NEED FOR BUDGETING AND EFFICIENT FINANCIAL MANAGEMENT IN THE LOCAL GOVERNMENT ADMINISTRATION

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Abstract

Most Local Governments in Nigeria are faced with the problem of inadequate internal revenue generation capacity and thus rely heavily on statutory allocation from the federation account. The result is their inability to meet the demands from various communities for provision of essential services. This problem calls for planning and prioritization as well as effective control of the use of organizational or governmental resources. In other words the problem calls for budgeting and prudential management of Local Government financial resources. In this paper, the author examines the concept and relevance of budgeting in local Government administration and suggests effective planning and control strategies. The use of the Zero Base Budgeting (ZBB) approach is advocated instead of the traditional or incremental method, which is fraught with hidden inefficiencies.

Introduction

Government at all levels have as their major function the provision of basic socio-economic infrastructure to the people in the area of education, health, good road network, electricity, security of lives and property and other services that are directed at improving the welfare of the populace. Expectations and demands on government have continued to heighten as the level of political awareness of the people increases and these exert considerable pressure on Government resources.

Local government administration operating at the lowest rung of societal ladder has direct interaction with the masses at the grassroots. The various local governments face competing and sometimes mutually conflicting demands from the people all aimed at securing their fair share of the national cake. Only very few people bother about the baking of the cake and many strive in various ways to repudiate their civic responsibilities through tax evasion and tax avoidance.

Unfortunately most local Governments in Nigeria have very limited sources of internally general revenue. Few in urban centres have industries and other viable corporate establishments from which to make their revenue. As a result there is heavy dependence by local governments on statutory allocation from the federation account for the execution of their various programmes.

It is this basic economic problem of relative scarcity of resources vis-avis numerous and apparently insatiable demands from various segments of the society that underline the concept of budgeting and the need for prudential management of financial resources of the local Governments. I will attempt in this paper to examine the concept and relevance of budgeting in Local Government administration and suggest strategies for prudential management of financial resources,

The Concept And Nature **Of Budgeting**

From the brief introductory survey of operational environment of Local Governments, it is clear that no Local Government can provide for all the demands on its resources. The natural concomitance is therefore an effort to effectively manage available resources through planning and prioritization, and these constitute the basic concept of budgeting and its resultant outcome, the budget.

The encyclopedic edition of Lexicon Webster Dictionary (1981) defines budget as a financial statement of expenditures covering specified future period of time, a plan for financing operation based on such a statement. Horngren (1982) defines budget as "a quantitative expression of plan of action over a specified period of time and an aid to coordination and implementation".

Thus budgeting involves planning the use of organizational or governmental resources within specified future period. Hicks and Gullet (1981) assert that as an expression of planned future expenditures, budgeting forces the allocation of scarce resources by priorities, hi the words of Horngren (1982), communication and coordination. Wixon (1973) claims that governmental budgeting was used in England as early as the eighteenth century to control the king's powers of taxation and expenditure.

The concept of budgeting has become universally accepted as an essential part of financial management both in the public and private sectors. Although one type of budget, the capital budget, is a long-term plan spanning over a period of five or ten years, operating and financial budgets normally cover a period of one year, broken down into months and quarters. The annual budget reflects two distinct components or classifications. The capital component of budget covers those expenditure items that span beyond the twelve months planning period. These serve as a link between one budget period and another and thus guide the direction and shape of long-term objectives. Under this category fall planned expenditures on physical projects like road construction, market development and non-physical projects such as research and development. It also covers the purchase of equipment, vehicles and other items whose expenses are written off over their life span through depreciation charges.

The second classification relates to revenue items covering planned expenditures on overhead for the relevant planning year. Items covered include staff emolument (basic salaries and allowances) traveling and hotel expenses, planned maintenance expenses on fixed assets, depreciation charges, stationeries and other working materials etc.

Budgeting Methodology

Local Government Administration as well as other public and private sector organizations in Nigeria practice the traditional approach to budgeting described by Horgren (1982) as **incremental budgeting.**

By this method the budget for a period is determined in the light of previous year's budget as a base with specified assumptions and expectations of the budget period. In other words the previous year's budget is used as the basis for determining the current year's budget. Incremental adjustments are made to reflect expected changes, for example in price level and other variable factors. Thus a percentage increase of say 10% may be added to the previous year's basic salary figures to derive the current budget.

Although the traditional or incremental budgeting is popular and easy to use, it is fraught with hidden inefficiencies. In the first place and previous budget figures are taken for granted and assumed needed in future. In other words, the budget figures for the previous year form the basis for the current and future budgets and it is assumed that all the provisions in the previous budget will still be required in the current and future budgets. This does not necessarily follow and therefore there must be justification for continuing budgeted amount. Secondly the incremental method leads to ever-growing budget as every year an additional amount is added to previous figures. In order to impose some upper limit, the approving authorities are compelled to effect periodic across-the-board cutting to trim the requests by say 10%. The third defect is that it leads to padding as departmental heads deliberately inflate their budget figures to take care of budget cut. Finally it leads to haggling and politicking as departmental heads and council chairmen try to save their pet programmes from being trimmed. In this way approval may be given to budgets that do not satisfy specified objective criteria.

It is in the light of these problems that the writer advocates the use of the **Zero-Base Budgeting (ZBB)** approach. By this process, each departmental head is required to justify his entire budget request in detail from scratch hence the name zero-base. Hicks and Gullet (1981) assert that some vital information required for ZBB budgeting, such as goals and objectives, consequence of not performing the activity. Measures of performance alternative courses of action and cost/benefit analysis are required to ensure objectivity and facilitate the determination of real value of proposals. Unnecessary activities and budget items are easy to detect and the most efficient and cost effective choice can be made. However ZBB has its own shortcomings. It involves a large number of decision packages that must be reviewed. It is time consuming and above all requires high level of expertise, which many supervising or approving authorities may not possess.

Critical Factors In Local government Budgeting

For the purpose of this paper Local Government budgetary provisions can be classified into two categories; namely:

Those that are service-oriented and The
commercially oriented investments.

The purpose of this classification is to meaningfully identity critical factors that must be taken into account in evaluating any investment proposal. Services oriented investments relate to all items in the budget, which cannot be justified on the basis of their profitability or return on investment. In other words economic considerations do not constitute decision variables. They have political motivation and are desired to provide services to the people. Under this category are all social infrastructural facilities and welfare services such as roads and bridges, electricity, water supply, health care delivery system, education, rural sanitation, grants to remand homes, motherless babies homes, the sick and disabled.

One common characteristic of this group of services is that their benefits cannot be expressed in quantitative terms. They are rather evaluated on the basis of social profitability index. The index is a measure of expected impact of any project on the general welfare of the people. This can be evaluated by changes in health, social and economic lives of the people. Prioritization of projects in the category is therefore a function of socio-political rather than economic considerations.

Under the second category fall projects that are required to generate revenue for the Local Government. They are profit oriented and compete with similar business in the private sector. These include such projects as intercity and interacity transport services, industrial establishment, lockup stores and development of tourist centres.

The critical factor in selection and prioritizing of projects in this category is commercial profitability. Thus capital budgeting in this case must involve making systematic analysis of investment alternatives and choosing among the alternatives the projects that have the greatest promise of expected return over a future period. This is necessary to avoid white elephant projects that eventually constitute serious drain on public funds.

Process of Capital Budgeting

Home (1980) explains that systematic analysis,selection and succesful administration of capital project involve a number of facts: first is the generation of investment proposals. Which could be borne out of perceived need or service gap. Next, estimation is made of expected cash flow over the life of the projects. Since the final result obtained will depend on the accuracy of estimates. Finally the investment worthiness of the projects is evaluated in order to determine the best out of the alternatives.

In evaluating a group of projects, it is important to establish which projects are mutually exclusive and which are mutually dependent. Two projects are mutually exclusive if a choice of one means a rejection of another, as for example the use of labour intensive and capital-intensive technology. On the other hand, two projects are mutually dependent if the acceptance of one necessarily involves the incorporation of another. The proposal to purchase a new generating plant must incorporate the decision to build an engine house. Alternative investments must be mutually exclusive and mutually independent.

Bierman and Smith (1975) examined the various methods that can be employed in evaluating project proposals, ranging from ranking by inspection, return on investment (ROI) , pay-back period, the use of internal rate of return (IRR),the net present value method and the use of profitability index. The various methods vary in reliability and sophistication. The simple ones like the ranking by inspection, return on investment or payback period have limited applicability and reliability. They fail to recognize the time value of money and therefore are less valuable for statistical computation and comparism than others that use discounted cash flow method.

From the brief survey of the concept and processes of budgeting in the Local Government administration, I can now proceed to examine issues involved in prudential management of Local Government financial resources. It is important to begin by asking the questions: what is prudential management and why is it necessary in local government administration?

It is equally important to appreciate the significance of the key words "prudential" and "management". Prudential is derived from Latin word "prudentia" which means good judgement. Practical wisdom and being shrewd in planning for the future. The word management is a household terminology, which means different things to different people. For the purpose of this work, the writer adopts the definition by Hicks and Gullett (1981) that management is the act of getting things done by and through other people. It involves the planning, organizing, directing and controlling human and material resources to achieve desired ends.

In every organization whether in the private or public sector, there are two categories of workers: the managers and the non-managers, otherwise known as operatives. In the local government administration, the chairmen with their executives or supervisory councilors, the legislative arm and principal officers of Local Government constitute the managers of their respective local governments. The chairmen as chief executives take responsibility for the management of their respective local council areas by planning, organizing, directing and controlling available resources to achieve their objectives. However what is of interest here is the management of financial resources.

In the introductory part of this paper was sketched an administrative scenario of basic economic problem facing the local government administrators, i.e. the need to satisfy ever-increasing demands from various segments and communities in the face of limited resources. This calls for prudential management as defined above. It was Franklin D, Roosevelt one-time President of

United States of America, who in 1937 said that "a government without good management is like a house built on sand". There can be no good government in the local government system if financial resources are not judiciously and prudentially managed.

Strategies For Prudential Financial Management In Local Government Administration

For effective and effective management of local government financial resources, the author suggests the following strategies:

- The budget must be used both as planning and as control mechanism. As earlier highlighted, the budget as planning tool anticipates the future, ensures systematic and prioritized allocation of resources and defines strategies for accomplishment of organizational objectives. As instrument of control, the budget provides tangible and readily measurable standards against which actual performance is determined to establish variances or deviation from planned targets. For effective use of budget as cost control device, there must be regular (monthly or quarterly) budget reports and periodic, review and adjustments in the light of changing circumstances. Discrepancies and deviations highlighted by budget reports must be addressed and rectified.
- There must be budgetary discipline. As much as possible the budget must be used as operational guide. Limits imposed in the budget must be respected and expenditures not provide in the budget must be avoided.
- The legislative arm of local government administration must be functionally independent. This will ensure effective system of checks and balances. Undue influence, interference or usurpation in any form must be avoided.
- There must be respect for bureaucratic processes and hierarchical administrative functional ism. Vouchers for example must pass through their normal route for approval and payment.
- The internal auditor must be knowledgeable, bold, efficient, and dedicated to his duties. His functions must not be compromised.
- Local Government accounts should be subjected to external audit as least once a year and follow up reviews must be installed to ensure compliance with audit report and recommendations.
- There must be effective operational controls. Records must be accurately kept and up-to-date. All local government vehicles and equipment must be properly used and kept in good usable form through regular maintenance. The use of consumable working materials must be properly monitored and common sources of leakages including pilferage must be blocked.
- Above all, local government executives must manifest transparency and accountability in the discharge of their functions.-They must live by example and avoid excessive flamboyance and acts that portray reckless spending.

Conclusion

We can summarily state that the greatest legacy any local government administration can bequeath to posterity is good government, concrete development-oriented projects and sensitivity to the feelings of the common man

Ability to provide good government, meaningful projects and programmes that positively impinge on socio-economic life of the people depends on prudence and transparency in resource utilization and a good sense of responsibility on the part of key operators. The budget if properly drawn and religiously implemented can serve as an invaluable guide in ensuring prudential financial management in local government administration.

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