COURSE MATERIALS

The course material package is composed of:

1. The Course Guide
2. The Study Units

THE STUDY UNITS

The study units are as listed below:

Module 1 The Concept of Budgeting

Unit 1 Conceptual Clarification on Budgeting and Budgetary Procedure
Unit 2 Types of Budget
Unit 3 Zero Base Budgeting

Module 2 Government Budgeting

Unit 1 Balanced Budget
Unit 2 Budgeting Process
Unit 3 Budget Process in Appropriation Bill (1)
Unit 4 Budget Process in Appropriation Bill (2)

Module 3 Budgeting and Control

Unit 1 Budgetary Control
Unit 2 The Accountant-General of the Federation
Unit 3 The Auditor-General for the Federation
Unit 4 Expenditure Control

Module 4 Budgeting and Strategy

Unit 1 Operational Budgeting
Unit 2 Capital Budgeting
Unit 3 Budgeting and Development Planning
Unit 4 Project Performance Budgeting System
Unit 5 Strategic Decision Making Process, Implementation and Control

ASSIGNMENTS

Each unit of the course has a self-assessment exercise. You will be expected to attempt them as this will enable you understand the content of the unit.

TUTOR-MARKED ASSIGNMENT

The Tutor-Marked Assignments (TMAs) at the end of each unit are designed to test your understanding and application of the concepts learned. Besides the preparatory TMAs in the course material to test what has been learnt, it is important that you understand that at the end of the course, you must have done your examinable TMAs as they fall due, which are marked electronically. They account for 30 percent of the total score for the course.

SUMMARY

PSM 829 Budgeting and Budgetary Procedure exposes you to issues in budgeting relating to public sector management.

On successful completion of the course, you would have been armed with viable knowledge that will aid your academic and professional pursuit.

MAIN COURSE

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MODULE 1 THE CONCEPT OF BUDGETING

Unit 1 Conceptual Clarification on Budgeting and Budgetary Procedure
Unit 2 Types of Budget
Unit 3 Zero Base Budgeting

UNIT 1 CONCEPTUAL CLARIFICATION ON BUDGETING AND BUDGETARY PROCEDURE

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1.0 INTRODUCTION

Budgeting is what governments, government departments, business organisations and individuals do to keep their financial lives in shape between what they earn and what they spend.

You will observe that government has to spend its money on defense, the judiciary, the police force, health, education, roads, etc. through government departments. These government departments have their budgets for infrastructure, plant and machinery, property, schools, hospitals, staff training and other things needed to run their operations.

You will also observe that alongside governmental departments are major corporations for example, Power Holding Company of Nigeria and Nigerian Railway Corporation. These corporations have to budget, although their incomes do not necessarily come directly from government (unless they are given a development grant), but from earnings on sales of the goods and/or services they provide.

Similarly, businesses set their budgets for staff wages, rent, and property among others. In the same vein, as an individual, you must have drawn up a budget showing what comes in as revenue from work or other sources of income, and what goes out in housing, food, clothing, education, and so on. Therefore, budgeting is relevant to all.

2.0 OBJECTIVES

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

- discuss what a budget is
- describe budgeting
- explain budget committee
- describe the functions and responsibilities of a budget committee
- discuss the various responsibility centre.

3.0 MAIN CONTENT

3.1 What is a Budget?

You will observe that the word budget has been mentioned in the introduction to this unit as what government, major corporations, businesses and individuals carry out to keep up their financial shape in order. In this sub unit, let us discuss the question, what is a budget?

A budget is a financial document used to protect future income and expenses. It could also be defined as a formal statement of the financial resources set aside for carrying out specific activities in a given period of time. It is the most widely used means for planning and controlling activities at every level of an organisation. A budget indicates the expenditures, revenues, or profits planned for some future date. The planned figures become the standard by which future performance is measured.

Why are budgets such a fundamental part of many organisations' control programmes? There are some reasons for this question. First and most importantly you should note that budgets are widely used because they are stated in monetary terms. Secondly, budgets establish clear and unambiguous standards of performance. Budgets cover a set time period. At stated intervals during the time period, actual performance will be compared directly with the budget. Often, deviations could quickly be detected and acted upon. In addition, by submitting budgets to a higher authority for approval, managers commit themselves to reaching the budgeted objectives. Thus, their responsibility for those objectives is clear.

For these reasons, budgets are not only a major control device but also one of the major means of coordinating the activities of an organisation.

3.2 What is Budgeting?

Budgeting is a programme for spending. If you are having difficulty conceptualising the word "budgeting," just call it by a different name such as "financial planning". That is what budgeting is. It is a proactive approach rather than a reactive approach to managing resources. Budgeting makes it easier for governments, government departments, businesses and individuals with incomes and expenses of all sizes to make conscious decisions about how they will prefer to allocate their resources.

Budgeting is a plan to balance expenditure against income, to balance the financial books. It is what governments, government departments, businesses and individuals have to do to keep financial demand in place between what they earn and what they spend. Budgeting is a plan for spending, saving and paying debts within income.

Budgeting is one of the most important skills that you can have. In any economic forecast, planning and budgeting are crucial when it comes to conserving and increasing your resources. The use of a budget can be helpful to not only individuals and companies but governments and government departments to stay afloat. The services of accounting professionals are often utilised by these departments to keep track of their finances in order to succeed.

3.3 Budget Committee

A budget committee is a group of people that creates and maintains fiscal responsibility for an entity or organisation. A budget committee typically reviews and approves departmental budgets that are submitted by the various departmental heads.

Budget committees play key roles in the success or demise of a company or other corporate entity. Committees that are able to keep their organisational budgets on track ensure smooth operation and financial solvency; those that cannot soon encounter financial problems. You should note that apart from companies and private businesses, government have committees on budget. For example, the United States House Committee on the Budget, commonly known as the House Budget Committee, is a standing committee of the Lower House of Congress of the United States. Its responsibilities include legislative oversight of the Federal budget process, reviewing all bills and resolutions on the budget, and monitoring agencies and programmes funded outside of the budgetary process. Similarly, in Nigeria, we have the Finance and Budget Committee of the National Assembly.

SELF-ASSESSMENT EXERCISE

Differentiate between the term budget and budgeting.

3.4 Functions and Responsibilities of a Budget Committee

A budget committee will usually be responsible for overall policy matters relating to budget programme and for coordinating the preparation of the budget itself. This committee generally consists of the chairman, vice chairman in charge of various functions such as sales, production and purchasing; and the controller.

Difficulties and disputes between segments of the organisation in matters relating to the budget are resolved by the budget committee. In addition, the budget committee approves the final budget and receives periodic reports on the progress of the organisation in attaining budgeted goals.

Disputes can erupt over budget matters. Because budgets allocate resources, the budgeting process to a large extent determines which department gets more resources, and which get relatively less. Also, the budget sets the benchmarks by which managers and their departments will be, at least, partially evaluated. Therefore, it should not be surprising that managers take the budgeting process very seriously and invest considerable energy in ensuring that their interest and those of their departments are protected.

3.5 Responsibility Centres

Any organisational or functional unit headed by a manager who is responsible for the activities of that unit is called a responsibility centre. We shall discuss four responsibility centres in this sub unit. They are revenue centre, cost centre, profit centre and investment centre.

1. **Revenue Centre**
   Revenue centres are those organisational units in which outputs are measured in monetary terms but are not directly compared to input costs. A sales department is an example of such a unit. The effectiveness of the centre is not judged by the extent to which revenue (in the form of sales) exceeds the cost of the centre (in salaries or rent, for example). Rather, budgets (in the form of sales quotas) are prepared for the revenue centre and the figures are compared with sales orders or actual sales. In this way, a

useful picture of the effectiveness of individual sales persons or of the centre itself can be determined.

2. Cost Centre

In a cost centre, inputs are measured by the control system in monetary terms, but outputs are not. The reason is that these centres are not expected to produce revenues. Examples are maintenance, administration, service, and research departments. Budgets will be devised only for the input portion of these centre's operations.

3. Profit Centre

In a profit centre, performance is measured by the numerical difference between revenues (outputs) and expenditures (inputs). Such a measure is used to determine how well the centre is doing economically and how well the manager in charge of the centre is performing. A profit centre is created whenever an organisational unit is given responsibility for earning a profit. In an organisation with divisions in which each of a number of divisions is completely responsible for its own product line, the separate divisions are considered profit centres.

4. Investment Centre

In an investment centre, the control system does not only measure the monetary value of inputs and outputs, it also assesses how those outputs compare with the assets employed in producing them. For example, assuming that a new hotel requires a capital investment of five hundred million naira in property, building, equipment and working capital, in its first year, the hotel has ten million naira in labour and other input expenses and thirty million in revenue. For two reasons, the hotel would not be considered to have earned a twenty million naira profit. First, an allowance must be made for the depreciation of building and equipment. Second, management must account for the interest that could have been earned from alternative investments. By assessing these factors as well, the company obtains a much more accurate picture of profitability. Managers can identify the return on an investment, not merely the actual inflow and outflow of naira.

4.0 CONCLUSION

A budget is an essential tool for all who want to ensure that their financial life remains healthy, whether as a body corporate or as an individual. An important part of effective budgeting is setting goals and using your budget to help you achieve them.

5.0 SUMMARY

Having studied this unit, you should recall that a budget is a formal statement of the financial resources set aside for carrying out specific activities in a given period of time. Budgeting is a plan for spending, saving and paying debts within income. A budget committee is a group of people that creates and maintains fiscal responsibility for an entity or organisation. A budget committee will usually be responsible for overall policy matters relating to budget programme and for coordinating the preparation of the budget itself. And finally, you should recall that any functional unit headed by a manager who is responsible for the activities of that unit is called a responsibility centre.

6.0 TUTOR-MARKED ASSIGNMENT

i. Explain the term budget committee.
ii. List and explain the various responsibility centres.

7.0 REFERENCES/FURTHER READING

Hansen, D. R. & Mowen, M. M. (2007). *Management Accounting*. USA: Thomson South-Western.

Robinson, M. (Ed.). (2007). *Performance Budgeting Linking Funding and Results*. USA.

Stoner, J. A. F., Freeman, E. R. & Gilbert, D. R. (1995). *Management*. New Jersey: Prentice-Hall, Inc.

UNIT 2 TYPES OF BUDGET

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1.0 INTRODUCTION

In this unit, you will be familiar with the various types of budgets. We will describe the various types of budgets an organisation can use. Before we begin our discussion, you should note that the comprehensive budgets of an organisation are usually divided into two parts: operating budgets and financial budgets. The operating budgets indicate the goods and services the organisation expects to consume in the budget period: they usually list both physical quantities (such as barrels of oil) and cost figures. The financial budgets spell out in detail the money the organisation intends to spend in the same period and where that money will come from. These different types of budgets make up the firm's overall budgetary plan. Specifically, in this unit, we shall discuss the master budget, cash budget, sales budget, production budget and capital budget.

2.0 OBJECTIVES

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

- describe a master budget
- describe and prepare a cash budget
- describe a sales budget
- describe and prepare a production budget
- explain a capital budget.

3.0 MAIN CONTENT

3.1 Master Budget

A master budget is an overall financial and operating plan for a forthcoming calendar or fiscal year. The master budget is really a number of sub-budgets tied together to summarise the planned activities of the business. The format of the master budget depends on the size and nature of the business.

As stated above, the overall or master budget summarises the other functional budgets. Consolidating the functional budgets, an income and expenditure budget and budgeted balance sheet are prepared. The master budget is usually a one year or quarterly budget expressing the expected asset, capital and liability positions for the projected year or quarter. Let us illustrate the master budget using the income statement below.

Master Budget - Profit and Loss Account

Particulars	January	February	March	Total
	₦'000	₦'000	₦'000	₦'000
Sales	150,000	180,000	160,000	490,000
Less: Cost of goods sold	49,000	67,000	52,000	168,000
Administration overheads	12,000	12,000	12,000	36,000
Selling overheads	8,000	11,000	9,000	28,000
Net profit	**81,000**	**90,000**	**87,000**	**258,000**

3.2 Cash Budget

The cash budget is for cash planning and control. Properly preparing your cash budget will show how cash flows in and out of your business. Also, it may then be used in planning your short-term credit needs. In today's financial world, you are required by most financial institutions to prepare cash budgets before making capital expenditures for new assets as well as for expenditure associated with any planned expansion. The cash budget determines your future ability to pay debts as well as expenses as they fall due. For example, preliminary budget estimate may reveal that your disbursement are lumped together and that with more careful planning, you can spread your payments to creditors more evenly throughout the entire year. Consequently, less bank credit will be needed and interest costs will be lower. Banks and other credit-granting institutions are more inclined to grant you loans under favourable terms if your loan request is supported by a methodical cash plan. Similarly, businesses that operate on a casual day-to-day basis are more likely to borrow funds at inopportune times and in excessive amounts. Without planning, there is no certainty that you will be able to repay your loans on schedule. However, once you have carefully designed a cash budget, you will be able to compare it to the actual cash inflows and outflows of your business. You will find that this comparison will go a long way in assisting you during future cash budget preparation. Also, a monthly cash budget helps pinpoint estimated cash balances at the end of each month, which may foresee short-term cash shortfalls. It presents expected cash inflow and outflow for a designated time period. The cash budget helps management keep cash balances in reasonable relationship to its needs and aids in avoiding idle cash and possible cash shortages.

The cash budget typically consists of four major sections. They are:

- Receipts section, which is the beginning cash balance, cash collections from customers and other receipts
- Disbursement section comprised of all cash payments made by purpose
- Cash surplus or deficit section, showing the difference between cash receipts and cash payments
- Financing section, providing a detailed account of the borrowings and repayments expected during the period.

The cash receipts section consists of a listing of all of the cash inflows during the budgeting period except for financing. Generally, the major source of receipts will be from sales. The disbursement section consists of all cash payment that is planned for the budgeted period. These payments will include raw materials purchases, direct labour payments, manufacturing overhead costs, and so on as contained in their respective budgets. In addition, other cash disbursements such as equipment purchase, dividends and other cash excess or deficiency section is computed as follows:

Cash balance beginning	XXX
Add receipts	XXX
Total cash available	XXX
Less disbursements	XXX
Excess (deficiency) of cash available over disbursements	XXX

If there is a cash deficiency during any period, the company will need to borrow funds. If there is cash excess during any budgeted period, funds borrowed in previous periods can be repaid or the excess funds can be invested.

The financing section deals with the borrowings and repayments projected to take place during the budget period. It also includes interest payments that will be due on money borrowed.

A cash budget is cumulative in that the balance from one month is carried forward to the other month. The cash budget ignores none-cash items, such as depreciation, which is a loss of value of fixed asset which does not cause a loss of cash.

From the discussion on cash budget stated above, you can see that a cash budget consolidates all the cash inflows and outflows for the business. The cash budget is also a functional budget. The cash budget helps the business to plan the project purchases as well as to provide for the loan requirements. The cash budgets also help in defining the repayment plans for short and long term loans of the business. The cash budget is based upon the business policy of holding a certain amount of cash. This is the desired opening cash balance for the business. Accordingly, the cash budget forecasts the loan requirements or short term investments that are to be made with excess cash at any point in time.

Format of a Cash Budget

Months	**January**	**February**	**March**	**April**
Receipts:				
Cash sales		X		
Debtors		X		
Loan		X		
Total receipts		Y		
Payments:				
Cash purchases		X		
Creditors		X		
Fixed assets		X		
Expenses		X		
Total payments		Z		
Net receipts/payments		W		
Add opening balance		B		
Closing balance		C		

Y is equal to the total of all the receipts.
Z is equal to the total of all the payments.
W is equal to Y minus Z.

C is equal to W plus B, which is the closing balance for that month, and this becomes the opening balance in the next month.

So, the cash budget format can be summarised as follows: the total of all the receipts, less the total of the payments equals the net receipt, if the answer is positive or net payment if the answer is negative. This net receipt or payment is then added to the opening balance to give the closing balance, which becomes the opening balance in the next month. The opening balance represents the figure for cash or bank at the end of last month.

Example
A company produces only one product and it sells for ₦60 each. Total variable cost is ₦20. This is made up of material ₦10, labour ₦6 and overheads ₦4. Fixed costs are ₦10,000 per month payable one month in arrears. Sales in units are 1,800, 2,100, 2,300 for April, May and June respectively. Productions in units are 2,000, 2,200, 2,200 for April, May and June respectively. Labour costs are paid in the month they are incurred. Suppliers of materials give one month credit. The variable overheads are paid for in the month following production. Sales are 50% for cash and 50% on one-month credit. Opening balance at the beginning of April is ₦60,000. Prepare the cash budget for the month of April to June 2010.

We have to calculate the individual cost of material, labour and overheads. This is done by taking the number of units produced in each month and multiplied by the cost per unit. For example, the material cost for April will be 2000 x ₦10 = ₦20,000. It will be the same calculation for labour and overheads for each month. The sales will be the number of units sold multiplied by the selling price per unit, that is, for April 1800 x ₦60 = ₦108,000.

Solution
Cash budget for the three months ending June 2010

	April	May	June
	₦	₦	₦
Receipts			
Sales			
Cash	54,000	63,000	69,000
Debtors		54,000	63,000
Total receipts	54,000	117,000	132,000

Payments			
Materials		20,000	22,000
Labour	12,000	13,200	13,200
Overheads		8,000	8,800
Fixed overheads	10,000	10,000	10,000
Total payments	22,000	51,200	54,000
Net receipt/payment	32,000	65,800	78,000
Add opening balance	60,000	92,000	157,800
Closing balance	**92,000**	**157,800**	**235,800**

SELF-ASSESSMENT EXERCISE

The expected sales and purchases figure of Great Atlantic Ltd. from November 1995 to June 1996 are as follows:

Month	Sales	Purchases
	₦	₦
Nov. ’96	3,000	3,000
Dec. ’95	3,500	1,000
Jan. ’96	2,500	800
Feb. ’96	2,000	1,000
Mar. ’96	2,500	1,200
April ’96	3,000	1,400
May ’96	3,500	1,500
June ’96	3,800	1,500

The company has established a sale policy of 20% cash and 80% credit, 40% and 60% of credit sales are collectable in the first and second month after sales respectively. The company suppliers granted credit purchase of one month. All company’s purchases were on credit. The company has budgeted for a capital expenditure of ₦1,500 and ₦300 for the month of March 1996 and April 1996 respectively. Dividend of ₦1,200 is to be paid in three installments starting from April 1996. An outstanding tax liability of ₦250 is planned to maintain a minimum cash balance of ₦1,500 in each month. Salary for each month will amount to ₦500.

You are required to determine the cash position of the company from Jan. 1996.

3.3 Sales Budget

A sales budget is a detailed schedule showing the expected sales for the budget period. Typically, it is expressed in both naira and units of production. An accurate sales budget is the key to the entire budgeting in some way. If the sales budget is poorly done, then the rest of the budgeting process is largely a waste of time.

The sales budget will help to determine how many units will have to be produced. Thus, the production budget is prepared after the sales budget. These budgets are then combined with data from the sales budget and the selling and administrative expenses budget to determine the cash budget. In essence, the sales budget triggers a chain reaction that leads to the development of the other budgets. The selling and administrative expenses budget is both dependent on and a determinant of the sales budget. This reciprocal relationship arises because sales will in part be determined by the funds committed for advertising and sales promotion. The sales budget is the starting point in preparing the master budget. All other items in the master budget including production, purchase, inventories, and expenses, depend on it in some way. The sales budget is constructed by multiplying the budgeted sales in units by the selling price. Usually, the first of all budgets to be compiled is the sales budget. This particular budget will be dependent for creating the others.

For example, XYZ Ltd is expecting (budgeting) the following sales revenue in the next three months.

	January	**February**	**March**
Product A	1,800	1,900	2,000
Product B	2,000	2,200	2,100
Product C	1,700	1,500	1,500

These figures will have been calculated by multiplying the expected number of sales by the selling price of the product. If you have close relations with a majority of your customers, you could contact them in advance to find out how much they are expecting to buy from you in the forthcoming budget period. If you allow credit to customers, it is important that you put all credit sales in the month that you receive the money; not when you made the sale. For example, if you sell a product in January with two months credit, the revenue would be counted for in March and not January.

SELF-ASSESSMENT EXERCISE

List the major sections of a cash budget.

3.4 Production Budget

The production budget is prepared after the sales budget. The production budget lists the number of units that must be produced during each budget period to meet sales needs and to provide for the desired closing stock. Production needs can be determined as follows.

Budgeted sales in units	XXX
Add desired closing stock	XXX
Total stock needed	XXX
Less opening stock	XXX
Required production	XXX

Production requirements for a period are influenced by the desired level of closing stock. Stock should be carefully planned to avoid excess stock and storage problems. Insufficient stock can lead to loss of sales or crash production efforts in the following period. Again, production budget is assuring that the business is product oriented. Should your business be a service centre organisation, you could use the same approach calling it an operating budget.

The production budget is made to ensure the business will be made for the proposed flow of stock using unit numbers instead of financial figures. The production budget would be split up for the individual products/services if you supply more than one as in the sales budget example in section 3.3 above. For example, assuming there is a desired closing stock of 300 units for January, 250 units for February and 350 units for March, for each of the products. And if the opening stock were 240, 180 and 330 for product A, B, C respectively, we have:

Production Budget

Product A	**January**	**February**	**March**
Budgeted sales in units	1,800	1,900	2,000
Add desired closing stock	300	250	350
Total stock needed	2,100	2,150	2,350
Less opening stock	240	300	250
Required production	1,860	1,850	2,100
Product B			
Budgeted sales in units	2,000	2,200	2,100
Add desired closing stock	300	250	350
Total stock needed	2,300	2,450	2,450
Less opening stock	180	300	250
Required production	2,120	2,150	2,200

Product C

Budgeted sales in units	1,700	1,500	1,500
Add desired closing stock	300	250	350
Total stock needed	2,000	1,750	1,850
Less opening stock	330	300	250
Required production	1,670	1,450	1,600

You should note that the sales units are the ones in unit section 3.3 above. And also note that the closing stock for a period becomes the opening stock for the next period. This budget will be used to propose how much you will manufacture so that you can meet the demand identified in your sales budget.

3.5 Capital Budget

A capital budget includes planned outlays for long-lived assets that are expected to generate income or support business operations over a number of years. These usually exceed cost minimums as dictated by accounting and/or tax rules, and include, but are not limited to: land, building, machinery, office equipment, furniture and fixtures, vehicles, investments in other companies and so on.

According to accounting and tax rules, and varying by type of asset, the expenditures made on capital items such as those listed above normally, are spread over a number of years for the purposes of computing net income.

The process in which a business determines whether projects such as building a plant or investing in a long-term venture are worth pursuing is known as capital budgeting. Often, a prospective project's lifetime cash inflow and outflows are assessed in order to determine whether the returns generated meet a sufficient target benchmark. This process can also be known as investment appraisal.

Ideally, business should pursue all projects and opportunities that enhance shareholder value. However, because the amount of capital available at any given time for new projects is limited, management needs to use capital budgeting techniques to determine which projects will yield the most return over an applicable period of time. Quantitative methods used to evaluate projects for possible funding out of a capital budget include net present value (NPV) and internal rate of return (IRR).

4.0 CONCLUSION

Now that we have discussed the master budget, cash budget, sales budget, production budget and capital budget, you could see possible application of these types of budgets in your business endeavour or aid in your administrative functions wherever you are privileged to work.

5.0 SUMMARY

Having studied this unit, you should recall that a master budget is an overall financial operating plan for a forthcoming fiscal year. A cash budget consolidates all the cash inflows and outflows for the business.

A sales budget is a detailed scheduled showing the expected sales for the budget period. And the production budget lists the number of units that must be produced during each budget period to meet sales needs and to provide for the desired closing stock. Finally, a capital budget includes planned outlays for long-lived assets that are expected to generate income or support business operations over a number of years.

6.0 TUTOR-MARKED ASSIGNMENT

i. What is a master budget?
ii. What is a production budget?
iii. A company produces only one product which sells for ₦80 each. Total variable cost is ₦30. This is made up of material ₦15, labour ₦10 and overheads ₦5. Fixed costs are ₦15,000 per month payable one month in arrears. Sales in units are 2300, 2500 and 2600 for January, February and March respectively. Productions in units are 2400, 2600 and 2800 for January, February and March respectively. Labour costs are paid in the month they are incurred. Suppliers of materials give one-month credit. The variable overheads are paid for in the month following production. Sales are 60% for cash and 40% on one month credit. Opening balance at the beginning of January is ₦100,000. Prepare the cash budget for the month of January to March 2011.

7.0 REFERENCES/FURTHER READING

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UNIT 3 ZERO BASE BUDGETING

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
    3.1 The Concept of Zero Base Budgeting
    3.2 The Process of Zero Base Budgeting
    3.3 Performance and Zero Base Budgeting
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References//Further Reading

1.0 INTRODUCTION

One of the purposes of budgeting is to evaluate performance and motivate employees to direct their efforts towards organisational goals. It may be difficult to develop a budget that satisfies simultaneously the purpose of forecasting and motivating performance. This has given rise to various approaches to the budgeting process.

There are two approaches to the budgeting process which are Planning Programming Budgeting System (PPBS) and the Zero Based Budgeting (ZBB). For the purpose of this unit, we shall discuss the Zero Base Budgeting.

The ZBB approach was initially developed by a corporation in the United States, after which President Carter mandated its use for the 1979 Federal Budget.

2.0 OBJECTIVES

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

- explain the idea underlying zero based budgeting
- discuss the three major steps involved in the process of zero base budgeting
- discuss zero base budgeting vis-à-vis performance.

3.0 MAIN CONTENT

3.1 The Concept of Zero Base Budgeting

You will notice that in a normal budgeting process, the previous year's level of expenditure is often assumed to have been appropriate. Base on this, the task of individuals preparing the budget will be to decide what activities and funds should be removed and what activities and funds should be added. The problem this may create for the organisation is that there will be a bias towards continuing the same activities year after year even when the relevance of such activities have been lost due to changes in organisation's objectives or environmental changes, therefore, the need for zero-based budgeting which enables the organisation to evaluate its activities and priorities afresh. Similarly, previous year's resource allocations are not automatically considered as the basis of the present year's allocations. So, each manager has to justify anew his or her entire budget request. Hence, we can state that zero-based budgeting involves allocating an organisation's funds on the basis of a cost-benefit analysis of each of the organisation's major activities.

3.2 The Process of Zero Based Budgeting

The process of preparing a zero-based budget basically involves three major steps.

a. **Decision package -** The first step is to break down each of an organisation's activities into decision packages. A decision package includes all the information about an activity that managers need to evaluate that activity, and compare its costs and benefits with other activities. Such information might include the activity's purpose, costs and estimated benefits, plus the consequences expected if the activity is not approved and the alternative activities that are available to meet the same purpose.
b. **Prioritising -** The next step is to evaluate the various activities and place them in order of decreasing benefit to the organisation. The process starts by each manager ranking the activities for which he or she is responsible. These rankings are then passed on to a superior, who with the lower managers establish rankings for all the activities in his or her department. This process continues until rankings for all organisation activities are reviewed and selected by top managers.
c. **Allocation of resources -** When the final ranking has been determined, the organisation's resources are budgeted to meet the demand. Generally, funds for top priority activities would be

allocated more quickly while lower priority items would be scrutinised much more carefully.

SELF-ASSESSMENT EXERCISE

Define zero based budgeting.

3.3 Performance and Zero Based Budgeting

One of the purposes of budgeting is to evaluate the performance and motivate employees to direct their efforts towards organisational goals. This is achieved by allocating to employees the responsibility for achieving certain budget targets.

Optimal performance is likely to occur when a budget provides sufficient challenges. Budgets that are set to challenge may not always reach their target, so, they are not suitable in situations where accurate forecasting is the major concern. It may be difficult to develop a budget that satisfies simultaneously the purpose of forecasting and motivating performance.

In zero based budgeting, budget for virtually every activity in the organisation is initially set to zero. Zero base budgeting has been criticised as being too introspective. When managers focus on their own part of the business, they can overlook the interactions with other departments and the relevance of their operations to overall business objectives and strategies. For this reason, ZBB may not be very useful in helping business to manage costs or improve their performance. It has been claimed that ZBB does not help in identifying areas of waste, redundant activities, communication barriers or opportunities for more effective allocation of resources to support business demands.

4.0 CONCLUSION

Many organisations have attempted to measure discretionary costs through zero base budgeting. Many companies and government units have implemented ZBB at one time or the other. Under ZBB, the budget for virtually every activity in the organisation is initially set to zero. To receive funding during the budgeting process, each activity must be justified in terms of its continued usefulness.

The ZBB approach forces management to rethink each phase of an organisation's operations before allocating resources.

5.0 SUMMARY

You should recall that zero based budgeting involves allocating an organisation's funds on the basis of a cost-benefit analysis of each of the organisation's major activities. In other words, in zero based budgeting, budget for virtually every activity in the organisation is initially set to zero. The steps involved in the process of zero base budgeting are decision package, prioritising and resource allocation.

6.0 TUTOR-MARKED ASSIGNMENT

i. Explain the concept underlying zero base budgeting.
ii. Discuss the three steps involved in the process of zero base budgeting.

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MODULE 2 GOVERNMENT BUDGETING

Unit 1 Balanced Budget
Unit 2 Budgeting Process
Unit 3 Budget Process in Appropriation Bill (1)
Unit 4 Budget Process in Appropriation Bill (2)

UNIT 1 BALANCED BUDGET

CONTENTS

1.0 Introduction.
2.0 Objectives
3.0 Main content
    3.1 What is a Balance Budget?
    3.2 A Balanced Budget Amendment
    3.3 Problems Associated with Balanced Budget Rule
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Reading

1.0 INTRODUCTION

We defined in unit 1 that a budget is a formal statement of the financial resources set aside for carrying out specific activities in a given period of time. We did also discuss that a budget is the most widely used means for planning and controlling activities at every level of an organisation. Due to the fact that a budget is used for planning and controlling, when actual events or activities are seen, sometimes, there is a difference between what was budgeted for and what was actual event, which is known as variance. However, for the purpose of this unit, we shall be discussing a situation which does not express a variance situation such that budget and actual are the same.

2.0 OBJECTIVES

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

- explain the meaning of a balanced budget
- discuss a balanced budget amendment
- discuss problems associated with balanced budget rule.

3.0 MAIN CONTENT

3.1 What is a Balance Budget?

A balanced budget is when there is neither a budget deficit nor a budget surplus. This is when revenues equal expenditure. This is particularly associated with government account. More generally, it refers to when there is no deficit, but possibly a surplus.

A cyclically balanced budget is a budget that is not necessarily balanced year to year but is balanced over the economic cycle, running a surplus in boom years and running a deficit in lean years, with these offsetting over time.

Balanced budgets, and the associated topic of budget deficits, are a contentious point within politics, notably in American politics. The mainstream economic view is that having a balanced budget in every year is not desirable, with budget deficit in lean times being desirable. Within American politics, the situation is much more debated with all US States other than Vermont having a balanced budget amendment of some form; while conversely, the US Federal Government has generally run a deficit since the late 1960s and the topic of balanced budgets being a consistent topic of debate.

3.2 A Balanced Budget Amendment

A balanced budget is a constitutional rule requiring that the state cannot spend more than its income. It requires a balance between the projected receipts and expenditures of the government.

Most balanced budget provisions make an exception for times of war or national emergency or allow the legislature to suspend the rule by a super-majority vote. A supermajority or a qualified majority is a requirement for a proposal to gain a specified level or type of support which exceeds a simple majority (over 50%).

Balanced budget provisions have been added to the constitutions of most US States and Swiss constitution. After years of rising deficits and debt in the 1990s, Switzerland’s citizens adopted the debt brake as a constitutional amendment in 2001. The rule was implemented starting in 2003. It states that each year, the budget must be in balance, adjusted for economic conditions.

Every US State other than Vermont has some form of balance budget amendment. The precise form varies. State level balanced budget amendments have been strongly criticised as worsening the late 2000s recession by forcing States to cut services in the middle of a slump.

SELF-ASSESSMENT EXERCISE

Do you agree that all government budgets must be balanced?

3.3 Problems Associated with Balanced Budget Rule

Member countries of Europe feel obliged to introduce balanced budget clauses into their constitutions. The German government argues that balanced budget constitutional clauses are necessary to avoid future government debt crises. Paul De Grauwe argued that a balance budget rule is not a good idea. He stated that first the rule is based on defective diagnosis of the government debt crisis in Europe area. With the exception of Greece, the reason countries got into this crisis has little to do with the poor management of government finances. The root cause of the debt problems in Europe is the unsustainable debt accumulation in the private sectors of many countries in Europe. From 1999 until 2007, when the financial crisis erupted, private households in Europe increased their debt levels from about 50% of GDP (gross domestic product) to 70%. The explosion of bank debt in Europe was even more spectacular and exceeded 250% of GDP in 2007.

The second problem is that nobody wants to introduce a rule that says the government budget should be balanced every year. This is because such a rule would imply that when a recession sets in and the budget deficit automatically increases, the government would be forced to raise taxes and cut spending immediately.

The third problem with the balanced budget rule is that it is based on a cyclical view of what governments actually do. The rule implies that in the long run the debt to GDP ratio moves towards zero. The reason is that with balanced budget rule, the government cannot issue new debt (over the business cycle). Since GDP increases, the debt to GDP ratio must decline and ultimately go to zero.

4.0 CONCLUSION

Balanced budget rules take the cynical view that government debt is bad. This is also the view that governments are simply wasteful and do not contribute to the productivity of a nation. If one takes this view, then yes, a balance budget rule makes sense. Such a view however, is the expression of an economic fundamentalism that says that what governments do is bad, and what markets do is good.

5.0 SUMMARY

You should recall that a balanced budget is when there is neither a budget deficit nor a budget surplus. A balanced budget is a constitutional rule requiring that the State cannot spend more than its income. This gives a cynical view that all government debt is bad.

6.0 TUTOR-MARKED ASSIGNMENT

i. Explain the term balanced budget.
ii. A balance budget is a constitutional rule, discuss.
iii. Discuss the problems associated with balanced budget rule.

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UNIT 2 BUDGETING PROCESS

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
    3.1 How Budgets are Drawn and Approved
    3.2 The Role of Budget Personnel
    3.3 How Budgets are Revised
    3.4 Keys to a Successful Budgeting Process
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References/Further Reading

1.0 INTRODUCTION

The first step in influencing decision making is to understand the way budgets are drawn. A budget is a product of a process. How long the process should take and who should be involved in the process varies depending on the management style and complexity of the organisation. Establishing a schedule of key action and decision centre in the process allows adequate time for information to be collected and decision be made. Generally, the budgeting process should begin at least four months before the end of the fiscal year to ensure the budget is approved by the Board before the start of the New Year.

However, in this unit, we shall focus on four areas of discussion which are how budgets are drawn and approved; the role of budget personnel; how budgets are revised and keys to a successful budgeting process.

2.0 OBJECTIVES

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

- state the stages involved in the budgeting process
- discuss the role of budget personnel in budgeting process
- state briefly how budgets are revised
- state briefly the keys to a successful budgeting process.

3.0 MAIN CONTENT

3.1 How Budgets are Drawn and Approved

In this sub-unit, let us look at the various stages involved in the budgeting process.

a. **Planning the Process**
In this first step, we should be interested in identifying who will coordinate the budgeting process and which staff, board members and committees needed to be involved. We shall further agree upon key definitions, assumptions and document format and set timeliness and key deadlines required to complete the process. In this stage, we can determine and schedule any training or key meetings that would enhance the budgeting process.

b. **Communicating about the Process**
In this stage, we should communicate responsibilities, expectations and deadlines to everyone involved. It would also be required to explain and distribute forms and assumptions.

c. **Goal Setting**
At this stage, we have to determine programme goals and objectives, estimate staffing requirements and salary and benefit assumptions based on programme goals and assumptions.

d. **Collection of Information**
At this stage, we shall research and gather information about incomes and expenses based on programme goals and assumptions. Similarly, construct budget details by programme while communicating regularly information collected to avoid duplication of effort among the budget personnel.

e. **Compilation and Revision**
This stage requires us to appoint one person to compile all information, review it for consistency and redistribute to everyone involved. It is important that there is enough time for review and revision.

f. **Committee Review**
At this stage, the budget draft and key assumptions are reviewed by the finance committee and other appropriate staff and board committee. Be sure to allow enough time between committee meetings and the final approval deadline to address questions and recommendations and make revisions.

g. **Approval**
At this stage, the budget proposal is presented to the board for final approval by the finance committee or treasurer. It is important to note that information about the budget draft,

programme goals and other supporting information should be distributed to the board prior to the board's meeting.

3.2 The Role of Budget Personnel

It is important you note that developing budgets is primarily the function of line managers. However, personnel from a planning group or budget department may provide information and technical assistance but the main duty for budgets resides with the line personnel. Many organisations have formal budget departments and committees. These groups are likely to exist in large segmented organisations in which the division budget plays a key role in planning, coordinating, and controlling activities.

The budget department provides budget information and assistance to organisational units, designs budget systems and forms, integrates the various departmental proposals into a master budget for the organisation as a whole and reports on actual performance relative to the budget.

The budget committee which is made up of senior executives from all functional areas, reviews the individual budgets, reconciles divergent views, alters or approves the budget proposals and then refers the integrated package to the board of directors. Later, when the plans have been put into practice, the committee reviews the control reports that monitor progress. In most cases, the budget committee must approve any revisions made during the budget period.

3.3 How Budgets are Revised

You would agree with the fact that no manager can be allowed to revise a budget whenever he or she likes; otherwise, the entire review and approval process would be a mockery. However, due to the fact that budgets are based on forecasts, which could easily go wrong, some provision must be made for necessary revisions.

In circumstances where the budget is used basically as a planning instrument, formal updating periods may be established at stated intervals. Where the budget is a main part of the control and evaluation mechanism, revisions are limited to circumstances where deviations have become so great as to make the approved budget unrealistic. The aim is to build reasonable stability and firmness into the budget without being excessively rigid.

Comparisons of actual performance with budgets are known as reviews or audits. To be effective, audits depend on a regular, accurate flow of data from organisational units. Unit managers will regularly submit monthly or weekly progress reports, unless a problem requires immediate attention. Usually, these reports are audited on monthly basis by those individuals with control responsibility. If deviations are detected, the appropriate managers will be asked to explain them and to specify the corrective action they plan to take.

SELF-ASSESSMENT EXERCISE

List and discuss the stages involved in a budgeting process.

3.4 Keys to a Successful Budgeting Process

Let us briefly state some points that would enhance a successful budgeting process.

- You should clearly identify programme objectives that are aligned with the mission and strategic plan of the organisation.
- You should determine the financial resources needed and available to achieve programme goals.
- You should involve staff and board members in the process to improve accuracy of information and commitment to the plan.
- Document- it is good not to rely on memory. It is important to write down assumptions and formulas. This is very crucial in managing the budget throughout the year.
- Each organisation should customise its process. The steps each organisation takes would be somewhat different.

4.0 CONCLUSION

Once a budget is approved, it becomes imperative to ensure proper implementation and management. Therefore, staff should be communicated on the budget, programme goals and timeliness for the next year. There should be review of actual income and expenses compared to the budget on a monthly basis. Similarly, update and revision of the budget as there are changes during the year should apply depending on the significance of changes. The board of directors may need to approve revisions.

5.0 SUMMARY

You should recall that a budget is a product of a process. The budgeting process involves various steps before a budget is produced. Different personnel play their roles in the budgeting process but primarily, the function of developing the budgets is that of the line managers. You should also recall that comparing actual performance with budgets is known as review or audit.

6.0 TUTOR-MARKED ASSIGNMENT

i. State and explain the various stages involved in the budgeting process before a budget proposal is approved.
ii. What are the steps to take to ensure a successful budgeting process?

7.0 REFERENCES/FURTHER READING

Morse, D. C. & Zimmerman, J. L. (1997). *Management Accounting*. USA: Irwin/McGraw Hill.

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UNIT 3 BUDGET PROCESS IN APPROPRIATION BILL(1)

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
 3.1 The Presentation of Proposal
 3.2 The Draft Estimates
 3.3 The Appropriation Bill and Legislative Approval
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References//Further Reading

1.0 INTRODUCTION

In this unit, we shall discuss the budgeting process as it applies to government budget.

The federal budget and appropriations process take place each year and can have a significant impact on the funding of education, health and other critical issues of a nation. In order to be the most effective advocate possible, it is a good idea to familiarise with this budget process.

Consequently, we shall focus our attention on the budget process as it applies to the Nigeria government. We shall consider the presentation of proposals, the draft estimates, the appropriation bill and legislative approval.

2.0 OBJECTIVES

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

- discuss the process involved in getting proposal from government departments
- explain how draft estimates are developed
- discuss how budgets are approved in government budgeting process.

3.0 MAIN CONTENT

3.1 The Presentation of Proposal

The planning of government expenditure is essentially the duty of the Minister of Budgeting and Planning/Finance. When the returns of revenue from the ministries reveal to the Ministry of Finance that there will be a substantial increase in revenue for the next financial year, it is normal for the Ministry of Finance to allow the departments some reasonable expansion to make an intelligent forecast of what their additional needs and requirements will be during the following year.

These needs of the departments are expressed in estimates in terms of staff, equipment, buildings and materials, which the departments require in order to carry out their services to the public. Where ministries are allowed to submit their proposals, they will be summoned to appear before the Estimate Committee to justify their proposals. After a detailed examination of their proposals, the approving ministries (the Office of the Head of Service in the case of proposal for increase in staff; and Ministry of Finance in the case of proposal for equipment, materials, building and the running cost of the ministries) will communicate to the respective ministries the list of approved items of their proposals so that the ministries may then prepare their draft estimates.

3.2 The Draft Estimates

The departments submit their draft estimates to the Ministry of Finance who in turn go through them carefully to see that nothing is added which was not previously approved. The budget department has to arrange meetings with departments to clear areas of doubt, that is, circulars inviting ministries departments to schedule meetings with the budget department which is normally issued around November/December and each head and items of the recurrent budget are considered.

When satisfied with the draft estimates, the Ministry of Finance presents them to the budget division in the office of the President who would examine the estimates to see whether they conform to the government policy.

Items of capital expenditure, which the budget committee selects from the National Development Plan, for inclusion in the annual estimates will be embodied in the draft estimates. The draft estimates are then sent for printing. The estimates of each ministry forms a ‘head’ of the printed draft, and after printing, they are returned to the Ministry of Finance for its presentation to the House of Assembly by the President.

3.3 The Appropriation of Bill and Legislative Approval

When the budget has been approved, the President presents it to the National Assembly at a joint session. The House is summoned to consider among other things, the draft estimate of the government. This meeting of the House is generally referred to as the 'Budget Session' and the principal business is the introduction of the draft estimate of the House in the form of an 'Appropriation Bill'.

There are two Houses which are the Representatives and the Senate. In each of these, there are committees more or less coinciding with the ministries. If each of the Houses agrees with the budget, the budget is approved by each House. However, where there are areas requiring reconciliation by the two Houses, the Finance Committee is constituted to thrash out areas of disagreement and report made to each House, which then approve the Appropriation Bill. Thereafter, the President signs the budget approved by the National Assembly and the Appropriation Bill becomes Appropriation Act to enable Ministries, Departments and Agencies to spend.

SELF-ASSESSMENT EXERCISE

Explain how draft budget estimates are prepared.

4.0 CONCLUSION

When the President signs the budget that has been approved by the National Assembly, it becomes an Appropriation Act or Law which empowers ministries to expend resources as stated in the budget. However, if the approval of the National Assembly is not gotten as at 1st January, the President can authorise the release of funds in accordance with section 76 of the Constitution.

5.0 SUMMARY

You should recall that draft estimates are forwarded from the various ministries to the Ministry of Finance which has the duty of planning government expenditure. When the draft estimates are approved, they are forwarded to the National House of Assembly by the President. When it is approved by House and signed by the President, it becomes an Appropriation Act to empower the ministries, departments and agencies to spend according to the approved budget.

6.0 TUTOR-MARKED ASSIGNMENT

Describe the process of approval of draft estimates.

7.0 REFERENCES/FURTHER READING

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UNIT 4 BUDGET PROCESS IN APPROPRIATION BILL(2)

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
  3.1 Method of Preparing Budgets by the various Tiers of Government in Nigeria
  3.2 Advantages and Disadvantages of the Incremental Budgeting Method
  3.3 Factors Affecting Good Budgeting System in the Public Sector
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References//Further Reading

1.0 INTRODUCTION

In this unit, we shall discuss issues relating to government budget process that was not discussed in the previous unit. This is to enable you have a wider view on issues relating to government budget process.

Therefore, we shall discuss the methods of preparing budgets by the various tiers of government in Nigeria and see the merits and demerits of this method. It would also be useful to look at certain factors which militate against the budgeting system in public sector.

2.0 OBJECTIVES

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

- discuss the method of preparing budgets adopted by the various tiers of government in Nigeria
- state the advantages and disadvantages of the incremental budgeting method
- describe the factors affecting the budgeting system in the public sector.

3.0 MAIN CONTENT

3.1 Method of Preparing Budgets by the various Tiers of Government in Nigeria

The budgeting method adopted by the Nigeria Government to allocate funds for a succeeding year is the “incremental method”. The approach is itemising proposed disbursements under different heads and sub-heads of the various ministries and extra-ministerial departments. The expenditure side of the incremental budget is made up of personal emoluments, other charges and capital or developmental items.

This involves picking of last year’s figures and adding a percentage to arrive at this current budget. The percentage added is based essentially on three factors, which are trend of economic event, inflation and the available fund.

Budgeting in government can be appreciated as being made up of two main elements. The first aspect is the procedure of budgeting. This consists of the practices, documentations and norms which govern the preparation, approval, implementation and review of the budget. The second element is the ‘budgeting system’. This has to do with the management process. This provides for the purchase, allocation and use of available resources by setting in advance operational criteria which result in the achievement of corporate goals.

3.2 Advantages and Disadvantages of the Incremental Budgeting Method

Advantages

1. It is simple to operate and understand.
2. It suits the country’s level of development where there is paucity of data.
3. It is cheaper to produce.
4. It encourages the continuity of projects.
5. Allocations into heads and subheads facilitate the monitoring of performance.

Disadvantages

1. The method allows past errors to be carried forward.
2. Detailed scrutiny is not contained in the budget.
3. It fails to clarify the cost of alternative methods of achieving programmed objectives.

4. It fails to fund new programmes of high priority.
5. The method does not clearly spell out the relationship between capital and recurrent expenditures.

SELF-ASSESSMENT EXERCISE

What is the budgeting method adopted by the Nigerian government?

3.3 Factors Affecting Budget Implementation

Let us consider some factors which affect the implementation of budget in the public sector.

1. **The human factor**: Top management members see budgeting as restraining and challenging. They tend to develop a lot of apathy towards its adoption and implementation. The lack of probity and accountability of some operatives affect successful budgeting.
2. **Incorrect data**: There are a lot of uncertainties in the data used for the budget preparation. The projections in revenue accruing from oil may not be forthcoming in view of the vagaries in the world market.
3. **The type of project for which budget is prepared**: How successful a budget will be depends on the type of project to which it relates. Some projects are popular while others are not. Those which are not popular may face stiff implementation problem.
4. **Inflation**: Inflation tends to reduce purchasing power of money. When the value of money is falling, budget implementation may run into problems. The revenue available will not be able to cover the expenditure.
5. **Political, social and cultural elements**: Each segment of the nation has its own cultural beliefs and taboos which may take time to change. Introducing innovation may be met with stiff opposition.
6. **Changing government policies**: To implement a budget, a lot depends on the policy of government. For effective budget implementation, government policies have to be harmonised and consistent. Frequent changes of government policies affect budget implementation.
7. **The problem of debt management and optimal use of limited resources**: There is the challenge of striking a balance between what part of the nation's resources should be used for servicing debts and the amount that should be utilised for economic development.
8. **Fiscal indiscipline**: Most spending officers under the incremental budgeting system, tend to expend the last naira available in a

year's budget in order to justify the demand for increased allocation in the subsequent year, with little or nothing to show under the current dispensation.

4.0 CONCLUSION

The budget process is a cycle of events which occur sequentially every year and which results in the approved budget.

5.0 SUMMARY

You should recall that in this unit we discussed the incremental budgeting system which is normally adopted by the three tiers of government. We also stated the advantages and disadvantages of the incremental budgeting system. Conclusively, we considered various factors that affect the implementation of budget.

6.0 TUTOR-MARKED ASSIGNMENT

i. Mention and discuss the method of preparing budgets in Nigeria used by the three tiers of government.
ii. Is there any disadvantage using incremental budgeting system? If any, state them.

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MODULE 3 BUDGETING AND CONTROL

Unit 1 Budgetary Control
Unit 2 The Accountant-General of the Federation
Unit 3 The Auditor-General for the Federation
Unit 4 Expenditure Control

UNIT 1 BUDGETARY CONTROL

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1.0 INTRODUCTION

Budgetary control is the whole system of controls that ensure incomes and expenditures are in line with the budgets and that wastage is reduced to the barest minimum. Budgetary control is a positive and integral part of a public sector organisation planning and appraisal activities so as to achieve the set objectives.

Budgetary control can be defined as the establishment of budget, relating the responsibility of executive to the requirement of a policy and the continuous comparison of actual with budgeted results, either to secure by individual action the objective of that policy, or to provide a basis for its revision. Budgetary control and standard costing are the most powerful control technique at the disposal of the cost and management accountant.

2.0 OBJECTIVES

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

- state the objectives of budgetary control
- state the fundamental differences between budgetary control and standard costing
- state the pre-requisite for budgetary control technique.

3.0 MAIN CONTENT

3.1 Objectives of Budgetary Control

The objectives of budgetary control may be summarised as follows:

a. To combine the ideas of all levels of management in the preparation of budgets.
b. To coordinate all the activities of an organisation.
c. To centralise control.
d. To decentralise responsibility to each manager.
e. To act as a guide for management decision when an unexpected conditions affect the budgets.
f. To plan and control incomes and expenditures so that maximum benefit is achieved.
g. To channel capital expenditures in the most profitable manner.
h. To ensure that sufficient working capital or cash is available for efficient operation of the organisation.
i. To provide a basis against which actual results can be compared.
j. To show management where actions is needed to remedy a situation.

3.2 Organisation for Budgetary Control

These include:

a. **The Preparation of Organisation Chart**: This defines the functional responsibilities of each member of management and ensures that everyone knows his position in the organisation and his relationship to other members.
b. **The Budget Period –** This is the time to which the plan of action relates. Period budgets cover a fixed period of time, most commonly one year. They will be divided into shorter time periods, known as control periods, for purpose of reporting control. With a one year period budget, control periods may be four weeks (13 periods each year) or one month (12 periods each year). Long-term budgets (for example, capital expenditure

budgets) may be for periods of up to five or ten years, or even longer.

c. **Budget Manual**: The organisation for budgeting (and budgetary control) should be documented in a budget manual, which has been described as a "procedure or rule book which sets out standing instructions governing the responsibilities of persons, and the procedures, forms and records relating to the preparation and use of budgets" (CIMA).

Even though organisations are different, the content of a manual are:

1. Description of budgetary planning and control.
2. Goals of each level of the budgetary process.
3. Association with long term planning.
4. Nature of organogram depicting duties and level of budget officers.
5. Analysis of relevant budgets and association with accounting activities.
6. Description of principal budgets.
7. Composition of budget committee and mode of operation.
8. Modalities for the preparation and publication of budget.
9. Designation and responsibility of the budget manager.
10. Chart for codes.
11. Design and nature of form; and
12. Mode of operation especially where they concern procedures for accounting preparation of reports and dead line for the submission of such reports/budgets.

d. **Budget Committee**: The overall responsibility for budget preparation and administration should be given to a budget committee, normally chaired by the chief executive of the organisation, with departmental heads or senior managers as members. The purpose of the committee is to:

1. Ensure the active cooperation of departmental managers, and to act as a forum in which differences of opinion can be argued out and reconciled.
2. Ensure that managers in the organisation understand what other departments are trying to do.
3. Establish long-term plans around which the budgets should be built, then to identify budget objectives.
4. Review departmental budgets.
5. During the year, examine reports showing actual performance compared with budget and expectations.

e. **The Budget Officer**: The budget officer controls the budget administration on a day to day basis. He will be responsible to the budget committee and should ensure that its decisions are transmitted to the appropriate people and relevant data and opinion are presented for its consideration. The budget officer will normally have the vital job of educating and selling the budget idea. Since the master budget is summarised in cost statements and financial reports, the budget officer is usually an accountant.

f. **The Introduction of Adequate Accounting and Records**. It is imperative that the accounting system should be able to record and analyse the information required. A chart of accounts should be maintained which corresponds with the budget centre.

The general instruction on techniques to all concerned in operating system: Each person must feel that he is capable of carrying out the budgeted programme.

g. **Budget Centre**: An organisation's planned activities are divided into separate areas known as budget centre or cost centre. Each area selected as a budget centre must be clearly definable, and should be the natural responsibility of one particular manager (or supervisor). A separate budget is prepared for each as departmental budgets. Departmental budgets are often used to build up budgets for overhead costs, that is:

1. The production overhead budget will be compiled from separate budgets for the production departments, maintenance, production planning, quality control, and so on.
2. The administrative budget will be compiled from separate budgets for personnel, finance, management services, data processing, and so on.
3. The selling and distribution budget will be the amalgamation of budgets prepared by sales office managers, marketing managers, warehouse and transport managers.
4. The research and development budget.

h. **Principal Budget Factor**: This is also known as the key budgeting factor or limiting budget factor. This first task in budgeting is to identify the factors which impose limitation or ceilings on the level of activity. It is usually sales demand; but it may also be limitations on any resources, labour, machine, time, working capital, etc. Once this factor is defined, the rest of the budget can be prepared. It determines priorities functional budgets, for example, it may be material, labour or plant. Management may not know in advance the principal budget factor. One method to identify this factor is to prepare a draft sales budget, and then consider whether any resource shortage prevents this level of sales budget, and then being met.

i. **Level of Activity**: It will be necessary to establish the normal level of activity, that is, the level the company can reasonably be expected to achieve: quantity to produce, quantity to be sold and so on.

SELF-ASSESSMENT EXERCISE

What are the objectives of budgetary control in Government?

3.3 Fundamental Differences between Budgetary Control and Standard Costing

Although, the two techniques involve setting of targets, accumulation of costs as it becomes historic and has a feedback mechanism, let us see the fundamental differences between budgetary control and standard costing as follows:

a. Budgetary control is used in relation to major cost classification or different cost centre whereas standard costing is set in relation to element of cost or specific operation of an undertaking.
b. Standard costing is desirable when products are fairly divided into sections.
c. Standard costing could be integrated into the double entry system whereas budgetary control report is a mere memorandum record.
d. The target under budgetary control is invariably changed year in year out whereas target under standard costing are seldom change unless situation change drastically.
e. The cost allowance under standard costing technique is based on the actual level of activities attained whereas the budgeted cost allowance under budgetary control is invariably fixed.
f. Standard cost is a unit cost concept whereas budgeted cost is a total cost concept.

3.4 Pre-Requisite for Budgetary Control Technique

a. Decision of corporate objective must be well defined.
b. The support of top management must be obtained and indicate other line and staff management.
c. Preparation of an accurate and up to date organisation chart.
d. Preparation of a budget manual.
e. Design of a comprehensive code of account at cost centre with name of the individual responsible for each cost centre.
f. Formulation of the budget committee and the appointment of the budget officer.

Behavioural Aspects of Budgeting

Despite all the benefits/objectives already narrated on the budgetary control system and the management accounting control techniques, the operations of budgetary control techniques have met with little success. Many scholars have done research on these, in order to detect what should have been responsible for the failure. Such researchers are Hopwood (1974), Argris (1952), Horngreen (1960) and a host of others.

The main causes of the level of low success in practice have been attributed to lack of cooperation and negative attitude of the operating managers to the control techniques. Managers' personal objectives also override the goal congruence of the organisation. This negative and dysfunctional attitude of managers manifest at both the planning stage and implementation stage.

Planning Stage: Assuming the operating managers are involved in preparing a budget; they may:

a. Intentionally build in slack in the budget.
b. Express the opinion that budget is time wasting and that they are always busy to operate the budget.
c. Argue that formalising a budget on paper is too restrictive and that they should be granted some flexibility in making their operational decisions.
d. Always prefer incremental system of budgeting to considering alternative option and new ideas.
e. Have in mind that the budget is unattainable, that is, having negative idea about the achievement of the budget.

Implementation Stage

a. Lack of co-operation and co-ordination with other budget centre.
b. Putting in less effort to achieve budget targets without putting all efforts to achieve more than budgeted.
c. Managers may disregard control reports which show negative variances.
d. Having much interest in short-term factors to the detriment of more important longer term consequences.
e. Lack of controlling cost to achieve their selfish end.
f. Blaming budgeting systems for any problem which may occur.

SELF-ASSESSMENT EXERCISE

Distinguish between budgeting control and standard costing

3.6 Solving Behavioural Problems in Budgeting

Let us discuss some factors that help in solving behavioural problems in budgeting.

a. Motivation

Horngreen (1996) defined motivation as the "need, some selected goal and the resulting drive that influence action towards the goal". He suggested that motivation has two aspects:

1. Direction or goal congruence exists when managers working in their own best interest also are in harmony with the goals of top management (that is, the organisation as a whole). It is very difficult to obtain the goal congruence in an organisation. This is one of the essentially behavioural problems in budgeting.

   Strength with getting subordinates to run rather than work towards the desired goal. Incentive improves the performance of employee and helps to reduce personal or departmental objectives.
2. Motivation helps to improve business results and eliminate misdirected or dysfunctional operation. Horngreen argues that accounting system must be designed in such a way as to achieve a motivational response from its use, provided that the costs of providing such a system do not outweigh the expected results. He also acknowledges that human behaviour is inclined to damage the usefulness of formal accounting system.

b. **Participation**

Participation by employees in budget setting and the encouragement of a human approach, and man-management would remove the drawbacks to effective budgeting. All the operators of the budget should be fully involved in the preparation of the budget. Participation leads to more positive attitude and higher performance. Kenis (1979) reported a positive correlation of attitude and performance with participation, while other scholars such as Bryan and Locke, Stedry and others showed a negative relationship between participation and performances. Argris (1952) on the other hand cautioned against the level of participation, as different organisations use the word participation to describe quite different activities. He suggested that the involvement of managers should be total; otherwise pseudo-participation could lead to counter-productive results.

c. **Goal Congruence**

Goal congruence means the overall objective of an organisation. This overall objective should not conflict with the individual or group objectives entirely but recognition must be given to the fact that organisational objectives cannot be set and implemented through budgeting without consideration of the interaction of individual group and departmental objectives.

Hopwood (1976) emphasised that there are many problems in achieving goal congruence because:

- There may be numerous objectives in one organisation, some of which may conflict.
- Different managers may perceive their objectives differently.
- Departmental rivalries.
- Different and conflicting reward structures.
- Other practical realities make perfect goal congruence extremely unlikely. Efforts should be made to educate both top management and middle management on the importance of goal congruence.

d. **Management Support**

Top management should be interested in the budgetary system in order to ensure that operating managers give the necessary cooperation.

e. **Reporting System**

Efforts should be made to isolate uncontrollable cost from controllable ones in order to have meaningful variances reporting system.

f. **Communication**

Communication should be adequate with the operating managers at all stages of budgetary system.

4.0 CONCLUSION

A control technique whereby actual results are compared with budgets is budgetary control. Any differences or variances are made the responsibility of key individuals who can either exercise control action or revise the original budgets, this enables mangers to monitor organisational functions.

5.0 SUMMARY

In this unit, you should recall we discussed the objectives of budgetary control and stated the fundamental difference between budgetary control and standard costing. In addition, we discussed those conditions that must be present in order for there to be a successful application of the budgetary control technique. In addition, we discussed the behavioural aspects of budgeting and considered the factors in solving behavioural problems in budgeting.

6.0 TUTOR-MARKED ASSIGNMENT

i. State five objectives of budgetary control
ii. State five fundamental differences between budgetary control and standard costing
iii. What are the pre-requisite for setting budgetary control technique?

7.0 REFERENCES/FURTHER READING

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UNIT 2 THE ACCOUNTANT-GENERAL OF THE FEDERATION

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
    3.1 Purpose of Government Accounting
    3.2 Powers of the Accountant-General of the Federation
    3.3 Functions of the Accountant-General of the Federation
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7.0 References/Further Reading

1.0 INTRODUCTION

In this unit, we shall discuss some issues that relates to the Accountant General of the Federation; such as the purpose of government accounting, the power and the functions of the Accountant-General.

Public sector accounting could be defined as a process of recording, communicating, and summarising, analysing and interpreting government financial statement reflecting all levels of transaction involving the receipt, custody and disbursement of government funds. Obviously, this definition reflects the definition of financial accounting. It therefore follows that public sector accounting is essentially financial accounting.

2.0 OBJECTIVES

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

- state the purpose of government accounting
- state the powers of the Accountant-General of the Federation
- state the functions of the Accountant-General of the Federation.

3.0 MAIN CONTENT

3.1 Purpose of Government Accounting

The following are some of the main purposes of government accounting.

1. To ascertain the propriety of transactions and their conformity with established rules.
2. To give evidence of financial accountability.
3. To serve as a basis for planning.
4. To serve as a basis for controlling.
5. To serve as a basis for decision making.
6. To serve as a basis for appraisal of the performance of management.
7. To depicts sources of government revenue and the resultant expenditure.
8. To ascertain how capital expenditure will be financed.
9. To ascertain the economy and efficiency with which the government carried out its functions and or pursued its objectives.
10. To determine the cost-effectiveness with which planned objectives were achieved.
11. To ascertain details of financial commitments and the full cost of providing various services.
12. To ascertain key services indicators and comparison with targets.

3.2 Powers of the Accountant-General of the Federation

In accordance with Financial Regulations 103, the Accountant-General of the Federation has the following powers:

- Power of access to books and records of every ministry and extra-ministerial departments at any reasonable time.
- Power of request for information and explanation necessary for his duties.
- Power to carry out special investigation in any ministry and extra-ministerial departments.
- Power to carry out ad hoc investigation in any ministry or extra-ministerial departments.

SELF-ASSESSMENT EXERCISE

What do you understand by Public Sector Accounting?

3.3 Functions of the Accountant-General of the Federation

The functions of the Accountant-General of the Federation as contained in financial regulation include:

- Supervising the accounts of the Federal Government ministries and extra-ministerial departments.
- Collating, presenting and publishing the statutory financial statements of the Federal Government.
- Managing the Federal Government's investments through the Ministry of Finance Incorporated (MOFI).
- Maintaining and operating the Federation account.
- Establishing and supervising the Federal Pay Offices in each state of the Federation.
- Conducting routine and in-depth inspection of the books of accounts of the federal ministries and extra-ministerial departments to ensure compliance with the rules, regulations, policies, decisions and maintenance of accounting codes and Internal Audit Guides.
- Ensuring revenue monitoring and accounting.
- Formulating the accounting policies of the Federal Government.

SELF-ASSESSMENT EXERCISE

List the powers of the Accountant-General of the Federation.

4.0 CONCLUSION

In accordance with Financial Regulations 101, the Accountant-General of the Federation is the chief accounting officer of the receipts and payments of the Federal Government. He is saddled with the responsibility of general supervision of the accounts of all ministries and extra-ministerial departments, and the preparation of annual financial statements of the country as may be required by the honourable Minister of Finance.

5.0 SUMMARY

In this unit, we discussed some of the purpose of government accounting and state the powers and functions of the Accountant-General of the Federation.

6.0 TUTOR-MARKED ASSIGNMENT

What are the functions of the Accountant-General of the Federation?

7.0 REFERENCES/FURTHER READING

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UNIT 3 THE AUDITOR-GENERAL FOR THE FEDERATION

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
 3.1 Areas of Opinion of the Auditor-General for the Federation
 3.2 Powers of the Auditor-General for the Federation
 3.3 Indirect Accounting Functions performed by the Auditor-General for the Federation
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7.0 References//Further Reading

1.0 INTRODUCTION

In the previous unit, we discussed some issues as they relate with the Accountant-General of the Federation. Similarly, in this unit, we shall discuss some issues as they relate to the Auditor-General for the Federation. We shall discuss the constitutional requirement of the Auditor-General to give his opinion on the accounts prepare for the government, the powers conferred on the Auditor-General to do his job and the indirect accounting functions performed by the Auditor-General.

2.0 OBJECTIVES

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

- state areas the Auditor-General is expected to give his opinion
- state the powers of the Auditor-General for the Federation
- state some indirect accounting functions performed by the Auditor-General.

3.0 MAIN CONTENT

3.1 Areas of Opinion of the Auditor-General for the Federation

At the end of an audit, the Auditor-General is expected to write a report stating whether in his opinion:

a. The accounts have been properly kept.
b. All public monies have been fully accounted for, and the rules and procedures applied are sufficient to secure effective check on the assessment, collection and proper allocation of revenues.
c. Monies have been expended for the purposes for which they were appropriated and the expenditures have been made as authorised.
d. Essential records are maintained, and the rules and procedures applied are sufficient to safeguard public property and funds.

3.2 Powers of the Auditor-General of the Federation

In accordance with Financial Regulation 103, the Auditor-General for the Federation has the following powers:

a. Power of access to books and records of all ministries and extra-ministerial departments at reasonable times.
b. Power to request for information and explanation necessary for his duties.
c. Power to carry out special investigation in any ministry and extra-ministerial departments.
d. Power to carry out ad hoc investigation in any ministry or extra-ministerial department.

3.3 Indirect Accounting Functions Performed by the Auditor- General for the Federation

While performing the statutory auditing function, the Auditor-General performs some indirect accounting functions. The accounting duties include:

a. Seeing that proper system of accounts as prescribed by the Minister of Finance is maintained.
b. Exercise supervision over the receipt of public revenue and ensure its punctual collection.
c. Ensure that there are adequate securities over the custody of public money.
d. Ensure that there are adequate safeguards against the occurrence of fraud, embezzlement and carelessness.

e. Exercise supervision over all officers under his authority entrusted with the receipt, custody and disbursement of public funds.
f. Ensure that money is expended for the purpose for which they are meant for.
g. Ensure that all books are correctly posted up to date.
h. Ensure that authorised maximum cash balanced to be held are not exceeded.
i. Report any defect in the procedure for collecting revenue, which come to his notice during the course of his audit.

4.0 CONCLUSION

In accordance with the provisions of Financial Regulation 102, the Auditor-General is the Officer responsible under the constitution of the federation for audit and reports on the public accounts of the federation, including all persons and bodies established by law entrusted with the receipts, custody, issue, sale, transfer or delivery of any stamps, securities, stores or other property of the government of the federation and for the certification of annual accounts of the nation. He is given free hand to examine the accounts in such a manner as he may consider proper.

5.0 SUMMARY

In this unit, we discussed those areas the Auditor-General is expected by the constitution to give his opinion as regards the state of affair of such areas of accounting activities. In addition, we discussed the powers of the Auditor-General for the federation as provided by the Financial Regulation 103 and the indirect accounting functions performed by him while performing his statutory auditing function.

6.0 TUTOR-MARKED ASSIGNMENT

i. What are the areas the Auditor-General for the Federation is expected to give his opinion?
ii. What are the powers of the Auditor-General for the Federation?
iii. State five indirect accounting functions performed by the Auditor-General.

7.0 REFERENCES/FURTHER READING

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UNIT 4 EXPENDITURE CONTROL

CONTENTS

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    3.2 The Legislative Control
    3.3 The Ministry of Finance Control
    3.4 The Treasury Control
    3.5 The Departmental Control
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5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References//Further Reading

1.0 INTRODUCTION

Expenditure control could be defined as the strings of coordinating actions which have to be taken to ensure that all expenditures are 'wholly', necessarily, 'reasonably' and 'exclusively' incurred for the purpose for which they are meant.

One may wonder, why should we apply any control on government expenditure? After all, the money belongs to all of us and should be spent the way anyone chooses. That would only lead to wastage and mismanagement.

In government therefore, if no proper control is exercised from time to time, right from when the estimates is prepared to the time of spending, the government budget may inevitably end up in a deficit. Obviously, lack of control would lead to embezzlement and other vices by government officials.

2.0 OBJECTIVES

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

- describe the executive control over budgeted expenditure
- discuss the legislative control over budgeted expenditure
- discuss the control over budgeted expenditure exercised by the Ministry of Finance
- discuss the treasury control over budgeted expenditure
- discuss the departmental control over budgeted expenditure.

3.0 MAIN CONTENT

3.1 The Executive Control

The executive comprises the president and his cabinet members who have the responsibility for the efficient and effective control of the administration of the country, politically and economically. In order to ensure check and balances, the constitution created the legislative and judiciary arms of government. All measures and policies taken by the president are subject to the approval of the legislature within the orbit of the constitution.

In accordance with Section 75(1) of the constitution, "the President shall cause to be prepared and laid before each House of the National Assembly at any time in each financial year, estimates of revenue and expenditure of the federation for the following financial year."

The president, in order to satisfy the provisions of the constitution also appoints a cabinet committee on estimates, to advise him on the contemplated policy measures. The policy measures contemplated are then transmitted to the Budget Department in the Presidency. This development in turn leads to the issuance of guidelines on all the agencies involved in budget operation. Any unit of the government whose requirements are higher than the 'control figures' already issued, is invited to defend the excess request.

SELF-ASSEEMENT EXERCISE

List the basic controls over government expenditure in your country.

3.2 The Legislative Control

The National Assembly is the supreme authority on matters of the nation's finance. The legislature considers and approves the estimates submitted to her by the president. Furthermore, control is exercised when transaction is reviewed after payment. No amount of public fund may be spent without the approval of the National Assembly. However, Section 82 of the 1999 Constitution empowers the president to spend from the consolidated revenue fund to carry on administration of government of the federation for not more than 6 months or until the coming into operation of the Appropriation Act, whichever is earlier.

Much has been discussed about the Auditor-General in the previous sub-unit, however, it is important to note that in order to ensure that ministries make proper use of public funds voted for them, the appointment of the Auditor-General for the Federation must be ratified by the legislature. The Auditor-General scrutinizes all accounts and records of the money collected and spent and reports to the National Assembly appropriately on the instances of waste, extravagance, inefficiency or fraud. It is observed that the Auditor-General's duty is post-payment audit, except in the matters relating to pension and gratuity payments on which he performs pre-payment audit. This is in addition to the regularity and compliance audit that he carries out as a duty.

Again, the legislative organ performing post-mortem functions is the Public Accounts Committee of each House of the National Assembly. The purpose of the committee is to expose waste, corruption or inefficiency in the handling of public funds or projects. It is empowered to examine such audited accounts of the federation and all public offices and the Auditor-General's report thereon.

SELF-ASSESSMENT EXERCISE

Discuss the legislative control over budgeted expenditure.

3.3 The Ministry of Finance Control

When ministries/departments require money to pay for services, they normally apply to the minister of finance for such funds. The tradition is that once a year the ministries and extra-ministerial departments present estimates to cover their needs and requirements which are expected to be prudent, necessary and reasonable, in accordance with the Financial Regulations and Appropriation Act. The minister passes the consolidated revenue and expenditure estimates to the president who will present them to the Federal Executive Council for approval before they are forwarded to the National Assembly as Appropriation Bill.

Although the Estimates and Appropriation Act guides the disbursement of public funds, the release of money is subject to relevant warrants being approved by the finance minister for the expenditure. The warrant authorises the Accountant-General to issue money from the Consolidated Revenue Fund and Development Fund. Without the warrant no money will be released. The system of warrant gives the executive much higher control over the issuance of funds than would be offered by a system which relies solely on the provisions of the Appropriation Act.

3.4 The Treasury Control

The Treasurer has the overall responsibility for the total expenditure of government. The Office of the Treasurer must keep necessary books of accounts to record all the receipts and expenditures of all ministries and departments. The Treasury exercises some measure of supervision and checks over the accounting records of the non-self accounting units. The inspectorate officers visit the various ministries and departments to evaluate the system of internal control. They do this to ensure that the accounting system and maintenance of various books of accounts conform to the approved regulations and procedures.

Again, the Treasury dispatches internal auditors to the ministries and self-accounting departments to appraise the effectiveness of the existing internal checks and report upon any inadequacy found.

SELF-ASSESSMENT EXERCISE

Briefly explain what you understand by treasury control over budgeted expenditure.

3.5 The Departmental Control

Money voted for a ministry is vested in the minister of the ministry who is the accounting officer of his ministry, and as such it is primarily his duty to ensure that such money is not overspent on any sub-head of the vote under his control. The system of accounting introduced by the Accountant-General into his department is properly maintained, and that money for his ministry is used solely for the purpose for which they were meant for, and ensure punctual and proper collections of the revenue and its payment into the consolidated revenue fund. Responsibility for expenditure in various branches and units of the ministry is fixed and controlled by the accounting officer issuing department warrants.

A Department Vote Expenditure Allocation book is a record of expenditures and liabilities incurred under the votes or funds approved for each ministry or extra-ministerial department. A vote book is maintained for each head and sub-heads of expenditures. It is an integral part of the budgetary control system. The book is designed to facilitate vote watching to ensure that expenditures incurred are not in excess of appropriation. It is the duty of the officer who is controlling the vote to thoroughly investigate, without delay, payments or charges which appear in the schedules drawn up by the Accountant-General which do not appear in the vote books particularly with a view to the prevention and detection of fraudulent payments.

4.0 CONCLUSION

The various ministries and departments, control government expenditure through the following means:

- Maintenance or proper books of accounting entries
- Establishment of functional system of internal entries
- Establishment of Internal Audit Department to complement the internal control system
- Issuance of internal financial circulars
- Maintenance of vote book.

5.0 SUMMARY

In this unit, we discussed the various expenditure control adopted by the government, starting from the Executive Control to the Legislative Control; the Ministry of Finance Control; the Treasury Control; and the Departmental Control.

6.0 TUTOR-MARKED ASSIGNMENT

i. Describe the Executive Control over budgeted expenditure.
ii. Discuss the Legislative Control over budgeted expenditure exercised by the Ministry of Finance.
iii. Discuss the Departmental Control over budgeted expenditure.

7.0 REFERENCES/FURTHER READING

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MODULE 4 BUDGETING AND STRATEGY

Unit 1 Operational Budgeting
Unit 2 Capital Budgeting
Unit 3 Budgeting and Development Planning
Unit 4 Project Performance Budgeting System
Unit 5 Strategic Decision Making Process, Implementation and Control

UNIT 1 OPERATIONAL BUDGETING

CONTENTS

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  3.2 Overhead Cost Budget
  3.3 Revenue Budget
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1.0 INTRODUCTION

You would recall that in Unit 2 of Module 1, we discussed the master budget. A master budget can be divided into operating and financial budgets. The types of budget discussed in Unit 2 are both operating budgets (sales budget, production budget) and financial budgets (cash budget and capital budget).

The operating budgets describe the income generating activities of a firm: sales, production and finished goods inventories. These are directly applicable to the private sector. In this unit however, we do not intend to duplicate the operating budget but streamline the operating budget to public sector management. Consequently, we shall discuss personnel cost budget, overhead cost budget and revenue budget as would be applicable to government accounting.

2.0 OBJECTIVES

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

- prepare a personnel cost budget
- prepare an overhead cost budget
- prepare a revenue budget.

3.0 MAIN CONTENT

3.1 Personnel Cost Budget

Personnel cost budget depict the total basic salaries and allowances of the various categories of staff in each ministry or department. The procedure for the preparation of personnel cost budget involves the following.

- Identification of the various positions in each ministry from level 17 to grade level 01.
- Identification of the number of staff on each position which may include newly promoted staff, new recruitments and the existing staff.
- Identification of the grade level of each position.
- Identification of the basic salary and the annual incremental rate.

The example for the preparation of personnel cost budget of an audit department of a government agency is shown below:

Position	**Number in post**	**Grade Level**	**Salary ₦ (a) (b)**
Director of audit	1	17	2,180,000 x 650,000
Deputy Director of Audit	2	16	2,170,000 x 435,000
Assistant Director of Audit	6	15	1,750,000 x 325,000
Chief Auditor	8	14	1,420,000 x 240,000

It should be noted that the figure stated under salary as (a) above constitute the basic salary per annum, while (b) constitute annual incremental rate. To solve the above example, this formula should be used. {(x-1) incremental rate + basic salary}n where x = the new step each of the officers will be,1 = constant, n = number of staff in each position. Assuming the example above stated that it is management policy to prepare staff salary base on step 4 and that staff allowances constitutes 35% of staff salary. You should note that the solution must necessarily follow the pattern of the question. The solution will be as follows:

Office of the Auditor-General for the Federation Personnel Cost Budget for the year 2011

Position	**Number in Post**	**Grade Level**	**Salary ₦**
Director of Audit - wk1	1	17	4,130,000
Deputy Director of Audit - wk2	2	16	6,950,000
Assistant Director of Audit - wk3	6	15	16,350,000
Chief Auditor	8	14	17,120,000
Subtotal			44,550,000
Add staff allowances at 35% (35% of 44,550,000)			15,592,500
Total personnel cost			**60,142,500**

Working 1
Formula = {(x-1) incremental rate + basic salary}n

You should recall that it is management policy to prepare staff salary base on step 4. Therefore, Director of Audit = {(4-1)650,000 + 2,180,000}1 = ₦4,130,000

Working 2
Deputy Director of Audit = {(4-1)435,000 +2,170,000}2 = ₦6,950,000

Working 3
Assistant Director of Audit = {(4-1)325,000 + 1,750,000)6 = ₦16,350,000

Working 4
Chief Auditor = {(4-1)240,000 + 1,420,000}8 = ₦17,120,000

3.2 Overhead Cost Budget

Using the previous year actual expenditure under each vote head and increasing it using the inflation factor, the overhead cost budget is prepared. This is known as the incremental budgeting which was discussed theoretically in Unit 7 Module 2.

To compute the overhead cost budget, let us assume the following actual expenditure occurred in the office of the Accountant-General of the Federation in 2010 budget year.

a.	Maintenance of motor vehicle	₦3,500,000
b.	Travelling and transport	₦7,800,000
c.	Hotel accommodation	₦14,600,000
d.	Utility services	₦7,200,000
e.	Others	₦16,200,000

The inflation factor is 15%.

To solve the above problem under the incremental budgeting system, all you should do is to multiply the various expenditures by the inflation factor and add the result to 2010 expenditure to obtain the year 2011 estimate (overhead cost budget).

Office of the Accountant-General of the Federation
Overhead cost budget for the year 2011 fiscal year

2010 (actual) Inflation factor (15%) 2011 estimate

	₦	₦	₦
Maintenance of motor vehicle	3,500,000	(3,500,000x15%)= 525,000	4,025,000
Travelling & transport	7,800,000	(7,800,000x15%)=1,170,000	8,970,000
Hotel accommodation	14,600,000	(14,600,000x15%)=2,190,000	16,790,000
Utility services	7,200,000	(7,200,000x15%)=1,080,000	8,280,000
Others	16,200,000	(16,200,000x15%)=2,430,000	18,630,000
Total	cost budget overhead		56,695,000

SELF-ASSESSMENT EXERCISE

Discuss the personnel cost budget in a public sector establishment.

3.3 Revenue Budget

This is computed by aggregating all the various incomes accrued to a particular ministry, state or local government. For instance, you could have a question like this.

Ikeja Local Government has a population of eight million citizens of which five million are taxable adults who will pay tax at the rate of N500 per adult. It also has 25,000 market stalls rented to traders at N70,000 per annum per stall. There are 8,000 hawkers who will pay entrance fee to the market on daily basis at the rate of N150 per day. There are 28 days in a month and 12 months in a year. Prepare the revenue budget of the local government for the year 2006.

Solution

Ikeja Local Government

Revenue budget for the year 2006	₦
Taxes (5,000,000 x ₦500)	2,500,000,000
Market stall rentals (25,000 x ₦70,000)	1,750,000,000
Hawkers (8,000 x ₦150x28daysx12)	403,200,000
Total revenue budget	**4,653,200,000**

4.0 CONCLUSION

There has been a minor change in the preparation of the draft estimate in the new presidential system. In the past, the draft estimate features the personnel emolument on one hand and the other changes on the other. In the presidential system, it features personnel cost on one hand and overhead cost on the other. Overhead cost being other charges and special expenditure. Personnel cost budget is the simplest of the various divisions of budget to be prepared by each ministry and extra-ministerial department.

5.0 SUMMARY

In this unit, we discussed the functional budgets of government accounting. Specifically, we were able to describe the preparation of personnel cost budget, overhead cost budget and revenue budget.

6.0 TUTOR-MARKED ASSIGNMENT

i. An actual expenditure occurred in the office of Auditor-General which is given as follows for the year 2008.

	₦
Maintenance of motor vehicle	4,200,000
Travelling and transport	7,100,000
Hotel accommodation	12,300,000
Utility services	6,200,000
Others	8,900,000

The inflation factor is 5%

You are required to prepare the overhead cost budget for the office of the Auditor-General of the Federation, for the year 2009.

ii. Isolo Local Government has a population of five million citizens of which three million are taxable adult who will pay tax at the rate of ₦70 per adult. It also has 10,000 market stalls rented to traders at ₦52,000 per annum per stall. There are 5,000 hawkers who will pay entrance fee to the market on daily basis at the rate of ₦50 per day. There are 26 days in a month and 12 months in a year. Prepare the revenue budget of the local government for the year 2008.

7.0 REFERENCES/FURTHER READING

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UNIT 2 CAPITAL BUDGETING

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1.0 INTRODUCTION

In this unit, we shall concentrate on the planning and controlling decisions for projects that affect financial results over a period longer than just the next year. Such decision requires investments of large amounts of resources called capital outlays - in anticipation of future benefits.

The term capital budgeting describes the long-term planning for making and financing such outlays. Capital budgeting has three phases which are (1) identifying potential investments (2) choosing which investment to make and (3) follow-up monitoring of the investments. Accountants usually are not involved in the first phase, but they play important roles in Phase 2 and 3. Accountants gather and interpret information to help managers make capital budgeting decisions.

To help organise what could be pages worth of information; accountants rely on capital budgeting methods. Let us discuss some of these methods in this unit.

2.0 OBJECTIVES

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

- solve and apply the decision rule applicable to Payback Period Method on a given projects
- solve and apply the decision rule applicable to Accounting Rate of Return on given projects

- solve and apply the decision rule applicable to net Present Value on given projects
- solve and apply the decision rule applicable to Internal Rate of Return on given projects.

3.0 MAIN CONTENT

3.1 Payback Period Method

This method focuses on the time taken for an investment to recoup the amount invested in it. A project would be preferable when it takes a shorter payback period. That is, among three or more projects, this method suggests that the project with the shortest period to recoup should be the one selected. For a single project, the payback period is compared with a set standard. For mutually exclusive projects, they are ranked and the one with the shortest payoff time is selected. This method is a non-discounted cash flow method.

Advantages of Pay-Back Period Method

a. It is a useful measure of liquidity because the method ensures the selection of projects that provide the hope of immediate cash recoupment.
b. It may be used as a safeguard against risk.
c. It is simple to calculate and understand.
d. The method is popular with public project evaluations where liquidity predominates over profitability.
e. It serves as a useful screen to evaluate all projects.
f. The approach uses cash flows rather than accounting profits to appraise.

Disadvantages of the Pay-Back Period Method

a. It does not consider the time value of money.
b. It ignores variations in the timing of cash inflows within the payback period.
c. Cash inflows outside the payback period are ignored.
d. It does not take into consideration risks and uncertainties.

Example
Esan West Local Government Council is considering investing in one of the following three available projects. Using the payback period method, you are required to advise on which of the projects that should be selected.

Projects	**A1**	**A2**	**A3**
	₦	₦	₦
Initial investment outlays	200,000	260,000	280,000

Year	Sales Proceeds		
	₦	₦	₦
1	100,000	40,000	80,000
2	60,000	50,000	150,000
3	40,000	40,000	40,000
4	30,000	50,000	10,000

Solution
Esan West Local Government Council
Payback Period Method of Project Appraisal

Projects	A1	A2	A3
	₦	₦	₦
Outflow initial investment	(200,000)	(260,000)	(280,000)
Less inflow in year 1	100,000	40,000	80,000
	100,000	220,000	200,000
Less inflow in year 2	60,000	50,000	150,000
	40,000	170,000	50,000
Less inflow in year 3	40,000	40,000	40,000
	Nil	130,000	10,000
Less inflow in year 4	-	50,000	10,000
		80,000	Nil

From the appraisal conducted, you would observe that project A1 was able to pay off its initial capital injected in year 3. Project A3 was able to pay off its initial capital injected in year 4 but project A2 could not generate enough cash inflows for the period of four years. Project A1 is therefore more profitable than A3 and A2 should be dropped completely.

3.2 Accounting Rate of Return (ARR)

This is the return on initial outlay or return on average capital. It is computed using the formula, ARR = average annual accounting profit/average investment.

Where average investment is investment + residual value/2.

Profit is the accounting profit. This is gotten by taking income and deducts all necessary expenses incurred in earning the income. Using accounting rate of return, the decision rule is to pick the option which gives the highest percentage rate of return. This is also a non-discounted cash flow method.

Advantages of ARR Method

a. It considers the profits of a project throughout its useful life.
b. It is simple to calculate and understand.
c. It facilitates expenditure follow up due to more readily available data on accounting records.

Disadvantages of ARR Method

a. It does not take into account the time value of money.
b. It ignores the fact that profits from different projects may accrue at an uneven rate.
c. It fails to cater for risks and uncertainties.

Example

Assuming Oredo Local Government Council supplied the following information:

Projects		B1	B2	B3
		₦	₦	₦
Profit figure-year	1	1,500	1,000	4,000
	2	2,500	1,500	3,800
	3	3,500	2,000	2,000
	4	4,500	2,500	500
Initial investment sums		16,000	10,000	15,000
Residual investment		1,000	1,000	2,000

Using the accounting rate of return as performance measurement, which project should Oredo Local Government Council invest in?

Solution

Oredo Local Government Council
Computation of Accounting Rate of Return

Projects		B1	B2	B3
		₦	₦	₦
Project figure year	1	1,500	1,000	4,000
	2	2,500	1,500	3,800
	3	3,500	2,000	2,000
	4	4,500	2,500	500
Total		12,000	7,000	10,300

Average annual accounting profit:

Projects	B1	B2	B3
	12,000/4	7,000/4	10,300/4
=	N3,000	N1,750	N2,575

To obtain average investment:

Projects	B1	B2	B3
	₦	₦	₦
Initial investment	16,000	10,000	15,000
Add residual value	1,000	1,000	2,000
	17,000	11,000	17,000
Average investment=	17,000/2	11,000/2	17,000/2

=	N8,500	N5,500	N8,500
=	accounting rate of return = A/B		
=	3,000/8,500	1,750/5,500	2,575/8,500
=	35%	32%	30%

Oredo Local Government Council should invest in project B1 because it has the highest accounting rate of return of 35%.

SELF-ASSESSMENT EXERCISE

What are the advantages and disadvantages of the Pay-Back Period Method?

3.3 Net Present Value (NPV)

This is a discounted cash flow method. This method refers to the equivalents in present value terms of the cash inflows and outflows from a project when discounted at a particular or given cost of capital. The decision criterion is that a project is acceptable if it has a positive NPV. In total, the present value of cash inflows should be greater than that of cash outflows. The positive nature of the net present value pre-supposes the potential increase in consumption made possible by the investment, valued in present day terms.

For mutually exclusive projects, they would be ranked and the one with the highest net present value is selected.

The formula for the computation of the net present value is:

NPV = [C1/(1+K), C2/(1+K)2,C3/(1+K)3,Cn/(1+K)n] – Co

Where C series represent cash inflows, K represents the opportunity cost of capital, Co is the initial cost of the investment and n represents the project's expected life.

Advantages of Net Present Value

a. Timing of cash flows is considered.
b. Cash flows on the entire lives of the projects are considered.

Disadvantages of Net Present Value

a. There is the obligation for management to determine the appropriate cost of capital to use.
b. It is not suitable where capital rationing situation exists.
c. There is the assumption that the cash inflows will come as predicted which may not necessarily be so.

Example
Using the net present value method, you are required to advise Ifo Local Government Council on which of the projects A, B, C, is the most viable and should be selected.

	Project A	Project B	Project C
	₦	₦	₦
Cost of initial investment	150,000	240,000	210,000
Receipts from projects			
Year 1	40,000	20,000	60,000
Year 2	60,000	30,000	20,000
Year 3	80,000	60,000	70,000
Year 4	90,000	70,000	50,000
Year 5	100,000	100,000	30,000

You should assume that the cost of capital is 10% and use the discount table stated below.

Year	Discount factor
	0.9090
	0.8264
	0.7513
	0.6830
	0.6209

Ifo Local Government Council
Investment appraisal using NPV method

Project A

Year	Cash flow	Discount factor	Discounted cash flow (DCF)
	₦	(10%)	₦
0	(150,000)	(1.000)	(150,000)
1	40,000	0.9090	36,360
2	60,000	0.8264	49,584
3	80,000	0.7513	60,104
4	90,000	0.6830	61,470
5	100,000	0.6209	62,090
		NPV	119,608

Project B

Year	Cash flow	Discount factor	Discounted cash flow (DCF)
	₦	(10%)	₦
0	(240,000)	(1.000)	(240,000)
1	20,000	0.9090	18,180
2	30,000	0.8264	24,792
3	60,000	0.7513	45,078
4	70,000	0.6830	47,810
5	100,000	0.6209	62,090
		NPV	(42,050)

Project C

Year	Cash flow	Discount factor	Discounted cash flow (DCF)
	₦	(10%)	₦
0	(210,000)	(1.000)	(210,000)
1	60,000	0.9090	54,540
2	20,000	0.8264	16,528
3	70,000	0.7513	52,591
4	50,000	0.6830	34,150
5	30,000	0.6209	18,627
		NPV	(33,564)

Ifo Local Government Council is advised to invest in project A because it has a positive NPV among the three projects. In situation where the three projects have a positive NPV, selecting the project that has the highest positive NPV would have been the chosen option.

3.4 Internal Rate of Return (IRR)

This is also a discounted cash flow method. The Internal Rate of Return is the discount rate which when applied gives zero net present value. It can be found by either drawing a present value profile or graph, or mathematically through linear interpolation, using this formula.

R1 + P (R2-R1)/P+N
Where R1 is the positive rate
R2 is the negative rate
P is the positive net present value
N is the negative net present value

The decision rule is to accept the project appraisal where the calculated rate is greater than the company's cost of capital. We select the project with the highest percentage of internal rate of return where two or more mutually exclusive investments are being considered.

Example
Power Holding Company of Nigeria (PHCN) is preparing the capital budget for the forth coming year. Three mutually exclusive projects are being considered.

The projected performance of each of the projects is as follows:

Projects	A	B	C
	₦	₦	₦
Initial cash outlays	3,450	3,563	3,939
Inflows of cash			
Year 1	1,500	2,250	375
Year 2	1,500	1,125	375
Year 3	1,500	1,125	4,875

The Authority's cost of capital is 10% per annum. As the Management Accountant of PHCN, advise on the desirability or otherwise of choosing any of the three projects, using the internal rate of return method.

The following discount factor table is applicable for use:

Year	10%	15%
1	0.91	0.87
2	0.83	0.76
3	0.75	0.66
4	0.68	0.57
5	0.62	0.50

Solution
PHCN
Project A

Using 10% discount factor (rate)

Year	Cash flows	Discount factor	DCF
	₦'000	(10%)	₦'000
0	(3,450)	(1.00)	(3,450)
1	1,500	0.91	1,365
2	1,500	0.83	1,245
3	1,500	0.75	1,125
		NPV	285

Using 15% discount factor (rate)

Year	Cash flows	Discount factor	DCF
	₦'000	(15%)	₦'000
0	(3,450)	(1.00)	(3,450)
1	1,500	0.87	1,305
2	1,500	0.76	1,140
3	1,500	0.66	990
		NPV	(15)

Using the formula IRR= R1+[P/P+N] (R2-R1)

Project A = 10 + [285/285+15] 15-10
= 10 + [285/300] 5
= 10 + [0.95] 5
= 10 + 4.75
= 14.75%

Project B
Using 10% discount rate, we have

Year	Cash flows	Discount factor	DCF
	₦'000	(10%)	₦'000
0	(3,563)	(1.00)	(3,563)
1	2,250	0.91	2,047.50
2	1,125	0.83	933.75
3	1,125	0.75	843.75
		NPV	262

Using 15% discount rate

Year	Cash flows	Discount factor	DCF
	₦'000	(15%)	₦'000
0	(3,563)	(1.00)	(3,563)
1	2,250	0.87	1,957.50
2	1,125	0.76	855
3	1,125	0.66	742.50
		NPV	(8)

IRR = R1 + [P/P+N] (R2-R1)
= 10 + [262/262+8] 15-10
= 10 + [262/270] 5
= 10 + [0.970] 5
= 10 + 4.85
= 14.85%

Project C

Using 10% discount rate

Year	Cash flows	Discount factor	DCF
	₦'000	(10%)	₦'000
0	(3,938)	(1.00)	(3,938)
1	375	0.91	341.25
2	375	0.83	311.25
3	4,875	0.75	3,656.25
		NPV	370.75

Using 15% discount rate

Year	Cash flows	Discount factor	DCF
	₦'000	(15%)	₦'000
0	(3,938)	(1.00)	(3,938)
1	375	0.87	362.25
2	375	0.76	285
3	4,875	0.66	3,217.50
		NPV	(109.25)

IRR = R1 + [P/P+N] R2-R1
= 10 + [370.75/370.75+109.25] 15-10
= 10 + [370.75/480] 5
= 10 + [0.772] 5
= 10 + 3.86
= 13.86%

From the above computations, you would observe that project B has the highest IRR of 14.85%. Therefore, project B should be accepted while the other two rejected.

4.0 CONCLUSION

Investment is the judicious utilisation of resources on viable opportunities, with a view to earning reasonable returns beneficial to the providers of funds. Investment decisions are taken after the feasibility and viability of projects have been considered.

Although investments are undertaken in the public sector organisations just as in the private sector, operating environments and the goals pursued are different. While non-profitable projects may be dropped in the private sector, it may be unreasonable to act in this way in the public sector for political, socio-economic, historical and security reasons.

5.0 SUMMARY

In this unit, we discussed four capital budgeting methods which are payback period, accounting rate of return, net present value and internal rate of return.

You would recall that using the payback period method, the decision rule is that, a project is preferable when it takes a shorter payback period. Using accounting rate of return, the decision rule is to pick the option which gives the highest percentage rate of return. Using the net present value, the decision rule is that a project is acceptable if it has a positive NPV. Finally, using the internal rate of return, the decision rule is to accept the project appraisal where the calculated rate is greater than the company's cost of capital and we select the project with the highest percentage of internal rate of return where two or more mutually exclusive investments are being considered.

6.0 TUTOR-MARKED ASSIGNMENT

i. Ikeja Local Government Council is considering investing in one of the following three available projects. Using the payback period method, you are required to advise on which of the projects that should be selected.

Projects	D1	D2	D3
	₦	₦	₦
Initial investments outlays	250,000	290,000	360,000
Sales proceeds- year 1	150,000	80,000	120,000
2	100,000	100,000	150,000
3	40,000	110,000	80,000
4	80,000	20,000	10,000

ii. Isolo Local Government Council supplied the following information.

Projects		E1	E2	E3
Profit figures- year	1	1,800	1,200	3,200
	2	3,100	1,800	3,800
	3	3,500	2,200	2,500
	4	2,800	3,500	1,000
Initial investment sums		15,000	7,000	10,000
Residual investment		1,000	750	1,500

iii. Using the accounting rate of return as performance measurement, which project should Isolo Local Government Council invest in?

Using net present value method you are required to advise Oredo Local Government Council on which of the projects A, C, F, is the most viable and should be selected.

		Project A	**Project C**	**Project F**
		₦	**₦**	**₦**
Cost of initial investment		180,000	220,000	200,000
Receipts from projects- year	1	50,000	30,000	70,000
	2	70,000	40,000	30,000
	3	90,000	70,000	80,000
	4	100,000	80,000	60,000
	5	90,000	90,000	40,000

Assuming that the cost of capital is 10%

7.0 REFERENCES/FURTHER READING

Garrison, R. H. (1988). *Management Accounting, Concepts for Planning, Control, Decision Making.* Texas: Business Publication Inc.

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UNIT 3 BUDGETING AND DEVELOPMENT PLANNING

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 3.1 What is Development Planning?
 3.2 A Tool for Performing a SWOT Analysis
 3.3 Performance Development Planning
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1.0 INTRODUCTION

The most important part of any endeavor is the time spent planning the activity. Good planning can save time, effort and resources. The ability to plan effectively is an essential management skill.

Planning is a major weakness in most organisations including government agencies in the country. Most developed countries have exploited the benefits of planning to create development in their countries. This is the bane of poor economic development in the third world countries including Nigeria. Perhaps, this is because most people would rather be doing something than talking or thinking about it. In some cases, it may be because the planning process is not well understood.

Budgeting forces management to plan for the future. It encourages managers to develop an overall direction for the organisation, foresee problems, and develop future policies. In this unit, we shall discuss development planning, the tool for performing a SWOT analysis and performance development planning.

2.0 OBJECTIVES

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

- explain development planning
- discuss the tool for performing a SWOT analysis
- explain performance development planning.

3.0 MAIN CONTENT

3.1 What is Development Planning?

Development planning is the process of determining where an organisation is going. In other words, what it wants to be in the future and how it intends to get there. It involves looking carefully at the organisation and the environment it must work in, setting worthwhile but realistic goals and putting together a co-ordinate plan of action for reaching those goals.

Development planning typically follows a set of distinct phases:

- Situation analysis, both internal to the area, and the forces which are shaping the area. This may involve a range of tools to assess the strengths, weaknesses, threats and opportunities (SWOT) facing an area
- Prioritising key issues, problems or outcomes
- Developing objectives
- Developing plans to address the objectives, including strategies, activities and projects
- Developing a spatial picture of the situation as well as plans
- Developing budgets to achieve the plans.

SELF-ASSESSMENT EXERCISE

List the phases of development planning.

3.2 A Tool for Performing a SWOT Analysis

Strengths, weaknesses, opportunities and threats analysis guides one to identify the positives and negatives inside the organisation and outside of it in the external environment. Programme directors, policy groups and management teams can use this resource to guide them through the SWOT assessment. Included are some general questions in each SWOT category to prompt an analysis of an organisation or programme effort.

Internal	**Positives**	**Negatives**
Human resources Physical resources Financial resources Activities and processes, past experiences	What are your own advantages, in terms of people, physical resources, finance? What do you do well? What activities or processes have met with success?	What could be improved in your organisation in terms of staffing, physical resources, funding? What activities and processes lack effectiveness or are poorly done?
External	Opportunities	Threats
Future trends in your field or culture. The economy funding sources (foundations, donors, legislature), demographics, the physical environment legislation, local, national or international events.	What possibilities exist to support or help your effort in the environment, the people you serve, or the people who conduct your work? What local, national or international trends draw interest to your programme? Is a social change or demographic pattern favourable to your goal? Is a new funding source available? Have changes in policies made something easier? Do changes in technology hold new promise?	What obstacles do you face that hinder the effort in the environment, the people you serve, or the people who conduct your work? What local, national or international trends favour interest in other or competing programmes? Is a social change or demographic pattern harmful to your goal? Is the financial situation of a major funder changing? Have changes in politics made something more difficult? Is changing technology threatening your effectiveness?

3.3 Performance Development Planning

The performance development planning (PDP) process enables the manager and the people who report to the manager to identify their personal and business goals that are most significant to their organisation's success.

The process enables each staff to understand their true value-added to the organisation. They do so when they understand how their job and the requested outcomes from their contributions fit inside the department or work unit's overall goals.

In the process, staff members also set personal developmental goals that will increase their ability to contribute to the success of your organisation. The accomplishment of these goals also provides a foundation for their career success whether in the organisation or elsewhere, so they ought to be motivated and excited about achieving these goals.

Performance development planning is held at least quarterly to review staff progress on the overall goals and objectives. The staff progress on the action plans that result from performance development goals is reviewed at weekly one-on-one meeting. This meeting allows one to offer assistance and to identify any help or tools the staff needs to succeed.

4.0 CONCLUSION

It is important we see the link between development planning and budgeting. Development planning sets the priority areas of services and specifies the target outputs and accomplishments. Budgeting provides the available resources to carry out the activities required to accomplish the targets.

5.0 SUMMARY

In this unit, we discussed the meaning of development planning and practically see how a tool for performing a SWOT analysis could be used. In addition, we also discussed development planning as it would affect the staff of an organisation.

6.0 TUTOR-MARKED ASSIGNMENT

i. Discuss the tool for performing SWOT analysis.
ii. What is performance development planning?

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UNIT 4 PROJECT PERFORMANCE BUDGETING SYSTEM

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
 3.1 What is Project Performance Budgeting System?
 3.2 Main Steps in Project Performance Budgeting System
 3.3 Advantages and Disadvantages of Project Performance Budgeting System
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1.0 INTRODUCTION

The management of money is more important than ever for public and private entities. Public entities need to go through many processes before moving into the budget execution phase and post-execution analysis. Compared to private sector, the processes are cumbersome. The traditional methods of analysing and utilising budget figure are insufficient.

Project performance budgeting system is a new approach to budget analysis and utilisation which is many steps ahead of traditional methods. For instance, once the long-term plans are accomplished, the traditional way to assess the effectiveness of the project is to assess the gap between the budget and the actual money spent. However, with the new budgeting approach, the questions to answer are tougher, such as:

- Did we really succeed in accomplishing the set objectives?
- Did the project cost what we expected?
- Have we done what we should have done in meeting the objectives?

Therefore, it is important to approach the planning and budgeting cycle in holistic and integrated way, with collaboration across the areas of policy design, performance measures definition and policy evaluation.

2.0 OBJECTIVES

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

- explain the term project performance budgeting system
- state the steps involved in project performance budgeting system
- state the advantages and disadvantages of project performance budgeting system.

3.0 MAIN CONTENT

3.1 What is Project Performance Budgeting System?

Project performance budgeting system uses statements of missions, goals and objectives to explain why the money is being spent. It is a way to allocate resources to achieve specific objectives based on programme goals and measured results. It is important that you note the key to understanding project performance budgeting system is the word 'result'. The entire planning and budgeting framework is resulted oriented. There are objectives and activities to achieve these results and this form the foundation of the overall evaluation.

Project performance budgeting system comprises three elements which are:

- The result (final outcome)
- The strategy (different ways to achieve the final outcome)
- Activity/outcomes (what is actually done to achieve the final outcome).

Project performance budgeting system is a way to allocate resources for achieving certain objectives. PPBS set a goal or a set of goals, to which funds are apportioned.

3.2 Main Steps in Project Performance Budgeting System

The following are the steps involved in project performance budgeting system.

a. Identification and enumeration of goals and objectives of the organisation
b. Defining the total system in detail, including objectives' environment, available resources, the programmes and their objectives etc

c. Planning and analysis. These involve continuous process of developing, comparing and analysing alternative programmes, so as to evolve the most appropriate package for the organisation
d. Development of the appropriate measures of performance for the programmes of the organisation
e. Programming and budgeting: The agreed package of programmes completed with resource requirements and expected results are expressed in the form of 'programmed budgets'
f. Reporting and controlling: Project performance budgeting system requires sophisticated information service which is able to monitor the progress made towards meeting the organisational objectives, rather than the amount spent which is the focus in traditional budgeting system
g. Development each year of a multi-year programme and financial plan.

SELF-ASSESSMENT EXERCISE

Explain the term project performance budgeting system.

3.3 Advantages and Disadvantages of Project Performance Budgeting System

Advantages

a. The technique provides information on the objectives of the organisation.
b. It lays emphasis on long-term effects.
c. It achieves effective use of budgeted resources and anticipated performance.
d. The technique ensures rational decision making and forces those seeking budgetary allocation to consider alternatives.
e. It leads to rapid economic development.

Disadvantages

a. Natural resistance to change, particularly among the very senior officers in the government hierarchy.
b. Transitional problems at the introductory stage.
c. Problem of staff shortage.
d. Paucity of data.
e. Re-orientation of the old accounting system to cater for the requirements of the new concept.
f. Problem of data collection and physical monitoring.
g. It is difficult to install.
h. It makes heavy demand on resources.

i. The uncertainty of the future makes long term planning difficult.

4.0 CONCLUSION

Project performance budgeting system is not easy to tackle, but in the ever-changing business and political climate, it definitely worth a closer look.

5.0 SUMMARY

In this unit, we discussed project performance budgeting system. You should recall that project performance budgeting system is a way to allocate resources for achieving certain objectives. The main steps in project performance budgeting system and the advantages of PPBS were equally discussed.

6.0 TUTOR-MARKED ASSIGNMENT

i. Describe the Executive Control over budgeted expenditure. State the steps involved in project performance budgeting system.
ii. State five advantages and disadvantages of project performance budgeting system.

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UNIT 5 STRATEGIC DECISION MAKING PROCESS, IMPLEMENTATION AND CONTROL

CONTENTS

1.0 Introduction
2.0 Objectives
3.0 Main Content
 3.1 Strategic Decision Making Process
 3.2 Corporate Strategy
 3.3 Strategy Implementation
 3.4 Evaluation and Control in Strategic Management
4.0 Conclusion
5.0 Summary
6.0 Tutor-Marked Assignment
7.0 References//Further Reading

1.0 INTRODUCTION

Planning and control are inextricably linked. Planning is looking ahead to see what actions should be taken to realise certain goals. Control is looking backward, determining what actually happened and comparing it with the previously planned outcomes. This comparison can then be used to adjust the budget.

A key component of planning which are budgets, are financial plans for the future; they identify objectives and the actions needed to achieve them. Before a budget is prepared, an organisation would develop a strategic plan. The strategic plan identifies strategies for future activities and operations, generally covering at least five years. The organisation can translate the overall strategy into long-term and short term objectives. These objectives form the basis of the budget. There is a tight linkage between the budget and the strategic plan.

2.0 OBJECTIVES

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

- outline the steps involved in strategic decision making process
- discuss corporate strategy
- discuss strategy implementation
- discuss evaluation and control in strategic management.

3.0 MAIN CONTENT

3.1 Strategic Decision Making Process

This process deals with the long-run future of the entire organisation and has three features.

a. Rare-strategic decisions are unusual and typically have no precedent to follow.
b. Consequential-strategic decisions commit substantial resources and demand a great deal of commitment.
c. Directive-strategic decisions set precedents for lesser decisions and future actions throughout the organisation.

The most typical approaches or modes of strategic decision making are entrepreneurial, adaptive and planning.

In order to make better strategic decision, according to authorities, the following seven steps strategic decision making process is proposed.

a. Evaluate current performance results.
b. Review corporate governance.
c. Scan the external environment.
d. Analyse strategic factors (SWOT).
e. Generate, evaluate and select the best alternative strategy.
f. Implement selected strategies.
g. Evaluate implemented strategies.

SELF-ASSESSMENT EXERCISE

What are the features of strategic decision making process?

3.2 Corporate Strategy

Corporate strategy is primarily about the choice of direction for the firm as a whole. This is true whether the firm is a small one product company or a large multinational corporation. In a large multi-business company however, corporate strategy is also about managing various product lines and business units for maximum value. In this instance, corporate headquarters must play the role of organisational ‘parent’ in that it must deal with various product and business unit ‘children’. Even though each product line or business unit has its own competitive or cooperative strategy that it uses to obtain its own competitive advantages in the market place, the corporation must coordinate these different business strategies so that the corporation as a whole succeeds as a ‘family’.

Corporate strategy therefore, includes decisions regarding the flow of financial and other resources to and from a company's product lines and business units. A company transfers skills and capabilities developed in one unit to other units that need such resources. In this way, it attempts to obtain synergies among numerous product lines and business units so that the corporate whole is greater than the sum of its individual business unit parts. All corporations, from the smallest company offering one product in only one industry to the largest conglomerate operating in many industries in many product must at one time or another, consider one or more of these issues.

3.3 Strategy Implementation

Strategy implementation is the sum total of the activities and choices required for the execution of strategic plan by which strategies and policies are put into action through the development of programmes, budgets and procedures. Although, implementation is usually considered after strategy has been formulated, implementation is a key part of strategic management. Thus, strategy formulation and strategy implementation are the two sides of the same coin.

Depending on how the corporation is organised, those who implement strategy will probably be a much more divorced group of people than those who formulate it. Most of the people in the organisation who are crucial to successful strategy implementation probably had little to do with the development of corporate and even business strategy. Therefore, they might be entirely ignorant of vast amount of data and work into formulation process. This is one reason why involving middle managers in the formulation as well as in the implementation of strategy tends to result in better organisational performance.

The managers of divisions and functional areas worked with their fellow managers to develop programmes, budgets and procedures of implementation of strategy. They also work to achieve synergy among the divisions and functional areas in order to establish and maintain a company's distinctive competence. A programme is a statement of the activities or steps needed to accomplish a single use plan. The purpose of a programme is to make a strategy action-oriented.

A budget is a statement of corporation's programme in monetary terms. After programmes are developed, the budget process begins. Planning a budget is the last real check a corporation has on the feasibility of its selected strategy. Procedures are system of sequential steps or techniques that describe in detail how a particular task or job is to be done.

3.4 Evaluation and Control in Strategic Management

Evaluation and control is the process by which corporate activities and performance results are monitored so that actual performance can be compared with desired performance. Evaluation and control information consists of performance data and activity reports. Top management need not be involved. If however, the processes themselves cause the undesired performance, both top managers and operational managers must know about it so that they could develop new implementation programmes or procedures. Evaluation and control information must be relevant to what is being monitored. One of the obstacles to effective control is the difficulty in developing appropriate measures of important activities and outputs.

Controls can be established to focus either on actual performance results or on the activities that generates the performance. Behaviour controls specify how something is to be done through policies, rules, standard operating procedures and orders from superior. Output controls specify what is to be accomplished by focusing on the result on the end result of the behaviour through the use of objectives or performance targets or milestones. Behaviour controls are most appropriate when performance results are hard to measure and a clear cause-effect connection exists between activities and results. Output controls are most appropriate when specific output measures are agreed upon and no clear cause-effect connection exists between activities and results.

4.0 CONCLUSION

Strategic management is an ongoing process that enables and controls the business and the industries in which the company is involved; assess its competitors and sets goals and strategies to meet all existing and potential competitors, and then reassesses each strategy annually or quarterly to determine how it has been implemented and where it has succeeded or needs replacement by a new strategy to meet changed circumstances, new technology, new competitors, a new economic environment, or a new social, financial or political environment.

5.0 SUMMARY

In this unit, we were able to discuss the strategic decision making process, outlining seven steps involved in it. Corporate strategy includes decisions regarding the flow of financial and other resources to and from a company's product lines and business units.

Strategy implementation is the sum total of the activities and choices required for the execution of strategic plan by which strategies and policies are put into action through the development of programmes, budgets and procedures.

Evaluation and control is the process by which corporate activities and performance results are monitored so that actual performance can be compared with desired performance.

6.0 TUTOR-MARKED ASSIGNMENT

i. Outline the steps involved in strategic decision making process.
ii. Discuss the term corporate strategy.
iii. Discuss the term strategy implementation.
iv. Explain what you understand by evaluation and control in strategic management.

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