

An Overview of Accounting in the Nigerian Public Sector

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Introduction

The public sector in Nigeria includes the federal government, the 36 states, the 774 local government councils, all government corporations, commissions and institutions.

This paper¹ highlights the main differences between accounting in the public sector and the private sector. In doing this, attention is first drawn on the main differences between the two different sectors that can assist us in our understanding of some differences that exist between accounting in the public sector and that of private sector. However, because the public sector institutions are not homogenous, the two types of public sector institutions that are of interest to this paper are identified and briefly discussed.

After this, the paper discusses the roles of government in the society before rounding up with what the research challenges have been in the area of Public Sector accounting.

1.1 Non-Profit Organization

According to Anthony (1978) a non-profit organization to which a public sector organization belongs is characterized by two main features which are:

- i. It does not operate for the primary purpose of making profit.
- ii. Any income raised or asset acquired cannot be distributed; to or benefit members, directors, or officers of the organizations. Even in the event of the dissolution of such an organization the proceeds realized revert to the state and not to any particular individuals.

Two Types of Non-Profit Organizations

Anthony (1978) went on to classify non-profit organizations into two broad categories.

i. Type A Non-Profit Organization

This is a non-profit organization whose financial resources are obtained entirely or almost entirely from the sale of goods and services. It may be termed a government business enterprise or a parastatal organisation. All the 31 corporations initially listed in the Schedule to Fiscal Responsibility Act before seven of them were privatised and reproduced in Appendix 1 are Type A public sector institutions. Although many of them engage in business type of activities, their conditions for doing business in Nigeria are not the same as private sector business organizations. Before any business in the private sector can operate in Nigeria, such business must first register with Corporate Affairs Commission,

¹ This paper is the first chapter of the book by the authors: **Theory and Practice of Government Accounting in Nigeria** (2011). It is reviewed later in this issue of the Journal.

Abuja. Government corporations in Nigeria are not required to register with Corporate Affairs Commission. They are all created by Acts of Parliament and consequently no public funds can be spent on any government corporation that has not been created by law.

Type B Non-Profit Organization

This is a non-profit organization that is financed from sources other than sale of goods and services. Such an organization is financed primarily through taxes raised by the government. Within the Nigerian context, Nigerian Police force is an example of type B non-profit organization.

1.2 Profit Oriented Organizations Vs Non-Profit Organizations

The dominant purpose of a profit oriented organization is to earn profit. The success of such an organization can be measured to some extent by the amount of profit earned in relation to the assets of the organization. An investor who is interested in such an organization can look at its financial statements for the relevant information on the extent of fulfillment of the profit goal of the company. On the other hand, the dominant purpose of a non-profit organization is to render socially desirable specific service to the society at a reasonable cost. While profit is a good measure of performance of a profit oriented organization; this cannot be said of a non-profit organization even in the case of Type A organization that raises its financial resources predominantly through the sale of goods and services. A high excess revenue over expenses in a non-profit organization, is not enough evidence that the organization is doing well because it is less subjected to market forces than a profit oriented organization in a competitive industry.

This means that while a profit oriented organization is expected to produce goods at the selling price that are in line with what the market is willing to pay or go out of business, a non-profit organization has no such danger signal because of the unique circumstances in which the services are priced. Power Holding company of Nigeria (formerly Nigerian Electric Power Authority, NEPA) is a Type A Non-Profit Organization in Nigeria that as at the time of going to press is a monopolist in its own area of operation and it is not likely to be bothered about going out of business because of consumers revolt against the prices charged for its services. Thus, in the Non-Profit Organization, there is no satisfactory single overall measure of performance that is analogous to the profit measure in the private sector. In view of the importance of profit in performance measurement in the private sector, the public is more interested in the annual reports of companies than their annual budgets which are virtually internal documents of the companies.

On the other hand, the budget documents are of more interest to the public than the government annual financial reports (which they hardly care about). This is because the annual budget document communicates to the different stake holders the intended beneficiaries of the resource allocation for the financial year.

Another important area of difference is output measurement. In the private sector, especially in the manufacturing industry it is easy to determine the output of the organization. In the case of public sector especially Type B institutions, it is difficult to measure the output of the organization. This is because the core of government activities centers on provision of public goods like defence, diplomacy and law and order where output cannot be quantified. For example, how do we measure the output of Ministry of

Foreign Affairs that is involved with diplomacy or the military that is involved with protecting the territorial integrity of Nigeria?

Failure to recognize the problem of output measurement was one of the reasons why Nigerian government had unrealistic expectation from Planning Programming and Budgeting System (PPBS) which it introduced in 1980.

According to the former Adviser to the President, on Budget Affairs, Chief Akinyele (1981:19).

“For the avoidance of doubt often expressed ... almost every cost can be measured in terms of output, every activity will respond to quantifiable measurement”

If output cannot be determined how will “every cost be measured in terms of output”?

However, the problem of output measurement has not discouraged many countries from trying to develop some measures of performance that lay emphasis on outcome² rather than output. This is subject to the observation of Talbort et al (2000:4) that what

“governments say they are doing on performance measurement is not always the same as what has actually been implemented.”

1.3 Nature of Government Accounting

As indicated earlier in the paper, the primary purpose of a private sector organization is to make profit. As a result of this, the focus of accounting in private sector is to enable the business to determine the profit of the business over a given period. However, because government ministries are not run for the purpose of profit making, many factors influence government accounting such as the role of government in the different fields like health and education and the methods set by government to achieve its set objectives. The focus of accounting in government is the determination of how much money was received and the sources of such receipts, how much money was spent and for what purposes and what remains after meeting the financial obligations. This then means that government accounting is more concerned with information gathering that will enable government to prepare Receipts and Payments accounts as it is the case with Clubs and Societies rather than the profit and loss account of a private sector business. This point is reinforced by the fact that the Accountant-General of the Federation is referred to as the “Chief Accounting Officer for the receipts and payments of the government of the federation³.

As a result of more interest in receipts and payments account, the government accounting practice that evolved over the years focused on cash receipts and disbursements on the basis of budgetary headings to reveal the balances available at a given time under various heads and sub-heads of votes⁴.

² Outcome measure is concerned with the comparison of the results of a program activity with its intended purpose. This is to determine the impact of government policies on social conditions focused upon by government.

³ Federal Republic of Nigeria Financial Regulation, Regulation 107(a) January 2009 edition.

⁴ For the purpose of expenditure control, categories of government expenditures are coded and given expenditure heads. Expenditure head therefore represents a major expenditure category. Under each head are contained small groups of items called Sub-heads.

This therefore means that the basis of accounting in government is normally the cash basis (or modified cash) rather than the accrual basis of the private sector⁵. Under the cash basis, the government revenue is recorded and accounted for when cash is received and expenditure is incurred when cash is paid irrespective of the accounting period in which the benefit is received or the service rendered. This therefore means that the amount incurred by the government to purchase official car will be treated the same way as salaries paid to the workers in that both will be written off as part of expenditure for the period the costs were incurred.

Since the payments made for the acquisition of fixed assets by the government are written off in the year of acquisition irrespective of the useful life of the fixed assets, it follows that fixed assets like buildings and motor vehicles which will normally be seen on the balance sheet of a private sector business will be absent in the case of government. This explains why, for example, the Accountant-General's Statement No. 2 which is a statement of assets and liabilities of government does not indicate anything on the fixed assets of the government. Since fixed assets are not capitalized, it follows that there is no room for depreciation in government accounting system that uses cash basis of accounting.

It should also be pointed out that since revenue is recognized only when cash is received, debtors as it is known in the private sector will be absent from government financial statements (but will, of course, be recorded).

In the private sector, accrued expenses are recognized as current liabilities and taken into consideration in determining the total debt of the organization. Government departments do not recognize current liabilities thereby giving a wrong impression of total government debt (if the liabilities are significant).

One other point to discuss on the topic is the role of fund accounting in government. In the case of a private sector business, the whole of the business is treated as an accounting entity. This implies that accounting measures and reporting are carried out in the name of one single entity. As a result, unless an asset is set aside for a specific purpose (such as replacement of a fixed asset) the organization's resources are available as a pool which can be used in any area of its operation to achieve the main goal of profit making. Thus, the pool of resources can be used to acquire fixed assets, pay wages or pay debt. However, in the case of the government that has diversity of goals and functions to carry out, the resources are not available as a pool to be spent on just any area of government operation at the discretion of the officials. There are often restrictions on how available resources may be utilized on individual areas of government operation. The mechanism for carrying out the restriction is the fund accounting. Under this arrangement, separate funds are provided for carrying out different specific functions of government. A fund is the total amount of money set aside for a specific purpose. Each fund is then accounted for separately, so that the fund is the accounting entity on which accounting reports are based. Thus fund accounting can be defined as a method of accounting, which treats a fund as the accounting entity on which accounting reports are based rather than the organization as a whole. It should be remembered that the purpose of fund accounting is to ensure that the government organization uses the resources provided for each fund only for the purposes designated for the fund.

⁵ This is subject to the fact of the move to accrual basis of accounting in some countries.

Thus, the fund of motor vehicle advances can only be used to advance vehicle loans to the civil servants and money for other funds cannot be used by them as vehicle loans.

In the private sector, the technique of flexible budgeting has been developed to set standard for cost in the light of output achieved. For example, if Y is the cost allowed and X is the output achieved, a predictive model of cost with output may be given as

$$Y = N5,000 + 5x.$$

If output is 1000 units, then expected cost is N10,000. By the same token if one is given a budget of only N8,000, the output expected from the budget is 600. The absence of output measure in the delivery of public goods means that such technique cannot be used in a typical government department. In the absence of a predictive model, there is no way (for example) that we can know precisely as above, the impact on crime rate of increases/decreases in police funding.

1.4 The Role of Government in the Society

Adam Smith in the *Wealth of Nations* identified the three basic duties of the state as:

- i. protection of the citizens from external aggression
- ii. protection of the citizens from other members of the country and administration of justice.
- iii. engagement in activities that are of benefit to the society as a whole because they are not profitable for individual efforts⁶.

Thus, because government gets the problems that the private sector “can’t or won’t handle” (Taylor of OMB Watch⁷, 2,000:4) there is the need for government involvement in the provision of public goods.

A public good is characterized by two main features

- i. the consumption of the goods by one person does not prevent anyone else from consuming it (non – rivalry concept).
- ii. it is impossible to prevent people from using or benefiting from it (non – exclusion concept).

A very good example of this in Nigeria is the street light (wherever it exists). Other examples of public goods include security, defence and public roads. However, it is not only the citizens alone that the government is supposed to provide security for but also for business organizations such as the banks and the oil producing companies as reflected in the crisis in Niger Delta region of Nigeria. Government must also try to control the activities of the business organizations, through the setting up of various regulatory agencies.

Thus the government is expected to provide enabling environment to business organizations by ensuring reliable and efficient electricity supply, water, good roads and effective security among others. However, the extent of involvement of government in society has always been a constant source of controversy.

⁶ See Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* edited by E. Cannan. The Modern Library, New York, 1965.

⁷ OMB Watch is a non-profit Research and Advocacy Organization (in USA) that seeks to promote government accountability and citizen’s participation in government.

To Friedman and Friedman (1980) the need for government to engage in activities that are of benefit to the society as a whole because they are not profitable for individual efforts has been used as an excuse for unlimited extension of government power in the economic activities even though government spending is not a requirement for economic growth. To Friedman and Friedman even government's involvement with social security runs counter to economic growth because an attempt to divert funds from the rich to the social services tend to reduce the potential fund for investment.

However, to O'Connor (1973), government spending on economic and social matters is justifiable. In O'Connor's view while the state should assist in the process of capital accumulation through the provision of infrastructure and manpower, it should also cater for the less privileged members of the society, especially the unemployed if there is to be social harmony. To O'Connor, unemployment benefit (where it exists) is a necessary expenditure by the ruling class to pacify and control the surplus population which the capitalist system cannot absorb.

In the case of Nigeria, on gaining independence in 1960, the country's leader inherited socio-economic structures that they found unsuitable for economic development of the country. According to Nwankwo (1991) as far back as the 1930s, the United Africa Company (UAC) alone controlled over 40% of Nigerian import-export trade a situation the Nationalists did not find funny.

“It is not therefore surprising that economic nationalism was the dominant factor in government intervention and consequent expansion of public sector in economic management in Nigeria.... The expatriates dominated the scene and crowded out the indigenous sector which bitterly complained and cried out very loudly against the apparent domination and discrimination.”
(Nwankwo, 1991:11)

Thus, at the time of independence, the country had to use the “instrumentality of the public sector” to address the socio-economic problems of the country. The government was subsequently helped in its efforts by the oil wealth of 1973 – 1980. Such wealth gave the government the impression that it could play increasing role in the economy. This is reflected in the substantial role the government was expected to play in the 1981 – 1985 Fourth National Development Plan. This role as measured by the amount of money the government was expected to spend on capital investment in the country is illustrated in Table 1.1

Table 1.1
Projected Capital Investments in Nigeria Fourth National Development Plan 1981 – 1985

| Funding Body | Investment in Billion Naira | Percentage of the Total |
|-------------------------|-----------------------------|-------------------------|
| Federal Government | 42.5 | 51.8 |
| States and Local Govt. | <u>28.0</u> | <u>34.2</u> |
| Total Govt. Investments | 70.5 | 86.0 |
| Private Sector | <u>11.5</u> | <u>14.0</u> |
| Total | <u>82.0</u> | <u>100.0</u> |

Source: Page 9 of Outline of the Fourth National Development Plan.

From Table 1.1, the total government investment was expected to be 86% of the total investment plan out of which the federal government proposed investment amounted to 51.8%. Only 14% of the total

investment was expected from the private sector. The government was therefore expected to play a more important role in the economy than the private sector.

However, by the end of 20th century, the economy has become private sector-led and market-oriented with government primary role centered on ensuring.

“in co-operation with the private sector; the urgent creation of adequate and efficient infrastructure particularly of energy, telecommunications, water and financial services, to bring about a positive and internationally – competitive environment for economic activities.”⁸

More recently, there has been a growing realization that the state has a wider role to play in the form of a developmental state (UN Economic Commission for Africa and AU 2011).

1.5 Research in the Area of Public Sector Accounting

Until 1980s, accounting academics did not show enough interest in public sector accounting. According to Perrin (1981:297)

“Less than one percent of the papers published in the two British academic accounting and finance journals during the decade of the 1970s were concerned specifically with accounting or finance in the public sector institutions.”

In response to this neglect, a journal to cater solely for public sector institutions, *Financial Accountability and Management* was launched in 1985 in Britain.

In the field of government budgeting, the first journal devoted specifically to the area, *Public Budgeting and Finance* was launched in 1981 followed by *Public Budgeting and Financial Management* (now called *Journal of Public Budgeting, Accounting and Financial Management*) “in order to reflect its cross-disciplinary nature” in 1989 while OECD *Journal of Budgeting* made its debut in March 2001.

Even though there have been some interest in public sector accounting recently, Khumalawala (1997) is of the view that most researchers have virtually ignored the governmental accounting systems of developing countries. This is in spite of the fact that developing countries not only have the fastest growing economic segment but also tend to have very large, dominant government entities.

One of the reasons for the past neglect of research in the public sector institutions is provided by Hopwood (1980:185)

“Issues of both practical and theoretical significance have not been investigated because they have not been seen as being compatible with current methodological procedures and approaches.”

The methodological approach referred to by Hopwood is the rigorous quantitative analysis which McCosh et al (1981:7) claimed “has thrown out the baby of relevance in the search for an unimpeachable hygienic variety of methodological bathwater.”

Perrin (1985:14) also complained that in his editorial work in the journal devoted to the private sector

⁸ Federal Government of Nigeria: 2001 Budget Call circular Page 2.

“ a high proportion of academic research... is based mainly on cranking ‘published’ and ‘randomly’ collected numbers through statistical tests and computer programs with little evidence of in-depth research or close insight into real-life problems of the institutions whose behavior is being studied.”

Tomkins (1981) probably had this type of complaint in mind when he called for research in the public sector accounting that places greater reliance upon the analysis of qualitative rather than quantitative data. Tomkins then warned that in the case of public sector research

“The path has risks for accounting researchers trained in positivistic, quantitative research methods. When ice meets fire, one or the other or both vanish.” (Tomkins, 1981:335).

1.6 Problems Of Doing Research On Government Accounting In Nigeria

However, it is not just the problem of methodological approach that a researcher on government accounting in a country like Nigeria has to cope with but also having access to the data. In an earlier comparative study of planning and budgeting in the third world countries by Caiden and Wildavsky (1974) only two African countries (Ghana and Uganda) were included in the sample of 12 countries partly because

“it was more difficult to interview in Africa than elsewhere.” (Caiden and Wildavsky, 1974:xiii).

The observation of Caiden and Wildavsky is still relevant in Nigeria thirty six years after (2010). In spite of the fact that the Phillips Committee (2000) was a government commissioned one, it had difficulties collecting the required data.

For example, as at the deadline on January 31, 2000 for the submission of the required data, “only 5 out of over 30 ministries had submitted memoranda and only one Ministry had submitted its survey return on current financial commitments”(Phillips Committee; 2000:3).

Until 2004, some relevant information on Nigerian government accounting was not available on the Internet. Even the one provided was very scanty. The only relevant information that could be obtained from the websites of Ministry Of Finance, Accountant-General of the Federation and the Budget Office of the Federation (as at July 2005) was on monthly revenue allocation (from the Federation Account) to each of the three tiers of government from May 1999 (when the country returned to democratic rule). There was virtually nothing on government expenditure. The only relevant information for the purpose of this book was on Development fund General Warrants for the First and Second quarters of 2004 financial year.

However, anybody interested in doing research on government accounting in Nigeria needs not be discouraged as things have started to improve. As a result of ongoing reform on financial management at government level especially the enactment of Fiscal Responsibility Act 2007, government financial records are now relatively easier to come by. For example, the audited and more user friendly Federal Government Financial statements for 2008 were ready in 2009 and now available on the website of the

Office of Accountant-General of the Federation. In addition, the four quarterly reports of 2009 budget implementation were on the website of the Budget Office of the Federation as at July 2010.

Finally, it is worthy of note that even though the Institute of Chartered Accountants of Nigeria (ICAN) was given government backing by an act of Parliament in 1965, Government Accounting as a subject was not examined until 1992 and it still only forms one of the papers in the ICAN examinations. However, ICAN is working with CIPFA to develop a new public sector accounting qualification.

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APPENDIX 1

List of Corporations, Agencies and Government-Owned Companies that Come Under the Provisions of Fiscal Responsibility Act (FRA)

1. Nigerian National Petroleum Corporation
2. Nigeria Deposit Insurance Corporation
3. Bureau of Public Enterprises
4. National Agency for Science and Engineering Infrastructure
5. Nigerian Social Insurance Trust Fund
6. Corporate Affairs Commission
- *7. National Clearing and Forwarding Agency
- *8. Nigeria Unity Line
9. Nigeria Airspace Management Agency
10. Nigerian Shippers Council
11. National Maritime Authority
12. Raw Material Research and Development Council
13. Nigerian Civil Aviation Authority
14. National Sugar Development Council
15. Nigerian Postal Service
16. Nigerian Ports Authority
17. Federal Airport Authority of Nigeria
- *18. Nigeria Mining Corporation
- *19. Nigeria Re-insurance
- *20. Nigerdock Nigeria Plc
21. Securities and Exchange Commission

- *22. National Insurance Corporation of Nigeria
- *23. Nigeria Re-insurance Corporation
- 24. Nigeria Telecommunication
- 25. National Automotive Council
- 26. Nigerian Tourism Development Corporation
- 27. National Communication Commission
- 28. National Agency for Food & Drug Administration & Control
- 29. Nigerian Customs Service
- 30. Federal Inland Revenue Service
- 31. Central Bank of Nigeria

** Any other corporation, agency or government owned company that may be included by Minister of Finance through a local notice.

* The seven corporations that have since been privatized and hence the provisions of FRA do no longer apply.

(No additional corporation has been added to the list as at the end of 2011)