

67936

Report No. xxx

NIGERIA
Lagos Rolling Public Expenditure Review 1

May 2010

Poverty Reduction and Economic Management, AFTP3
AFCW2
Africa Region

CURRENCY EQUIVALENTS
(Exchange Rate Effective February 28, 2010)

Currency Unit = Nigerian Naira (NG)
NG1 = US\$0.00659
US\$1 = N147.29

FISCAL YEAR

January 1 to December 31

ABC	Alpha Beta Consulting
ASCON	Administrative Staff College of Nigeria
DMO	Debt Management Office
EBS-RCM	Electronic Banking System of Revenue Cycle Management
EIU	Economic Intelligence Unit
EXCO	Executive Council
FAAC	Federal Account Allocation Committee
FDMO	Federal Debt Management Office
FGN	Federal Government of Nigeria
FM	Financial Memorandum
FR	Financial Regulations
FSA	Fiscal Sustainability Analysis
GDP	Gross Domestic Product
GSDP	Gross State Domestic Product
ICPC	Independent Corrupt Practices and other Related offences Act
IDA	International Development Association
IGR	Internally Generated Revenue
ISA	Investment and Securities Act
ISPO	Irrevocable Standing Payment Order
LAS	Lagos State
LASG	Lagos State Government
LASEEDS	Lagos State Economic Empowerment and Development Strategy
LSPAR	Lagos State Procurement Assessment Review
LG	Local Government
LGA	Local Government Administration
LIRS	Lagos Internal Revenue Service
LSFAA	Lagos State Financial Accountability Assessment
NGN	Nigerian Naira
MDAs	Ministries, Departments, and Agencies
MEPB	Ministry of Economic Planning and Budget
MTB	Ministry Tender Board
MTBF	Medium Term Budget Framework
MTEF	Medium-Term Expenditure Framework
MTFS	Medium Term Fiscal Strategy
MTSS	Medium Term Sector Strategy
PE	Procuring Entity
PFM	Public Finance Management
PPP	Public Private Partnership

PSSDC	Public Service Staff Development Centre
PTB	Parastatal Tender Board
SEEDS	State Economic Empowerment and Development Strategy
SCB	State Consultancy Board
STB	State Tender Board
TB	Tender Board
TPA	Ten Point Agenda

Vice President:	Obiageli K. Ezekwesili
Country Director:	Onno Ruhl
Sector Manager:	Jan Walliser
Task Team Leader:	Khwima Nthara
Team Members:	Edith Kikoni, Lev Freinkman, Bayo Awosemusi, Winston Cole

TABLE OF CONTENTS

ACKNOWLEDGEMENTS	VI
EXECUTIVE SUMMARY	VII
CHAPTER 1: BACKGROUND	2
INTRODUCTION	2
OVERVIEW OF NIGERIA'S FISCAL FEDERALISM	3
CHAPTER 2: FISCAL PERFORMANCE AND SUSTAINABILITY	8
STATE REVENUE TRENDS	8
STATE EXPENDITURE TRENDS	11
FISCAL BALANCE, SUSTAINABILITY, AND RISK ANALYSIS	15
CONCLUSION AND RECOMMENDATIONS	22
CHAPTER 3: PERFORMANCE OF THE BUDGET SYSTEM	23
LEGAL FRAMEWORK	23
BUDGET PLANNING	23
BUDGET EXECUTION	27
BUDGET MONITORING AND EVALUATION	28
EFFICIENCY OF THE PUBLIC INVESTMENT SYSTEM	30
CONCLUSION AND RECOMMENDATIONS	34
CHAPTER 4: REVIEW OF THE PUBLIC PROCUREMENT SYSTEM	36
LEGISLATIVE AND REGULATORY FRAMEWORK	36
INSTITUTIONAL FRAMEWORK AND MANAGEMENT CAPACITY	37
PROCUREMENT OPERATIONS AND MARKET PRACTICES	39
INTEGRITY AND TRANSPARENCY OF THE PUBLIC PROCUREMENT SYSTEM	43
CONCLUSION AND RECOMMENDATIONS	45
ANNEXES	46
REFERENCES	50

TABLE OF TABLES

Table 1: Summary of Findings and Recommendation	ix
Table 2: Nigeria Fiscal Federalism: Distribution of Responsibilities for Taxation	4
Table 3: IGR distribution by percentage, 2005-2008	9
Table 4: Lagos State Finances, 2003-2009	16
Table 5: Lagos State Public Debt Outstanding	17
Table 6: Limits on Sub-national Borrowing in Selected Countries	18
Table 7: Actual Receipts in Percentage of Budget Forecast, 2005-2008	24
Table 8: Budget Spending Performance, 2005-2008	28
Table 9: Submission times for Financial Statements and Audit Report	30
Table 10: Agreement Fee Percentages	41
Table 11: Lagos Baseline Fiscal Projections, 2009-2018	47
Table 12: Lagos Projections for Key Fiscal and Debt Indicators 2008-2018 under Alternative Scenarios	48
Table 13: Lagos FSA Sensitivity Analysis: Assumptions for Alternative Scenarios	49

TABLE OF FIGURES

Figure 1: Lagos GDP Breakdown (2000-2007 average).....	2
Figure 2: Revenue Trends, 2004-2008.....	8
Figure 3: Actual Expenditure Trends, 2004-2008	11
Figure 4: Composition of Total Expenditure by Functional Classification, 2007-2008.....	13
Figure 5: Composition of Total Expenditure by Economic Classification, 2007-2008.....	13
Figure 7: Main expenditures within general administration and economic affairs.....	14
Figure 8: Overview of MTEF Components	25
Figure 9: Composition of Capital Spending by Functional Classification, 2005 – 2008.....	31
Figure 10: Lagos Fiscal and Debt Indicators under Alternatives Scenarios, 2008-2018.....	46

ACKNOWLEDGEMENTS

This report is the first in a rolling series of Public Expenditure Reviews on the State of Lagos. The team is grateful for the support received from the Lagos State Government during the review, notably from the Commissioner of Economic Planning and Budget, Honorable Ben Akabueze, the Commissioner for Finance, Honorable Rotimi, the Director of Budget, Mr Bayo Sodade, and the Director of Planning, Mr Emmanuel Oyegoke.

The report is the product of a team composed of World Bank Staff and external consultants, led by Khwima Nthara. Other team members include Edith Kikoni, Lev Frenkman, Volker Treichel, Pierre Strauss, Bayo Awosemusi, Mary Asanato, Akinrinmola Akinyele, Winston Cole, Phebian Omanukwue, Rita Itoro-Godfrey, and Aisha Kaga. Background Papers for the report were prepared by Edith Kikoni and Lev Freinkman (Fiscal Performance and Fiscal Sustainability), Olaseni Ogunsanya (Public Finance Management Assessment), and Rogati Kayani (Procurement Assessment Review)

Peer reviewers were Hassan Zaman and Carlos Cavalcanti.

EXECUTIVE SUMMARY

1. **This review provides an analysis of the fiscal performance and sustainability of the State of Lagos, performance of the budgeting system and of the public procurement system.** It is the first in a planned rolling PERs for Lagos State. The analysis finds that the State's fiscal policy is broadly sound and that its fiscal program is sustainable in the medium term, but only if certain conditions prevail. It also finds that the performance of the budget system has been mixed, and that the public procurement system is beset with many weaknesses. In spite of weaknesses in the budget and procurement systems, the review observes that various reforms are currently underway to address the weaknesses. Finally, the report offers a number of recommendations on the way forward.

Fiscal performance and sustainability

2. **Lagos State has enjoyed strong revenue growth in recent years which has triggered rapid expenditure expansion, especially on the capital budget.** The growth in revenue has been as a result of high world oil prices, a growing economy, increased federal transfers, and most significantly, increased internally generated revenues (IGR). Monthly IGR for Lagos State has increased from NGN0.6 billion per month in 2002 to NGN15 billion in 2009. Overall, total IGR collections have more than doubled in real terms since 2004, from 2.4 percent to 3.5 percent of GSDP. With increased revenues, the Government has been able to expand its total expenditure, mainly on the capital budget in an effort to improve the state of infrastructure and hence try to keep up with the needs of an expanding population. Between 2005 and 2008, total expenditure as a percentage of GSDP rose from 4.2 percent to 7.2 percent. During the same period, the share of capital expenditure increased from 19 percent to 56 percent.

3. **The State's fiscal policy is broadly sound and its fiscal program is sustainable in the medium term.** The Government continues to undertake the necessary reforms for increasing IGR. The Government has been maintaining a positive operating balance in spite of pressures to increase wage related recurrent expenditures. Nevertheless, the expanded public investment program has resulted in increased borrowing. As a result, the debt stock-to-state revenue ratio, rose from 27 percent in 2006 to 70 percent in 2008, which is above the statutory limit of 50 percent under the Investment and Securities Act. The state has been in full compliance with the external debt service indicator limit of 40 percent of federal allocations. Between 2003 and 2008, external debt service payments averaged at 35 percent of federation allocations. Overall, debt service payments (both domestic and external) remain within manageable limits at 10.3 percent of state revenues. A fiscal sustainability analysis finds that the State's fiscal policy is sustainable in the medium term provided world oil prices do not decline significantly, revenue growth remains strong, contingent liabilities are in check, and that the State has access to concessional financing.

4. **Going forward, the review recommends that the state undertake the following measures to ensure that the fiscal program remains robust:** (i) Strengthen efforts to increase property tax revenues by among other things, exploring options for increased land use charges (ii) Explore options for reducing the cost of tax collection but without compromising the

effectiveness and efficiency of the system. In this context, a review of the consultancy costs is warranted, (iii) Undertake a detailed review of expenditure on general administration in order to determine if current levels are reasonable. The review would need to pay special attention to the travel budget, and (iv) Undertake measures to improve the State's capacity to manage debt. Areas of improvement should include management of debt data, including contingent liabilities.

Performance of the budget system

5. **The review finds that the budget system in Lagos has performed well in a number of areas but that weaknesses remain in other areas.** There is broad based participation in the budget preparation process with the State House of Assembly able to effectively influence the substance of the budget. At the broad level, the budget seems to be aligned to the State's development priorities as contained in its ten-point agenda. There has also been some improvement in the monitoring of budget implementation. Further, the introduction of Oracle Financial System has improved timeliness in the production of financial reports and subsequently, of audit reports. Coverage of internal and external auditing has also significantly improved. On the weaker side, the State of Lagos is still operating without modern PFM laws. Reliance is still on the Federal Constitution and administrative guidelines. Second, internal revenue forecasting remains a challenge, which leads to unrealistic budgets. Third, budget preparation is still done within a one year planning horizon and with no mechanism for ensuring that budgets are aligned to the State's strategic priorities at a disaggregated level. Fourth, in spite of improvements in the monitoring of budget implementation, huge discrepancies between the actual and approved budget undermine the credibility of the budget. Fifth, financial and audit reports conform to national standards but still fall below international standards in certain respects. And finally, follow-up on audit recommendations is weak.

6. **The capital budget system is still underdeveloped.** While most projects are broadly in line with the State's strategic policy priorities, the institutional arrangement currently in place for conducting formal appraisals of projects needs strengthening. Once admitted into the budget, implementation has been slow, although Lagos's performance has been better than most states. The system provides for adjustments to be made to projects although these adjustments do not seem to follow specific guidelines. Finally, there is no formal ex-post evaluation of projects, and no central registry to keep a record of all assets.

7. **The review also finds that the State of Lagos is currently implementing several reforms to correct the weaknesses in its budget system.** Efforts are underway to enact new legislation to govern public financial management. The state has also introduced a multi-year perspective to budgeting and has prepared medium-term sector strategies that will improve alignment of the budget to the state's strategic priorities at a more disaggregated level. The capacity of the Ministry of Economic Planning and Budget to forecast revenues and coordinate budget planning and preparation is also being strengthened with the establishment of an Intelligence Economic Unit and the deployment of more planners in the Budget Division and in MDAs.

8. **In light of the review's findings and reform efforts already underway, the report suggests the following recommendations for improving the budget system further:** (i) Strengthening the capacity of the newly formed EIU in undertaking revenue forecasts, (ii) further

upgrading the MTSSs by strengthening their link to service delivery and incorporating recurrent expenditures (iii) Putting in place a mechanism for developing MDA-level work plans that would help them translate MTSSs into operational annual budgets, (iv) Taking steps to utilize all the functionalities of the Oracle system, (v) Strengthening current measures for dealing with under-performance of the budget in general and of capital projects in particular, (vi) Developing a mechanism for ensuring follow-up on audit recommendations, and (vii) Strengthening the capacity of the institutional framework for undertaking formal project appraisal, monitoring, evaluation, and maintenance of records for all State assets created.

Review of the public procurement system

9. **The review finds that the procurement system in Lagos is generally very weak.** The absence of a state procurement law is a major handicap that has led to reliance on administrative guidelines that do not conform to best practice. In spite of Government efforts to curb procurement related corruption, the high centralization of the procurement process renders it inefficient and susceptible to perceptions of corruption and political interference. It is also clear that capacity challenges at the technical level are immense and responsible for current procurement practices.

10. **In this context, the following recommendations are suggested:** (i) Finalization of the Procurement Bill and ensuring that it conforms to international best practice. One such best practice needs to be decentralization of the procurement function to Procuring Entities (PEs) in ministries and parastatals, and the establishment of a state-level office with regulatory and oversight functions, (ii) Speeding up the process of passing the Procurement Bill into law, and (iii) Developing and implementing a comprehensive procurement reform program based on the new procurement law. The reform program must include a capacity building plan based on a comprehensive assessment of training and material support needs.

Table 1: Summary of Findings and Recommendation

Review Finding	Recommendation	Timeline	Responsible Institution(s)
Fiscal performance and sustainability			
In-spite of significant increases in IGR in recent years, there is still scope for further increases	Strengthen efforts to increase property tax revenues by among other things, exploring options for increased land use charges and other taxes	Short to medium term	Lagos In-land Revenue Service, Lands Bureau, & Lands Records Company
The cost of collecting tax is high	Explore options for reducing the cost of tax collection but without compromising the effectiveness and efficiency of the system. In this context, a review of the consultancy costs is warranted	Short-term	Ministry of Finance
Expenditures on general administration are relatively very high	Undertake a detailed review of expenditure on general administration in order to determine if current levels are reasonable. The review would need to pay special attention to the travel budget	Short-term	Ministry of Economic Planning & Budget
There are weaknesses in debt management capacity and little is known about the extent of contingent liabilities	Undertake measures to improve the State's capacity to manage debt. Areas of improvement should include management of debt data, including contingent liabilities	Short-term	Debt Management Office & State Treasury Office

Performance of the budget system			
Revenue forecasts are usually off the mark by a wide margin	Strengthen the capacity of the newly formed EIU in undertaking revenue forecasts	Short to medium-term	Ministry of Economic Planning and Budget
MTSSs are not clearly linked to service delivery and focus only on capital expenditures	Further upgrading the MTSSs by strengthening their link to service delivery and incorporating recurrent expenditures	Short to medium-term	Ministry of Economic Planning and Budget
MTSSs are not significantly utilized by MDAs to prepare annual budgets	Put in place a mechanism for developing MDA-level work plans that would help them translate MTSSs into operational annual budgets. There is also need to strengthen even further stakeholder consultations currently being employed to determine priorities for the budget.	Short-term	Ministry of Economic Planning and Budget
Some of the modules of the Oracle financials are not being utilized	Take steps to utilize all the functionalities of the Oracle system	Short to medium-term	Ministry of Science and Technology & State Treasury Office
Execution rate of the capital budget is very low	Strengthen current measures for dealing with under-performance of the budget in general and of capital projects in particular	Short to medium-term	Ministry of Economic Planning and Budget & Office of the Governor
There is no evidence of follow-up on audit recommendations made by the Public Accounts Committee of the State House of Assembly	Develop a mechanism for ensuring follow-up on audit recommendations	Short-term	Office of the Governor
The institutional arrangements for undertaking investment appraisal, monitoring, evaluation, and maintenance of capital projects are not effective	Strengthen the institutional framework for undertaking formal project appraisal, monitoring, evaluation, and maintenance of records for all State assets created	Short to medium-term	Ministry of Economic Planning and Budget & Ministry of Finance
Review of the public procurement system			
Procurement Bill falls short of international best practices	Finalization of the Procurement Bill and ensuring that it conforms to international best practices.	Short-term	State Attorney General's Office & State Tenders Board
Procurement Bill is yet to be passed into law	Speeding up the process of passing the Procurement Bill into law	Short-term	State Attorney General's Office
Procurement system has many areas of weaknesses that require reform	Developing and implementing a comprehensive procurement reform program based on the new procurement law. The reform program must include a capacity building plan based on a comprehensive assessment of training and material support needs	Short-term	State Tenders Board & Ministry of Economic Planning and Budget
Absence of information on unit costs	Undertake an analysis of unit costs on major projects across sectors and compare with other major cities of the world	Short to medium-term	State Tenders Board & Ministry of Economic Planning and Budget

Scope of future PERs

11. **In light of the findings and recommendations of this PER, there will be need for future PERs to conduct detailed analyses in the following areas:** (i) The scope and size of contingent liabilities and their likely impact on the state's medium to long-term fiscal sustainability, (ii) Public expenditure on general administration with a view to assessing if the

levels are reasonable by international standards (iii) The relationship between sector expenditures and outcomes in key sectors such as transportation, environment, education, and health

CHAPTER 1: BACKGROUND

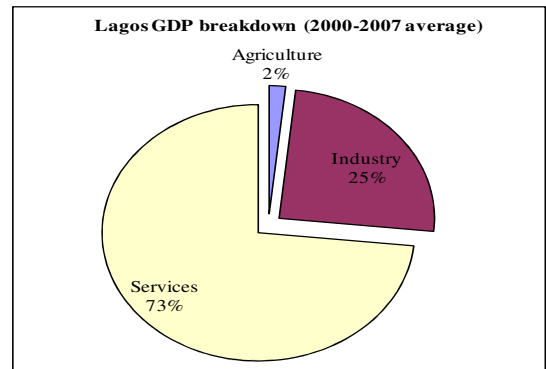
Introduction

1. **Lagos State was amongst the first states to be created when Nigeria was transformed from a federation of four regions into one of 12 states.** It was created on May 27, 1967 through a decree that restructured Nigeria into a federation of initially 12 states. The State is composed of five administrative divisions of Lagos, which Badagry, Ikeja, Ikorodu and Epe. These five divisions are themselves divided into 20 Local Government Areas and 37 Local Government Development Areas. The State is largely a city state, with the island area (composed of Lagos island, Victoria Island, and Ikoyi) forming the heartland of the City of Lagos and mainland area composed of mostly Ikeja, Surulere, Yaba, and Ebute-Meta. The outskirt areas consist of Ikorodu, Epe, and Badagry.

2. **Although the Federal Capital of Nigeria was transferred to Abuja, Lagos remains the country's financial and economic nerve centre.** Initially, Lagos Island played a dual role of being the Capital for Lagos State as well as the Federal Capital. However, when the Federal Capital Territory of Abuja was created in 1976, the State Capital was also shifted to Ikeja. Lagos ceased to be the Federal Capital on 12 December 1991, when the seat of Government was formally moved to Abuja. Nevertheless, it remains the country's financial and economic center. Most commercial and financial institutions have their headquarters in Lagos and are situated in the Island central business district. For example, 23 out of Nigeria's 24 banks are headquartered in Lagos. The State is also host to Nigeria's main international airport and seaport. Lagos is also the centre of Nigeria's film industry, popularly known as Nollywood.

3. **The State does not produce oil but accounts for a relatively significant proportion of Nigeria's GDP.** It is estimated that the Lagos economy contributes about 19 percent to Nigeria's non-oil GDP. Services account for 73 percent of the State's GDP while Industry and Agriculture account for 25 percent and 2 percent, respectively (See Figure 1). The main service sectors include wholesale and retail trading, financial sector, telecommunications, entertainment, public administration, hospitality, and transportation.

Figure 1: Lagos GDP Breakdown (2000-2007 average)



4. **Lagos has a mixed picture of socio-economic indicators while the summary welfare indicators are generally poor.** At 89 percent, Lagos state has the highest adult literacy rate in the country whose average is 64.2 percent. Similarly, 75 percent of the population has access to improved source of drinking water compared to the national average of 63.6 percent. Nevertheless, the summary welfare indicators are much poorer than the national average. In particular, 64 percent of the population lives below the poverty line compared to the national

average of 54 percent. At the same time, income inequality is very high, with a gini coefficient of 0.64 compared to the national average of 0.49. As a result, life expectancy at birth in Lagos is at 48, which is below the national average of 50.

5. **With one of the highest population growth rates in the world, Lagos State has an immense challenge of dealing with its many development challenges.** It is estimated that Lagos city alone has over 15 million inhabitants and is the second fastest growing city in Africa. As a result, the city is faced with typical challenges of a mega city: traffic congestion, poor housing conditions for the majority of the population, high incidence of crime, and poor sanitation. Apart from undertaking some policy and institutional changes, dealing with these challenges requires that in the main, the State Government undertake huge infrastructure investments.

6. **Given these challenges, the Government's development program is guided by an eight-point agenda that has a strong infrastructure focus.** The Ten-Point Agenda was initiated in 2003 and builds on the Lagos State Economic Empowerment and Development Strategy (LASEEDS). It has 10 focus areas as follows: Roads, Transportation, Power & water supply, Environment & Physical planning, Shelter, Health, Education, Food security, Employment, and Revenue enhancement. Given its bias towards infrastructure, implementation of this agenda has huge resource implications.

7. **In 2007, the World Bank conducted a review of the State's Finances.** The review found that there had been a 63 percent real increase in the state's revenue between 1998 and 2005. During the same period, real capital expenditures increased by 42 percent. In spite of this significant increase in capital spending, the review concluded that the State's investment needs still far exceed available resources. In this context, the review recommended a series of public expenditure reviews that would examine the effectiveness and efficiency of public spending including a fully fledged fiscal sustainability analysis that would provide insights into the sustainability of fiscal space available for investment in the medium and long-term.

8. **This PER aims at having a deeper understanding of key issues related to the sustainability of the fiscal framework for the State, performance of the budgeting system and of the public procurement system.** The findings and recommendations of the PER should guide the Government in the preparation and implementation of public sector reforms needed for ensuring fiscal sustainability and better use of the State's resources as it implements its infrastructure oriented public expenditure program.

Overview of Nigeria's Fiscal Federalism

The Constitutional Players

9. **Nigeria is a federation of 36 states, a federal capital territory and 774 local governments.** The 1999 Constitution gave increased responsibility to the states in the delivery of economic and social services and for the provision of infrastructure, both directly and jointly with local governments (LGs), while the Federal Government remains responsible for setting standards, coordinating policy, and discharging national functions such as security, foreign affairs, and macroeconomic management. However, most powers accorded to the states in the

Second Schedule of the Constitution are exercised concurrently with the Federal Government. This situation remains a source of debates over which tier of government, federal or state, is best placed to deal with various aspects of public services (such as education and police). Also, while the functions of local government are specified in the Fourth Schedule, Local Government Councils can exercise their responsibilities only in accordance with enabling legislation passed by the states. LGAs are therefore subject to state oversight and control to a large extent.¹

Public Revenue, Tax Policy, and Collection

10. **Different levels of Government in the federation have different tax collection responsibilities.** The Constitution of the Federal Republic of Nigeria places issues related to major taxes such as taxation of income, profits and gains, custom duties, excise and stamp duties, and road taxes under the Exclusive Legislative List at the federal level. This also applies to the value added tax (VAT). The most important state tax is the personal income tax collected by a state tax authority on individuals deemed to be resident in that state. Table 1 summarizes the tax-related responsibilities of the FGN and the states in terms of policy decision and collection.

11. **The Constitution establishes a distributable pool account called the Federation Account.** All revenues collected by the Government of the Federation are paid into this account, except the proceeds from the personal income tax of the personnel of the armed forces of the Federation, the Nigeria Police Force, the Ministry or Department of government charged with responsibility for Foreign Affairs and the residents of the Federal Capital Territory, Abuja. Revenues accruing to the Federation Account are essentially mineral revenues from oil and gas.

Table 2: Nigeria Fiscal Federalism: Distribution of Responsibilities for Taxation

	Legislation		Collection		Retention	
	Federal	State	Federal	State	Federal	State
Personal income tax	X		X	X	X	X
Withholding tax	X		X	X	X	X
Capital gains tax	X		X		X	
Profit tax	X		X		X	
Oil, gas, & mining revenues	X		X		X	
Stamp duties	X		X	X	X	X
Pool betting and lotteries,		X		X		X
Road taxes	X			X		X
Business premises	X			X		X
Development levy	X			X		X
Naming of Street		X		X		X
Right of occupancy		X		X		X
Value added tax	X		X		X	X
Custom and excise	X		X		X	
Non-tax IGR		X		X		X

¹ The 1999 Constitution of the Federal Government of Nigeria recognized 20 Local Governments in Lagos State. However, in 2002, the State created 37 new LGs, increasing the total to 57. As a result of pressure from the Federal Government, the State reverted to the 20 LGs structure while converting the intended additional LGs into Local Council Development Areas. In many respects, these development areas have been given operational responsibilities similar to the ones granted to the LGs listed in the Constitution. However, their fiscal relationships with the LASG and with the 20 fully recognized LGs are not formal.

Revenue-Sharing Arrangements

12. **The allocation of oil revenues across the three tiers of government has dominated the debate on Nigerian fiscal federalism.** The two main categories of revenues accruing jointly to the Federation before being distributed are mineral revenues and VAT revenue. Each of these has its own revenue-sharing arrangements, including both vertical (between tiers of governments) and horizontal (between states and between LGAs) formulas adopted by the National Assembly. Federal allocations amount to more than 80% of total revenues in most Nigerian states, but not in Lagos.

13. **The Constitution provides for the distributable proceeds of mineral revenues to be allocated to all three tiers of government based on a formula periodically determined by the Revenue Mobilization and Fiscal Allocation Commission and approved by the National Assembly.** The amount of the distributable proceeds is determined after deduction of a “derivation” share granted to oil-producing states (not less than 13% of the revenue accruing to the Federation Account directly from any natural resources). Under the current formula, the Federal Government receives 54.68%, state governments get 24.70%, and local governments receive 20.62% of distributable proceeds. The distribution of the states’ share between them is based on weighted criteria, including equality (45.23%), population (25.60%), internal revenue generation effort (8.31%) land mass (5.35%), and other considerations with smaller weights.

14. **The VAT revenue-sharing arrangement has been defined by law (as opposed to the Constitution, which includes a provision relating to mineral revenues).** The proceeds of the VAT that replaced the states’ sale taxes in 1994 are also pooled and redistributed according to particular formulas based on principles similar to the ones applicable to the distribution of mineral revenues. Vertically, the allocations to the FGN, the States, and the LGAs are currently 15%, 50%, and 35% respectively. The current horizontal VAT revenue-sharing formula among the states is based on weighted criteria including equality (40%),² derivation (50%), and population (10%). Although the formula reflects the importance that should be attached to the principle of derivation, the industrial states (Lagos, Rivers, Ogun, Kano), where the bulk of VAT is collected, feel deprived of what they consider a large part of their internally generated revenue because of the 40% of the proceeds being distributed equally among the states.

The Challenge of Fiscal Responsibility

15. **The Federal authorities have sought to limit the automatic pass-through of oil revenues to state spending, for reasons of macroeconomic management and efficiency of spending.** In 2005, an oil-price based fiscal rule was introduced. Under the rule, the approved budget is based on a conservative reference price for oil, and any excess revenue is saved in the Excess Crude Account. This mechanism, which largely de-links expenditure from oil prices, has succeeded in avoiding the boom-bust cycles of spending that had plagued Nigeria since the 1970s. The 2005 introduction of the oil price based rule for budgeting oil revenues has served as a major stabilizer of State finances by minimizing the volatility in federal allocations and further improving their predictability. As a result, states are able to predict future inflows of federal transfers with reasonable accuracy.

²“Equality” criterion means that 40% of the revenues are shared equally amongst the 36 states.

16. **Following the enactment of a federal Fiscal Responsibility Law in 2007, the federal government reached an agreement with the states to enact their own fiscal responsibility and procurement laws at the state level.** However, at this juncture only few states have adopted their own fiscal responsibility law.

Fiscal Relations between the State and Local Governments

17. **A Joint LG Account is maintained for collecting transfers from the Federal and State Governments to Local Governments.** By virtue of the provisions of section 162(6) of the 1999 constitution, each state must maintain a special account called the Joint LGs Account. All allocations to the Local Governments from the Federation Account and State funds are paid into the account; essentially the LGAs share of revenue in the Federation Account and 10% of state IGR. Section 162 (8) also stipulates that the amount standing to the credit of LGA councils to the state shall be distributed among the LGAs of the state on such terms and in such manner as may be prescribed by the House of Assembly of the state.

18. **Provisions are in place for monitoring the transfer of revenues to the Joint LG Account.** Following complaints from LGA Administrators in several states about the manner in which states were operating the Joint Local Government Account, in March 2005 the National Assembly adopted the Monitoring of Revenue Allocation to Local Governments Act 2005, which defines arrangements to ensure that allocations made to the LGAs from the Federation Account and from the state concerned are promptly paid into the Joint Local Government Account, that funds are distributed to the LGAs in accordance with the provisions of 1999 Constitution and any Law made by the SHoA, and that payment and distribution of the funds in the Account is monitored so as to ascertain the actual amount paid to each LGA. These arrangements have also been put in place in Lagos State.

19. **More broadly, state/local government relations are governed in each state by a state local government law.** The provisions of these laws vary across Nigeria, but in general terms such laws provide for a degree of supervision of LGs by the Governor. As a practical matter, the Governor has considerable influence on the affairs of local governments.

Borrowing Guidelines for Sub-national Governments

20. **Laws and guidelines are in place governing borrowing of sub-national governments.** The sub-national borrowing framework provides for federal oversight of sub-national fiscal and borrowing decisions through a combination of rule-based controls, and direct administrative controls requiring disclosure of all borrowing operations and prohibiting sub national governments from directly accessing external finance. Thus, Nigerian sub-nationals can freely borrow in Naira, within the established debt limits, while Federal approval and guarantee is required for loans or bonds in foreign currencies and markets.

21. **In 2007, the FDMO issued new external borrowing guidelines, as well as sub-national borrowing guidelines covering the period 2008-2012.** The main provisions are:

- States should seek federal government approval in principle ahead of full-scale negotiations for such loans;

- A minimum condition for such approval is evidence that the state has not over-borrowed externally or domestically. This is equated to evidence that the state's debt service obligation does not exceed 40 percent of its federation account statutory allocations;
- States should authorize Federal Ministry of Finance to deduct at source from their statutory allocation, the amount needed for debt service;
- States' external loans must be supported by Federal Government guarantee before final approval;
- Borrowing should be tied to specific investment projects whose feasibility studies should have been cleared by the National Planning Commission (NPC);
- Borrowing must be on highly concessional terms, specifically not to exceed one percent per annum;
- Borrowing should be limited to financing of projects for "poverty eradication" and for infrastructure.

22. **States have, within the established debt limits, a free hand to determine their domestic borrowing needs and seek such financing from domestic banks of their choice.** The sub-national borrowing guidelines state that any borrowing by a sub-national shall be the obligation solely of that particular sub-national unless explicitly guaranteed by the sovereign. For all FGN-guaranteed loans sub-national governments are required to issue an irrevocable standing payment order tied to the state's FAAC allocations. Federal disclosure requirements in place with respect to state borrowing from commercial banks require sub-nationals to immediately upon contracting a commercial bank loan, furnish the DMO with details of the loan. Also, the lending bank should furnish the DMO and the borrowing sub-national's Debt Management Department (where in existence), with reports on various stages of draw-down and utilization by the borrower, on a periodic basis. States are required to establish a sinking fund for each loan raised into which periodic contributions are made for meeting the loan obligations.

23. **To access the capital market, states must meet a certain number of legal and regulatory requirements** including requirements under the Investment and Securities Act (ISA) 1999, the Securities and Exchange Commission regulations and the listings requirements of the Nigeria and the Abuja Stock Exchanges. Under the ISA, states can issue securities in the form of registered bonds and or promissory notes. As with external borrowing, loans must be tied to specific projects. The total loan amount outstanding of the state and the proposed loan should not exceed 50 percent of the state's total revenues in the preceding year. A state's application to float bonds on the market should include audited accounts for the past five years.

24. **The guidelines stipulate a FGN guarantee as being compulsory for the states' borrowings from the capital market.** States are required to provide an irrevocable letter of authority giving the Accountant General of the Federation the authority to make deductions at source from the state's statutory allocation in the event of default by the state in meeting its payment obligation under the terms of the loan. The state is required to establish a sinking fund for each loan raised into which periodic contributions are made for meeting the loan obligations. Any deductions from the state's statutory allocation by the Accountant General are to be paid into the sinking fund account.

CHAPTER 2: FISCAL PERFORMANCE AND SUSTAINABILITY

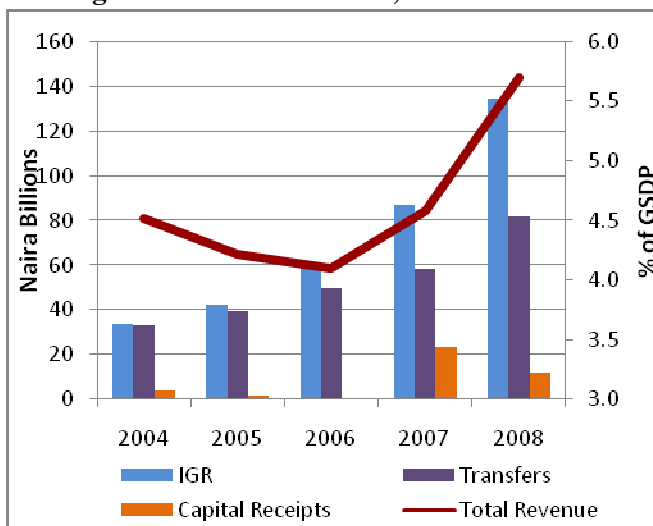
25. This chapter provides a picture of recent trends and patterns in revenue and expenditure by different types and categories and analyses the sustainability of Lagos’s fiscal program. An analysis of fiscal sustainability is especially important in the wake of the state’s plans to continue expanding its spending on infrastructure in line with its development agenda. Given the strategic importance of the economy of Lagos, ensuring fiscal sustainability is important not only for the State of Lagos but for the stability of Nigeria’s economy as well.

State Revenue Trends

26. **Lagos State has enjoyed strong revenue growth in recent years.** The increase has in part been due to high world oil prices, the growing economy (which exhibited an average 16 percent growth rate per year), increased federal transfers, but more importantly, substantial increase in IGR. Total revenues grew at an average real rate of 21 percent between 2005 and 2008, raising the revenue to GSDP ratio from 4.2 percent to 5.7 percent. Monthly IGR tripled to N6 billion during 2004-2007, and current estimates suggest that IGR reached a monthly average of N15 billion in 2009, up from N10 billion in 2008, as collection efforts were stepped-up. Overall, total IGR collections have more than doubled in real terms since 2004, from 2.4 percent to 3.5 percent of GSDP.

27. **Federal transfers have also grown, albeit less rapidly,** from N40 billion in 2005 to N82 billion in 2008-see Figure 2. Federal allocations, including excess crude in 2008, accounted for about 2 percent of GSDP. The continuous increase in oil prices over the decade has been a major explanatory factor for this. With the prices of Nigerian crude oil rising from an average of US\$38.3 per barrel in 2004 to an average of US\$96.7 per barrel in 2008, LAS has received growing statutory allocation transfers, in line with the arithmetic of Nigerian fiscal federalism. However, as the allocation formula favors geographically large states, Lagos receives federal allocations only 50 percent above those of states such as Kwara whose population is a third that of Lagos.

Figure 2: Revenue Trends, 2004-2008



Source: LASG Authorities

28. **The State revenue profile has improved markedly.** Strong IGR growth has led to a substantial change in the percentage share of revenue between Transfers and IGR, as illustrated in Figure 1 above. Since 2006, the share of IGR in Lagos State revenue (excluding grants) has risen significantly above par to an average of 61 percent, making Lagos much less reliant on

federal revenues that are highly susceptible to oil price fluctuations. The share of capital receipts in state revenue has been fairly stable at about 5 percent, but rose sharply in 2007 to 14 percent, owing to one-off proceeds from the sale of shares.

29. **Further analysis by source of revenue indicates that the composition of IGR has not changed substantially over the last eight years.** The largest category remains taxes (essentially personal income tax and capital gains tax), which represent usually 75-83 percent of IGR (See Table 2). Other IGR categories include fines and fees, licenses, earnings and sales, rents on government property, interest payments and dividends, contributions (actually some reimbursements by the FGN), and miscellaneous.

30. **The Lagos State Government is currently engaged in a legal battle with the Federal Government over the collection and retention of Sales Tax.** Under the case, the Lagos State Government is contesting the Federal Government's collection of sales tax when according to the constitution this should be collected by states. It is also contesting the fairness of the revenue allocation formula which distributes the sales tax revenues equally amongst all states when the bulk of Nigeria's sales tax revenue is collected from Lagos State. A positive outcome for Lagos on this case would result in a significant increase in the share of sales tax revenue in IGR.

Table 3: IGR distribution by percentage, 2005-2008

	2005	2006	2007	2008	Average 2005-2008
Taxes	76.9	83.2	75.9	78.8	78.7
Fines & Fees	12.3	10.5	8.6	7.0	9.6
Licenses	1.5	1.4	1.1	1.3	1.3
Earnings & Sales	3.7	3.3	3.6	3.0	3.4
Rent on Government Property	0.2	0.3	0.5	0.6	0.4
Interest & Dividends	1.3	0.9	1.9	2.9	1.7
Grants Revenue	0.0	0.0	0.0	0.8	0.2
Miscellaneous	4.2	0.4	4.0	5.6	3.5
Sale of Investments	0.0	0.0	4.5	0.0	1.1

Sources: LASG Authorities.

31. **The increase in IGR has been the result of several reforms implemented by the State Government.** These reforms have focused on the restructuring of the state's Internal Revenue Service, introduction of more convenient and fraud free processes of tax collection process, and a vigorous taxpayer education campaign (See Box 1). IGR collection has increased substantially, owing to the broadening of the tax base and the tightening of collection processes against various types of fraud. Currently, individual taxpayers total about 4 million and are projected to reach 5 million by 2010, or 50% of official residents, up from 44%. Corporations have grown to 330,000 in 2007 from about 250,000 in 2004, as the state has sought to diversify its tax payer profile by bringing more medium-scale enterprises into the tax net. However, despite diversification efforts, taxes related to the 10 largest corporations account for a significant share of total Lagos' IGR -20 percent.

Box 1: Tax Reforms Implemented by the Lagos State Government

Computerization of revenue collection and monitoring: In 2000, the LASG put in place a new computerized infrastructure for tax collection and monitoring known as the Electronic Banking System of Revenue Cycle Management (EBS-RCM). The EBS-CM is a sophisticated information network system linking Tax Stations & other Revenue Agencies to lodgment banks. The Objective of the EBS-RCM is to go online with the Direct Bank Lodgment System (DBLS) of the revenue collection process and provide information for tax administration and planning while monitoring and co-ordination of all revenue generating activities of the state. As a result, the system has led to the introduction of more effective and fraud reducing measures such as automated payment receipts and electronic tax clearance certificates. Alpha-Beta Consulting (ABC) Limited was appointed as the sole monitoring agent to control and monitor the collection of State revenue using the new system. The responsibilities of ABC under this arrangement, include:

- Monitoring and reporting on all revenue generation, collection, and accounting activities and operations of the Lagos State Board of Internal Revenue and all Lagos State ministries, departments, and agencies (MDAs).
- Developing and maintaining a comprehensive database of taxpayers in LAS, including the introduction of a unique tax identification number for all taxpayers.
- Ensuring computerization of processes, procedures, and documentation in respect of Lagos State revenue collection and accounting.
- Integrating the revenue generation, collection, and monitoring activities of all other tax consultants fully within the EBS-RCM infrastructure.
- Training staff of revenue-generating agencies on EBS-RCM.

Increased autonomy of the Lagos State Board of Internal Revenue: In 2005, a new Board of Internal Revenue (BIR) was created with a member representation including more individuals from outside public service, and acting through the Lagos Internal Revenue Service (LIRS) that has large operational autonomy to manage the collection and monitoring of revenue. The new BIR and LIRS commenced operation in November 2005. The BIR is a regulatory and supervising agency whereas the IRS is the actual service provider in terms of revenue collection and monitoring. The LASG was convinced that a properly organized public agency enjoying sufficient autonomy, especially in the areas of human resource management and budgets, could in due course take over a number of functions performed by the consultants at a lower cost to the government and ultimately the taxpayer.

Introduction of a Self-Assessment tax filing system: The new system was introduced in 2008 and is aimed at making tax payment convenient as well expand the tax payers list. Individuals can conveniently pay their taxes at any of the 1,200 branches of the designated banks as well as all the LIRS tax stations spanned all over the state and receive their receipts within 72 hours of payment.

Taxpayer education campaigns and improved taxpayer services: The LIRS has pursued a vigorous taxpayer education campaign and expanded its network of taxpayer service points in the State. As a way of encouraging Lagos residents to embrace tax payments as a measure of their responsibility to the society, thereby making them pay taxes voluntarily without been forced, enlightenment efforts has been boosted through tax campaigns in the print media, radio and television. These campaigns have been taken to traditional rulers and major trade associations as a way of co-opting them into the tax drive. Moreover, as a means of taking tax awareness and education to the potential tax-paying public as well as bringing the tax assessment and revenue collection closer to them, the LISR has also established several stations in markets and bank branches throughout the state. These explain how to fill in tax return forms and respond to all other types of taxpayer enquiries.

32. **There remains significant scope to improve the performance of tax revenue.** For example, the State of Lagos does not draw much from its property tax base. While property taxes account for a substantial share of municipal budgets around the world ranging from an average of 20 percent in India, over 50 percent in many Canadian cities, and 70 percent in many cities in USA, property tax rates in Lagos have been historically low. In 2008, actual collection from property tax was 2 percent of IGR against the estimated potential of over 15 percent. Results of property tax reforms, initiated in 2001 have remained elusive, at least in part due to its poor implementation and administration. However, the LASG is committed to re-launch its original plan to improve property tax collection, as the potential yield from this revenue source remains substantial in the medium term.

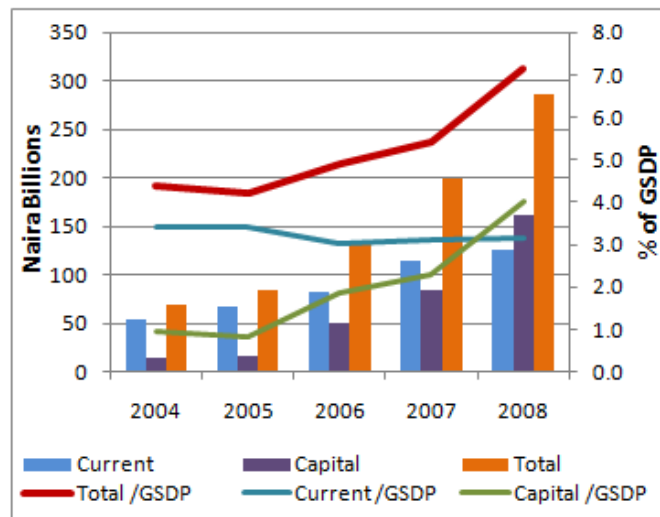
33. **Further, tax collection costs remain high.** In spite of the significant reforms undertaken by the State Government, the EBS-RCM has raised questions regarding the level of its operating costs. The consultancy services cost about 10 percent of total IGR collected. This represents a higher cost of collection than is typically found in modern revenue administrations, where costs of collection of less than 3 percent are common. The percentage currently charged should be renegotiated downward, especially given that revenues are likely to continue to grow in the medium term. Addressing the high collection costs will be critical to sustaining gains in revenue collection. This will also require building the capacity of the BIR to enable take-over of a number of functions currently performed by the consultants.

State Expenditure Trends

34. **Strong revenue growth has facilitated rapid expenditure expansion.** Between 2005 and 2008, total expenditure as a percentage of GSDP rose from 4.2 percent to 7.2 percent, driven largely by growth in capital expenditures. Figure 3 shows the trends for the two broad economic categories of expenditure: current and capital, illustrating a clear upward movement.

35. **Capital spending has risen sharply, to an estimated 4 percent of GSDP in 2008, up from 0.8 percent of GSDP in 2005.** This represents an eight-fold increase in real terms over the last 4 years. The doubling of the annual volume of capital expenditure in real terms reflects the large economic and social infrastructure rehabilitation and development program within the “Lagos 2020 plan”. The state government has made a determined effort at allocating higher capital budget envelopes to priority sectors mostly in the area of transport, environment (drainage and waste management), health and education.

Figure 3: Actual Expenditure Trends, 2004-2008



36. **In keeping with the government focus on infrastructure renewal, expenditure programs are now largely capital in nature.** The share of capital expenditure represented about 56 percent of state expenditures in 2008, compared to 42 percent in 2007 and 19 percent in 2005³. Capital expenditure is expected to rise further, in line with the 40:60 operating to capital spending ratio being sought by the state administration. However, in the medium term, growth in capital spending will depend on the boldness of the LASG investment policy in the coming years and improvements in absorptive capacity (project preparation, investment programming, procurement, release of funds). The administration envisages about NGN1trillion in total investments during 2009-2012 with a 3 percent cumulative average real growth rate, leading to a “stabilisation” at slightly more than NGN200 billion per year in the medium term compared with the exponential growth in 2004-2008. Among the reasons for the capital expenditure (capex) stabilisation is the fact that the state is trying to shift away from directly funded projects to PPPs, whereby the state’s portion of projects funding may be disbursed over up to 30 years of the concession agreement. Furthermore, once infrastructure has undergone at least part of the planned improvements, service delivery will take priority and the capital-to-total spending ratio, now heading towards 60 percent, could eventually bounce back. Land sales, transfers from the federal government and divestments of financial assets should help fund about 10 percent of the plan, while the bulk of it should be tax and debt funded.

³ The FY 2008 ‘Great Leap Budget’ was the first state budget to have a 60:40 capital/recurrent budget ratio

Figure 4: Composition of Total Expenditure by Functional Classification, 2007-2008

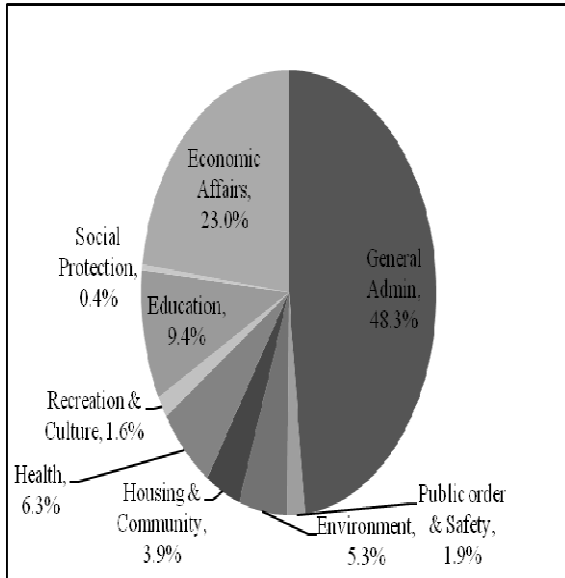
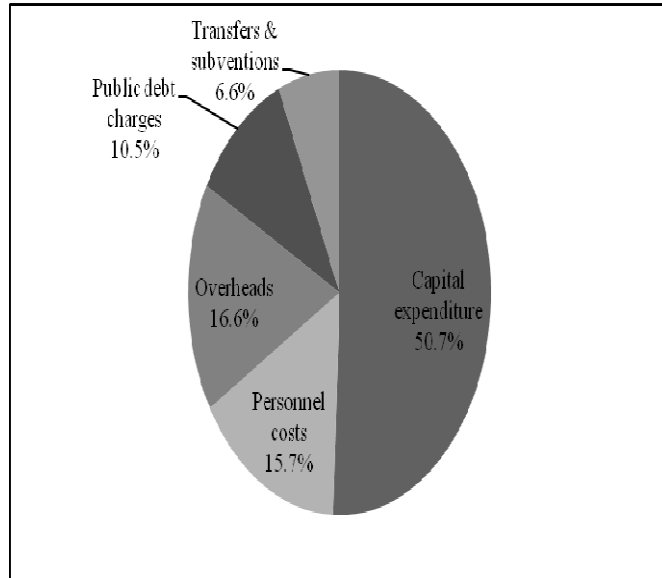


Figure 5: Composition of Total Expenditure by Economic Classification, 2007-2008



37. **General administration and economic affairs dominate expenditure by functional classification, while and in terms of economic classification, capital expenditures are the single largest, followed by overheads (goods and services), personnel (wages and salaries), and public debt charges.** As Figure 4 shows, general administration receives the largest share of total expenditure with an average of 48.3 percent between during 2007-2008, followed by economic affairs which had a share of 23 percent during the same period. With regard to expenditure by economic classification, it can be seen from Figure 5 above that on average, capital expenditure during 2007 and 2008 was 50.7 percent of total expenditure while overhead expenditures were at 16.6 percent and personnel costs at 15.7 percent.

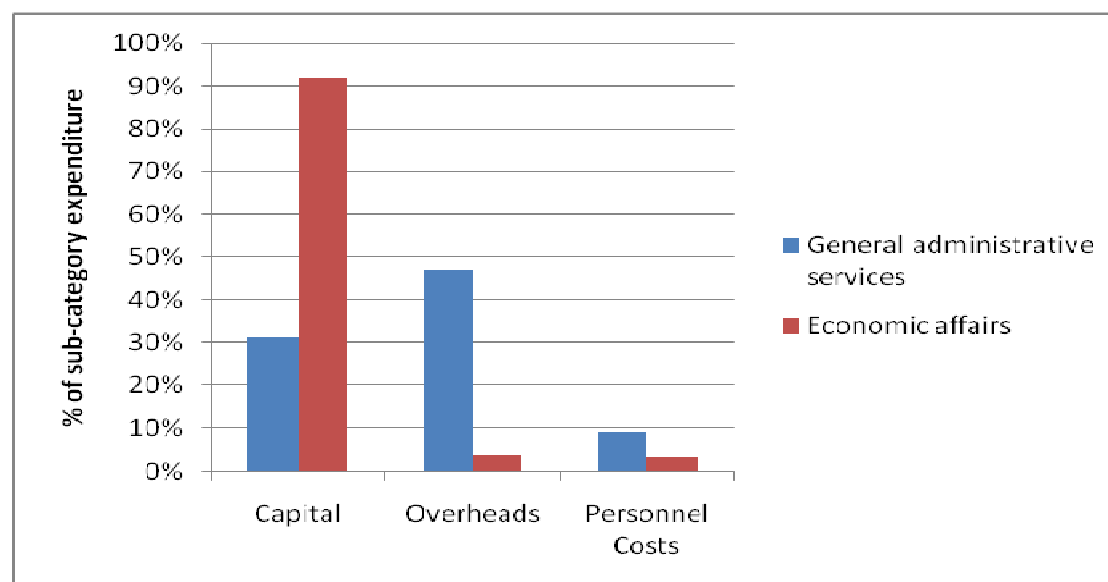
38. **An examination of trends in expenditure shares by functional classification over time shows some clear shifts in priorities in line with the State's ten-point agenda.** It can be seen from Table 4 that although general administration remains dominant, its total share of overall expenditure has declined from 53.9 percent in 2005 to 45.8 percent in 2008. The reduction in general administration's share of recurrent expenditure is even more spectacular, from 49.0 percent in 2005 to 29.6 percent. At the same time, the share of economic affairs has doubled from 12.6 percent in 2005 to 25.2 percent in 2008. Similarly, although the shares of total expenditure on environmental protection and housing and community amenities are low, they have also doubled from 2.9 percent to 5.3 percent and 2.4 percent to 4.2 percent. These increases though have been at the expense of expenditures on health and education whose shares have declined 8.5 percent to 6.3 percent and 17.3 percent to 9.1 percent, respectively. With an adult literacy rate of 89 percent as reported in the previous chapter, the highest in the country, perhaps the reduction in the share of expenditure on education may simply be a reflection of the significant progress that has been made in the sector in recent years.

Table 4: Trend in Percentage Share of Total Expenditure by Functional Classification

	Total				Recurrent				Capital			
	2005	2006	2007	2008	2005	2006	2007	2008	2005	2006	2007	2008
General administrative services	53.9	56.3	51.8	45.8	49.0	52.9	38.4	29.6	4.8	3.5	13.4	16.3
Public order and safety	1.3	1.0	1.9	1.9	1.3	1.0	1.2	0.9	0.0	0.0	0.7	1.0
Environmental protection	2.9	2.9	5.4	5.3	2.3	2.3	1.8	1.6	0.7	0.6	3.6	3.7
Housing and Community Amenities	2.4	3.4	3.4	4.2	0.8	0.5	0.6	0.4	1.5	2.9	2.8	3.8
Health	8.5	4.6	6.3	6.3	6.1	3.4	3.9	3.0	2.4	1.2	2.4	3.3
Recreation, culture & Religion	0.9	1.9	1.3	1.8	0.8	0.8	0.6	0.6	0.1	1.1	0.6	1.2
Education	17.3	8.8	9.8	9.1	15.0	7.3	7.9	6.4	2.3	1.5	1.9	2.7
Social Protection	0.2	0.4	0.4	0.4	0.2	0.4	0.1	0.2	0.0	0.0	0.3	0.2
Economic affairs	12.6	20.6	19.8	25.2	3.2	2.9	2.0	1.7	9.4	17.7	17.8	23.5
Total	100.0	100.0	100.0	100.0	78.8	71.4	56.5	44.3	21.2	28.6	43.5	55.7

39. **In spite of the declining share of general administration, the question still remains if its share in total expenditure is too large.** Some practices no doubt tend to push the cost of administration services up. A clear example is the centralization of the travel budgets of all ministries in the Ministry of Finance. As a consequence, travel costs associated with activities relating to infrastructure, rural development, or health end up being recorded as administration expenditures. As Figure 7 shows, close to 50 percent of total administration expenditures go to overheads, which are mostly dominated by travel. Under these circumstances, it is difficult to make an educated judgment on the extent to which resource allocation to administration, which remains on the high side, is really beyond advisable limits.

Figure 6: Main expenditures within general administration and economic affairs



40. **In general, Lagos's operating spending has grown by about 20 percent per year on average in nominal terms during 2005-2008.** This trend has been the result of increases in both personnel and overheads costs. Personnel expenses have doubled since 2005 owing to a

combination of both wage increases and increases in personnel size. The LAS civil service, which had about 36,000 employees at the end of 2002, included 47,000 employees at the beginning of 2006 and 51,000 as at end May 2009⁴. In addition, a general average increase of 15 percent to State civil servant wages was effected in 2008, with the change in state administration. Local officials maintain that the headcount of the core administration should only increase modestly in the medium-term as the state aims to improve the productivity of its staff. It remains to be seen, however, whether Lagos can push investment up above NGN200 billion per year over the medium-term without substantially boosting the headcount of the core administration and its parastatals.

41. **Parastatals employ an additional 45,000 people, funded via subsidies and other transfers accounted for among overheads.** The 37 local governments do not receive direct funding, i.e. subsidies, from Lagos due to its policy to directly finance infrastructure or service delivery related to it. This is then accounted as overheads or investments in the state budget. Operating subsidies have been budgeted at NGN21 billion in 2012, up from NGN15 billion in 2008 and NGN11 billion in 2007.

42. **Despite these efforts to stabilize operating costs, allocations for debt charges have trended upward.** Debt service grew to 20 percent of total recurrent spending in 2008 from 16 percent in 2006 and could edge towards 30 percent in the medium-term due to the high rate of interest and short debt maturities. The increase in debt charge spending is attributable to increased borrowing from domestic banks. Commercial loans outstanding in June 2008 had been taken out at fixed rates, with an average rate of 13 percent. Together with wages and salaries, debt charges make up about 47 percent of total government recurrent expenditure.

Fiscal balance, sustainability, and risk analysis

43. **Lagos State ability to meet its recurrent expenditure obligations has improved considerably.** Fuelled by rising tax collection, Lagos's operating balance strengthened to about 42 percent of operating revenue in 2008 from 17 percent in 2005. Lagos officials expect IGR growth to drive up the operating surplus, leading to an operating margin rising to about NGN100 billion per year, and about 50 percent of operating revenue, which will continue to fund investment spending during 2009-2012. But while positive operating balance growth in recent years has allowed expansion of funding for capital expenditures, resources available remain significantly below the amounts required to effectively implement the sizeable investment program. This has led to larger deficits, as investment spending gathers pace.

44. **Since 2006, Lagos State accounts have shown a rapidly rising fiscal deficit.** The State's fiscal balance position has deteriorated sharply over the past four years, from an overall fiscal surplus of 0.1 percent of gross state domestic product (GSDP) in 2004, to a deficit of 0.7 percent in 2009. On average, the state recorded an overall deficit of about 15 percent of revenues on its fiscal operations, between 2006 and 2009.

⁴ A detail analysis of the evolution of the main categories of personnel by grades, agencies, and functions is necessary. It would guide the formulation of relevant recruitment policies to ensure that the composition of the staff strength is aligned with the current and future requirement of the service.

Table 5: Lagos State Finances, 2003-2009

	2003	2004	2005	2006	2007	2008	2009
	Act.	Act.	Act.	Act.	Act.	Act.	Act.
	(Million Naira)						
Revenue	52,300	70,797	83,650	110,830	168,993	227,998	269,217
IGR	27,600	33,967	42,281	60,310	86,957	134,092	168,763
Federal Transfers	24,700	32,980	39,490	49,810	58,493	81,941	74,990
Statutory Allocation	n.a.	n.a.	27,380	33,420	35,332	41,180	35,030
Excess Crude	n.a.	n.a.	-	-	-	8,596	-
VAT	n.a.	n.a.	12,110	16,390	23,161	32,165	39,960
Capital Receipts	n.a.	3,850	1,879	710	23,543	11,965	25,464
Expenditure	46,300	68,750	83,650	127,160	186,137	275,602	303,507
Recurrent Expenditure	37,800	53,830	67,690	77,080	101,277	114,581	125,093
Personnel (wages, pensions & gratuities)	14,600	16,000	19,530	21,200	33,746	39,788	42,811
Overhead	14,400	27,170	34,020	47,580	56,714	64,943	73,485
Debt Charges, Domestic Debt	8,800	10,660	14,140	8,300	10,817	9,850	8,797
Capital Expenditure	8,500	14,920	15,960	50,080	84,860	161,021	178,414
Operating Balance	14,500	13,117	14,081	33,040	44,173	101,452	118,660
Overall Fiscal Balance	6,000	2,047	0	(16,330)	(17,144)	(47,604)	(34,290)
Financing	n.a.	n.a.	0	16,330	17,144	47,604	34,290
Domestic			0	16,330	17,144	47,604	34,290
Bonds			-	(3,000)	(3,000)	(6,000)	50,000
Commercial Banks			-	19,330	20,144	53,604	(15,710)
Debt Stock	n.a.	n.a.	n.a.	41,062	63,706	112,810	168,000
External			35,200	25,100	30,600	32,100	53,000
Domestic			n.a.	15,962	33,106	80,710	115,000
Debt Charges, External debt, N mn			n.a.	277	353	298	299
	(Percent of GSDP)						
Total Revenue	4.5	4.5	4.2	4.1	4.6	5.7	5.7
IGR plus capital receipts	2.4	2.4	2.2	2.3	3.0	3.7	4.1
Total expenditure	4.0	4.4	4.2	4.7	5.0	6.9	6.4
Recurrent Expenditure	3.2	3.4	3.4	2.9	2.7	2.9	2.6
Capital Expenditure	0.7	1.0	0.8	1.9	2.3	4.0	3.8
Overall fiscal balance	0.5	0.1	0.0	-0.6	-0.5	-1.2	-0.7
Debt Stock	n.a.	n.a.	n.a.	1.5	1.7	2.8	3.5
Memorandum item:							
Nominal GDP (Naira millions)	1,167,227	1,568,380	1,980,504	2,702,770	3,686,801	4,000,200	4,744,797
Nominal exchange rate	130.9	134.3	131.3	128.7	125.8	118.5	152.3
Real interest rate (%)	-10.42	12.53	15.20	-0.01	12.85	5.01	7.89
IGR growth (%)	n.a.	23.07	24.48	42.64	44.18	54.20	25.86

45. **The sizeable increase in the fiscal deficit was financed by borrowing, both domestic and external.** Debt levels rose sharply in 2007-08, following their decline in 2006, which was the result of the debt reduction deal secured by Nigeria in October 2005 with the Paris Club. Current data on Lagos state debt show that at the end of 2009, outstanding debt totaled N168 billion (Table 6) representing 3.5 percent of GSDP, up from 1.5 percent in 2006. In terms of its composition, domestic debt as a share of total debt increased from 39 percent in 2006 to 68 percent in 2009, while the share of external debt fell from 61 percent to 32 percent over the same period. The shift in debt structure was largely on account of the bond issuance program launched by the State in 2008.

Table 6: Lagos State Public Debt Outstanding

	2006	Percentage	2007	Percentage	2008	Percentage	2009	Percentage
External	25,100	61	30,600	48	32,100	28	53,000	32
Domestic	15,962	39	33,106	52	80,710	72	115,000	68
Total	41,062	100	63,706	100	112,810	100	168,000	100

Source: Lagos State Government

46. **Lagos State Government has met only partially the debt level requirements of Nigeria's Investment and Securities Act since its enactment in 2007.** The debt stock-to-state revenue ratio, which under the Investment and Securities Act should be lower than 50 percent, rose from 27 percent in 2006 to 70 percent in 2008. However, the state has been in full compliance with the external debt service indicator limit. Between 2003 and 2008, external debt service payments (interest plus amortization) averaged at 35 percent of federation allocations, below the statutory ceiling of 40 percent. Overall, debt service payments (both domestic and external) remain within manageable limits at 10.3 percent of state revenues, despite their significant rise in the last few years.

Table 7: Limits on Sub-national Borrowing in Selected Countries

<i>Country</i>	<i>Debt Service ratio</i>	<i>Debt-revenue ratio</i>	<i>Other restrictions</i>
Brazil	≤13% of net current revenue	≤200% of net current revenue	Total debt cannot exceed the capital budget, indebted governments should maintain a primary surplus, outstanding guarantees should not exceed 25 percent of net current revenue, borrowing in anticipation of future revenue should not exceed 8 percent of net current revenue.
Italy	≤25% of own revenue net of certain earmarked funds		Only for capital spending; no foreign borrowing allowed
Japan	Three year average ≤20% of own revenue		Mainly for subnational infrastructure projects; no foreign borrowing allowed
Lithuania	≤15% of general revenue	≤30% of total revenue	No state guarantees; Ministry of Finance can lower the ceiling for municipalities; long term credit can be used only for investment
Russia	≤15% of general revenue	≤30% of own revenue for provinces ≤15% of own revenue for municipalities	
Spain	≤25% of total revenue		Long-term credit can be used only for investment; approval required for foreign borrowing

Source: Nigeria, Subnational Borrowing Guidelines; World Bank PREM note, number 64: *Monitoring fiscal risks of subnational governments.*

47. **The fiscal trends above suggest that the fundamental longer-term fiscal sustainability question remains relevant:** In the long run, will the State be able to sustain expansionary fiscal policies (driven by economic and social needs) while servicing a debt substantially increased? Fiscal Sustainability Analysis shows that the answer will depend largely on the growth of IGR, the growth rate of public expenditure, the effectiveness and efficiency with which money is spent, and the ability to secure highly concessional external financing.

48. **Baseline projections for the period 2009-2018 depict a favorable evolution of the main fiscal indicators, but alternative scenarios indicate that fiscal indicators are highly sensitive to a more rapid than under the baseline increase in expenditures and lower revenue growth (Annex, Table 12).** Debt levels are forecast to stabilize at 3 percent of GSDP while annual budget deficits decline. A significant reduction in debt service pressure beginning in 2011 is projected, as commercial debt due in the next few years is partially substituted for planned concessional World Bank financing. The FSA concludes that the state fiscal framework is sustainable in the medium term if policies of strict fiscal discipline and debt responsibility, as outlined in the LSG reform program, are enforced.

49. **The fiscal framework should accommodate the public investment program without derailing the state from its sustainable debt path.** The state budget is expected to expand considerably over the medium term. Total budget expenditures in 2015 would be 31 percent

above 2008 levels in real terms. The baseline scenario assumes that budget investment spending would increase from about N161 bn in 2008 to N269 bn in 2012 and to N387 bn in 2015. This should facilitate execution of the state's medium term infrastructure investment program, to be largely funded with strong growth in IGR, combined with concessional IDA financing. Financing provided by IDA in 2010-12 would amount to over two thirds of the total deficit financing during that period. This would greatly reduce the overall costs of state borrowing and result in broad improvements in the overall state debt profile. The share of external debt in the total debt of LSG would steadily rise from 29 percent in 2008 to 58 percent on 2018.

50. **The analysis suggests that Lagos State's fiscal policy is sustainable in the medium term⁵ (Annex, Table 11).** Projected fiscal soundness under the baseline scenario is reflected in trends of fiscal and debt indicators, which remain at manageable levels over the projected period. Lagos' debt-to-GDP ratio is projected to peak at about 4.4 percent in 2011, and decline thereafter to 3 percent in 2018. The debt-to-revenue ratio (interest payment only)⁶ is also forecast to decline, stabilizing at an average of 50 percent of total state revenue from 2015 onward. The debt service-to-revenue ratio would remain below 10 percent throughout the forecast period and below 5 percent after 2012. Operating balances would stay positive for the entire period. Personnel-related costs (wages and pensions) are expected to stay below 15% of the total budget spending. Budget deficits are expected to decline. The baseline scenario shows that the LSG would incur a considerable budget deficit during the period of 2010-12, at an average level of about N30 billion a year. The deficit would be reduced considerably in 2012, and it is expected that the government would run a balanced budget in 2013. In relative terms, the baseline scenario assumes a significant fiscal adjustment effort, with the deficit as percent of total government spending being reduced from 11% in 2009 to 3.4% in 2012.

⁵ The total state debt considered in this FSA includes local government debts, but excludes (1) public enterprise debts; and (2) contractual arrears.

⁶ Total debt service, including both interest and principal on medium- and long-term debt, would decline from the average of 10% in 2010-12 to less than 7% of total revenues on average in 2015-18.

Box 2: Assumptions for fiscal projections

Growth prospects: Real average annual national GDP growth should remain substantially robust at 6 percent over the medium term. Improved macroeconomic management of the Nigerian economy and higher oil revenues would mean overall better economic growth prospects for Nigeria and Lagos state in particular.

Oil price and production: A considerable recovery in Nigeria's oil production after 2011, to reach an average of 2.6 mn bpd, while the oil price remains in the range of \$75-80 per barrel.

Interest rate: Real interest rates on domestic borrowing will decline gradually but remain above 4%. In combination with relatively high inflation, nominal lending rates will therefore remain within the range of 10-14%. The drivers for this decline relate to the ongoing banking sector reforms, high level of competition in banking, declining political risks, and an expected entry of foreign banks into the sector

Inflation rate: A gradual decline in inflation from its 2008 level to single-digit levels to a medium term average of 8.5 percent

Exchange rate: Recovery in oil revenues, supported by responsible macroeconomic policies of the federal government, will result in real appreciation of the Naira, at the rate of about 4% per annum after 2012

Internally Generated Revenue: The Lagos state government will continue with the recent revenue reform initiatives to strengthen IGR collection capacity. Average growth in IGR is therefore assumed to exceed 6% per annum in real terms, reflecting both stable economic growth as well as further improvements in tax administration. The current level of state and local tax burden is quite modest and provides considerable room for further improvements in tax collection.

Debt: The LSG will continue with steady implementation of all existing IDA credits (about \$USD 445 mn in outstanding commitments as of September 2009). It is assumed that these loans will be fully disbursed over the next 4-5 years, thus raising the external debt stock of LSG considerably. However, this is not expected to create serious risks for debt sustainability given the large grant element of IDA credits. Real appreciation of the Naira would further reduce relative costs of IDA borrowing denominated in foreign currency.

Over the next two years (by May 2012) the LSG will complete its repayments of several old IBRD loans (signed in 1990-91), resulting in marginal improvements to the current debt profile. Outstanding total IBRD loan balance as of September 2009 was less than US\$ 3 mn (at the average interest rate of 6.5%)¹.

New borrowing from IDA will be limited to budget support operations disbursed in 2010-12 with annual disbursements in the range of \$200 mn. These new loans will be directly linked to LSG deficit financing and explicitly reflected in the state budget.

The outstanding deficit (after IDA budget support) will be financed locally through a combination of commercial bank borrowing and local bond issuing. All such borrowing is assumed to take place at prevailing market terms.

51. **However, risks to stability of the fiscal outlook remain high.** Alternative scenarios indicate that fiscal indicators are highly sensitive to a more rapid than under the baseline increase in expenditures and lower revenue growth.

52. **Lower internal revenue growth would result in unsustainable fiscal dynamics, reflected in the steady deterioration of fiscal indicators after 2014.** The revenue-adjusted alternative scenario, which assumes a 50 percentage decline in revenue growth rates outlined in the baseline, implies substantial worsening in all debt indicators. Under this scenario, the debt to revenue ratio would be growing steadily to reach 163 percent in 2018, while the debt service ratio would gain 4 percentage points. This scenario highlights the importance of maintaining momentum in the implementation of tax revenue reforms to keep Lagos on a sustainable debt path.

53. **Debt indicators would deteriorate relative to the baseline under the expansionary fiscal policy scenario**, where annual growth in real non-interest recurrent expenditures is 150 percent higher from 2010 onward. The debt-to-GDP ratio would climb to 6.2 percent by 2018. The debt to revenue ratio would follow an upward path reaching 119 percent in 2018. This underscores the importance of phasing the implementation of the ambitious PIP, selecting and investing only in projects with a high rate of return, while keeping recurrent spending under control and undertaking PEM reforms to set the stage for efficiency gains alongside expenditure growth.

54. **A prolonged decline in oil prices would result in unsustainable fiscal indicators** relative to the base case. A drop in oil prices to \$40 per barrel relative to the baseline would triple Lagos' debt to revenue ratio from 70 percent in the baseline scenario to 221 percent in 2015. Stability of the debt profile could not be maintained in this scenario beyond 2015 even at the cost of considerable compression in the budget investment program. This scenario highlights further the importance of improving the non-oil tax collections in order to reduce long-term dependence on volatile oil revenues. It also points to the constraints of oil dependence: in the short to medium term LSG's investment plans would have to be scaled down in a case of prolonged period of low oil prices.

55. **Lagos' fiscal dynamics would become less favorable if its deficit financing were available on more expensive terms.** Failure to secure concessional financing from IDA would substantially increase Lagos' debt-to-revenue ratio, which would peak at 121 percent in 2012, up from 70 percent in 2008. But in contrast to three earlier alternative scenarios, the debt profile in this case would remain sustainable recovering to about 100 percent of revenues after 2015 and stabilizing at that level. This scenario indicates that Lagos should make an effort to secure highly concessional loans to finance its development needs. At the same time, it suggests that the baseline scenario (and associated fiscal and debt program) is sufficiently robust with respect to fluctuations in cost of deficit financing.

56. **One potential risk to fiscal sustainability is a build-up of contingent liabilities.** ISPOs issued to finance PPPs could be one such source of liabilities. Although local officials maintain that the need for roads and other user-pay facilities should largely support the revenue stream, efforts are underway to fully evaluate all potential risks from the PPP program, including contingent liabilities. This will involve evaluation of a number of risk-minimizing options, including a proposal to securitize all assets from the PPP program to offset liabilities created. Notwithstanding these efforts, it will be especially important for the Government to develop appropriate institutional and organizational arrangements— for analyzing contingent liabilities in respect of PPPs before they are incurred and monitoring these risks over their lifecycle—if it is to effectively manage the exposures that they create for the state governments balance sheet.

57. **The state has also accumulated significant obligations in the form of pension and contractor arrears, although these may have been cleared now.** The Lagos administration acknowledges about NGN160 billion of unfunded pension liabilities for the benefit of state staff, parastatals and the 20 local governments. These liabilities reflect a kind of severance pay and the administration plans to pay lump sums when employees retire. According to Lagos, annual disbursements should average NGN5bn-7bn over the medium term, peak at about NGN12bn in

2015 and decline afterwards until 2040 (included in this FSA under “Personnel Costs”). In 2008, the stock of contract expenditure arrears (above 5 million Naira) alone was 17.14 billion Naira, representing approximately 6 percent of total Lagos State expenditures. Indications are that these may have been cleared now.

58. **Debt management remains lacking.** The full extent of contractor arrears cannot be determined without improving the quality of recording and reporting of debt data. Lagos State does not keep a formal record of most of its overdue payments or commitments. In spite of recent efforts, Lagos State does not have a full roaster of its external and domestic liabilities and details of debt profile. Also, there exist discrepancies in debt statistics from the Debt Management Office of the FGN and the LASG. Debt service costs are not fully reflected in the budget since project funds such as IDA investment credits are reported outside the State budget. Thus, putting together a “clean” and comprehensive information base on Lagos state’s financial standing to allow more detailed analysis will have to be a key part of the State Government’s efforts to get a better handle on its fiscal and public expenditure management.

Conclusion and Recommendations

59. **The State’s fiscal policy is broadly sound.** Significant progress has been made in increasing IGR in recent years due to several tax administration reforms. The Government’s operating balance has been positive. Although the need to expand infrastructure investment in order to meet the critical service needs of the population has clearly stretched the state’s resources, the State’s fiscal program remains sustainable in the medium term. Risks to the program include a decline in world oil prices, a build-up of contingent liabilities, and unavailability of concessional financing.

60. Going forward, the review has the following recommendations:

- Strengthen efforts to increase property tax revenues by among other things, exploring options for increasing land use charges. Options for increasing taxes from other sources also need to be pursued;
- Explore options for reducing the cost of tax collection but without compromising the effectiveness and efficiency of the system. In this context, a review of the consultancy costs is warranted;
- Undertake a detailed review of expenditure on general administration in order to determine if current levels are reasonable. The review would need to pay special attention to the travel budget;
- Undertake measures to improve the State’s capacity to manage debt. Areas of improvement should include management of debt data, including contingent liabilities.

CHAPTER 3: PERFORMANCE OF THE BUDGET SYSTEM

61. **This chapter reviews the budget system in Lagos State in order to assess its efficiency in the allocation of resources.** The analysis looks at the legal framework and the budget process, starting from budget planning and preparation, through to execution, monitoring, and evaluation. Special attention is also paid to the capital budget process in order to assess the efficiency of the public investment system. A well functioning budgeting system improves chances that expenditure decisions made will meet the desired development objectives. Not only does it ensure that expenditures are properly aligned with development priorities, but also ensures value for money.

Legal Framework

62. **Like most states in Nigeria, Lagos has relied on the 1999 Federal Constitution and its own administrative rules and guidelines to provide a framework for public financial management in the State.** The Federal constitution among the many provisions stipulates the scope for States to raise revenues, intergovernmental fiscal relations, and the annual budget process, including financial reporting and auditing. Apart from the Federal constitution, the State of Lagos does not yet have separate laws regulating the state's public financial management system. Instead, reliance has been on administrative guidelines. For example, in 2007, a Circular was issued by the State's Tenders Board outlining interim public procurement procedures until a full State procurement law is enacted.

63. **The State Government is in the process of preparing its own state-specific legislation to govern its public finance management system.** Three key pieces of legislation are in draft form: A Public Finance Management (PFM) bill, an Audit Bill, and a Procurement Bill. Once passed and if properly implemented, the laws will go a long way towards strengthening Lagos State's PFM system. The PFM bill details the public finance management regulatory framework for government institutions and addresses the budget process, expenditure controls, banking, internal audit and reporting on public accounts. It also stipulates the circumstances under which appropriations in emergency are necessary. The Procurement Bill promotes value for money, open and effective competition, ethics and fair dealing, accountability and reporting, equity, and the establishment and securing of procurement records. The Audit Bill promotes autonomy of the State's auditing functions and timely submission of the audited financial statements and the final audit report to the State House of Assembly.

Budget planning and preparation

64. **Internal revenue forecasting remains a challenge.** At 69 percent of the budget, internal revenue performance is significantly lower than forecasted but has been improving, as indicated in Table 8 below. While Transfers resulting from the statutory allocation and VAT depend on factors outside the primary control of the LASG, this is not the case for IGR. Yet IGR has had high levels of variance since 2000. The poor projection of IGR is symptomatic of a weak budgeting routine and a tendency of over-optimism, encouraged by the strong growth of revenue collected in recent years and expectations from the recent revenue administration reforms.

Table 8: Actual Receipts in Percentage of Budget Forecast, 2005-2008

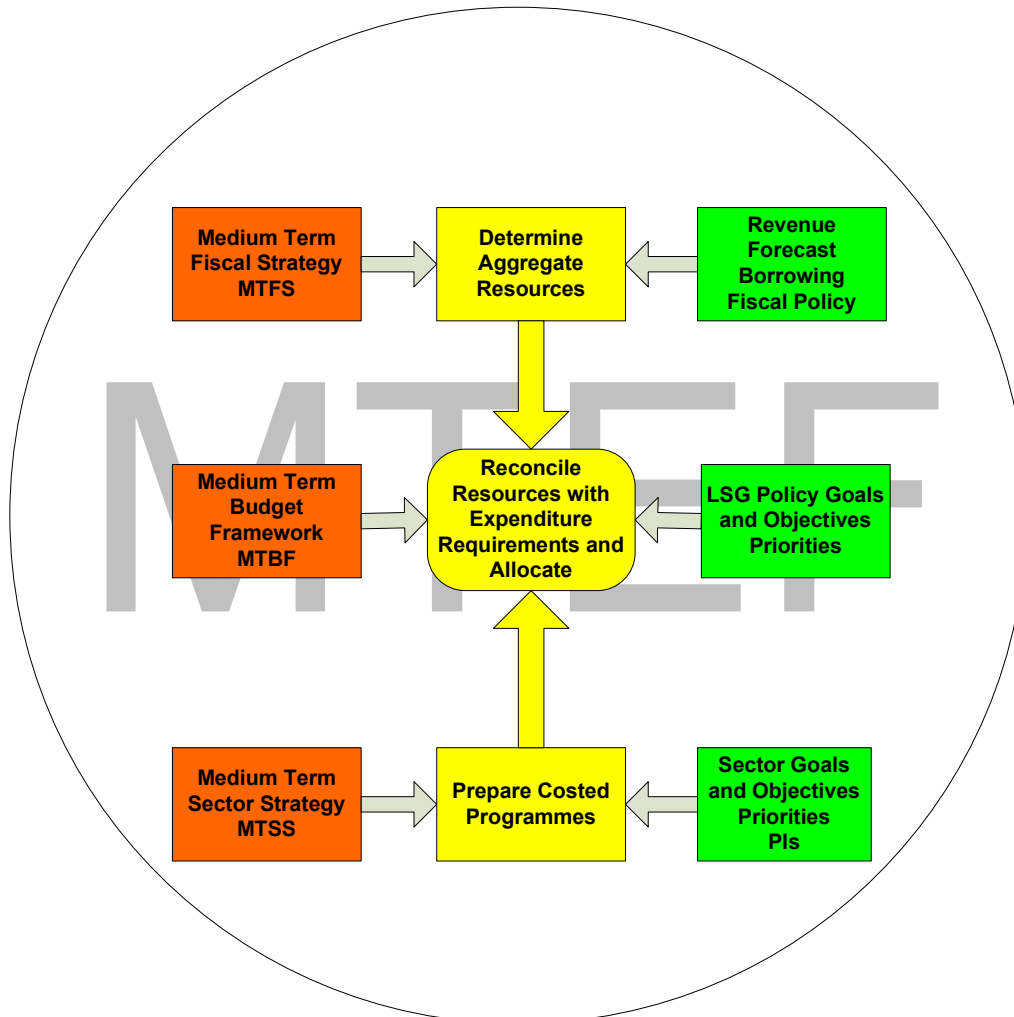
	2005	2006	2007	2008	Average
IGR	70.3	59.9	61.0	85.0	69.1
Transfers	106.8	100.0	97.0	101.8	101.4
Capital Receipts	82.0	2.6	101.5	48.7	58.7
Total Revenue	84.0	62.0	76.0	87.0	77.3

Source: Lagos State Government

65. **Expenditure planning and preparation in Lagos has generally been characterized by short-termism and weak linkages between budgets and priority sector strategies.** Preparation of the annual budget has normally adopted an incremental approach, where MDA level expenditure estimates for the year have been based simply on previous year's expenditure out-turns and projection of spending needs for the coming year. No ceilings are communicated in advance to MDAs although they are expected to arrange their capital projects in order of priority. There has also been no explicit linkage between capital and recurrent budgets. Budget proposals submitted by MDAs are discussed at bilateral meetings with the Ministry of Economic Planning and Budget which among other issues looks at the consistency of an MDA's budget with the State's overall strategic policy priorities. However, there has been no systematic and structured appraisal to see if MDA level budgets conform to priority sector strategies for achieving the State's overall development goals and objectives. This is because until recently, there have been no sector strategies in place to guide budget preparation.

66. **Recently, the State Government has been working on the introduction of new approaches to budget planning and preparation.** At the core of the new approaches to budgeting is the adoption of a Medium-Term Expenditure Framework (MTEF) which aims at ensuring that the budget has a multi-year perspective, is fiscally sustainable, and is aligned to the Government's strategic priorities in a more structured way. In this context, introduction of an MTEF has been nested in three components (See Figure 8): preparation of a medium-term fiscal strategy (MTFS), medium-term budget framework (MTBF), and medium-term sector strategies (MTSSs). The MTFS defines aggregate projected revenues, expenditures, and the Government's fiscal targets for the medium-term. The MTBF contains medium-term budget estimates for individual spending agencies based on the state's strategic priorities and in a manner that is consistent with overall fiscal objectives as outlined in the MTFS. The budget estimates for individual spending agencies contained in the MTBF represent resource ceilings within which MDAs are expected to prepare their detailed budgets. Finally, the MTSSs represent a crucial link in the process of translating the Government's policy priorities into the spending reality of the annual budget. It sets out for each sector, costed initiatives and expenditure plans through which a sector seeks to contribute to the attainment of the government's policy priorities within the limits of available resources. It also includes well-defined outputs and outcomes of the initiatives and expenditure plans and the measures by which the performance of these initiatives will be measured.

Figure 7: Overview of MTEF Components



Source: International Consultants Management Limited, 2009

67. **Some elements of the new approaches are already being utilized, although more work remains for the tools to achieve desired results.** The MTFS was used in determining the revenue, expenditure and financing position for the 2009 budget. However, the model had a one year perspective only. The MTFS has now been extended to cover a three year planning horizon and includes updated debt data from the state Debt Management Office (DMO). Further, a subsidiary spreadsheet loans model was developed in the Ministry of Finance to feed into the MTFS and allow the implications of alternative budget levels and financial options to be tested. However, the two models have not yet been integrated. A model for determining resource ceilings for each MDA has been developed. During preparation of the 2009 and 2010 budgets, the MEPB used MDA level ceilings to recommend revisions during bilateral discussions. However, the ceilings were still not communicated in advance to the MDAs. This led to arbitrary preparation and revision of budget proposals thereby undermining the process of aligning the budget to strategic priorities. Finally, the Government has since 2008 been preparing MTSSs. It started first with three pilot sectors (Health, Education, and Environment) and added seven more in 2009 (Works and Infrastructure; Housing; Physical Planning and Urban

Development; Transportation; Women Affairs and Poverty Alleviation; Youth, Sports and Social Development; and Justice). However, the MTSSs have not yet been used in the preparation of the relevant MDA budgets. One main weakness of the MTSSs in their current form is that they focus on capital projects only. Further, there are no practical guidelines in place on how MDAs can translate the MTSSs into operational annual budgets. For the MTSSs to be effective, MDAs need to have their own work plans for translating the MTSSs into annual budgets.

68. **Reforms are also underway to strengthen the capacity of the Ministry of Economic Planning and Budget and MDAs in budget planning and preparation.** The introduction of new tools and approaches has been facilitated by external consultants. Government efforts are therefore also focusing on enhancing internal capacity to utilize these tools as well as update them. In this context, a number of reforms have been undertaken. First, an Economic Intelligence Unit (EIU) has been established in the Ministry of Economic Planning and Budget. The unit will be responsible for updating the MTEF and the MTBF as well as leading the determination of MDA-level budget ceilings. Second, more planning officers will be deployed and trained in the Budget Division of MEPB. The main responsibility of these officers will be to lead the appraisal of budget proposals submitted by MDAs, including assessing proposed capital projects for budget readiness and alignment to medium-term sector strategies. The LASG is also enhancing the capacity of MDAs to prepare budgets within an MTEF. To date, budget preparation in the MDAs has been handled by mostly finance and administration officers who are not best placed to lead the process of translating sector strategic priorities into MDA annual budgets. Only a few MDAs are manned with planning officers. In this regard, planning officers will be trained and deployed to various MDAs. Finally, a budget manual for Lagos State has been drafted. The manual outlines principles governing the budget process in Lagos State, procedures as well as roles and responsibilities of various ministries, departments, and officers.

69. **The wider public is increasingly being consulted during budget preparation and the State House of Assembly has been effective in influencing the final outcome of the proposed budget.** The Ministry of Economic Planning and Budget has recently been organising budget consultation fora with the general public in the upstream stages of budget preparation. During such consultations, the Government solicits suggestions from the public on budget priorities. This development augurs well for improved transparency in public expenditure management, although it is not possible to verify the extent to which the public's views are reflected in the proposed budget. At the same time, the approval process by the State House of Assembly has been effective in influencing the final outcome of the budget. For instance, the State House of Assembly voted to reduce the 2010 budget by 9.3 percent on the basis that certain expenditure categories, such as personnel costs and capital expenditure were significantly overestimated when compared to the previous year's out-turn.

70. **In most years, the budget has not been passed into law in time for the start of the new fiscal year on January 1st.** The budget has usually been submitted to the State House of Assembly around November. Taking into account the December break, this has not allowed enough time for the budget to be debated upon and approved in time for the start of the new fiscal year. As a result, the budget has usually been approved well into the New Year. For instance, the budget for 2007 was approved on January 18, while that of 2008 was approved on January 24. The 2009 budget was an exception. It was submitted on November 17, 2008 and was

passed into law by the State House of Assembly in December 2009. In contrast, the 2010 budget was also submitted on November 17, 2009 but due to protracted debate in the House was only passed into law on February 25, 2010 and assented to by the Governor on March 1, 2010 - two months into the new fiscal year.

Budget Execution

71. **Although the performance of Lagos State is relatively much better than most states in Nigeria, the overall budget out-turn tends to be significantly different from the approved budget thereby undermining the credibility of the budget.** In particular, actual expenditures have been significantly lower than budgeted expenditures. For example, actual spending was below budgeted spending by 25.2 percent in 2006, 24.8 percent in 2007, and 33.9 percent in 2008. One of the major factors has been the unrealistic revenue projections of IGR. As mentioned earlier, internal revenue forecasting has been a challenge in Lagos, with a tendency to overestimate expected IGR for the year. Therefore, budgeted expenditures have largely been a mere reflection of these unrealistic revenue projections. Another problem has been poor cash management which has led to delays in release of funds to MDAs. There is no cash planning during the implementation of the budget. As a result, it is not uncommon for some MDAs to have more funds than they need at a particular point in time while others are cash strapped.

72. **Budget execution rates are lower for capital expenditure than recurrent expenditure.** As can be seen from Table 9, investment expenditure in Lagos is characterized by a relatively low level of execution in comparison to recurrent expenditure, although it must be said that Lagos's performance is much better than most states. First, some projects have been included in the budget before they are ready for implementation. Second, there has generally been limited absorptive capacity in the MDAs to implement projects. Even when resources are available, the ability to prepare implementation and procurement plans and, more generally, to carry out activities required for the timely execution of investment operations is often limited. Finally, deviations at the capital budget level may be amplified by the inconsistencies in financial information recording between the budget preparation stage and computation of the State accounts at the end of the year. For example, the document submitted to the SHoA lists among capital expenditures of a given ministry financing items such as "Provision for Specific Outstanding Debt" that should not appear there. During budget execution, the related payment is rightly computed under "Debt Charges." This creates an automatic discrepancy with the initial budget document.

Table 9: Budget Spending Performance, 2005-2008

(Actual expenditure in percentage of approved budget)

	2005	2006	2007	2008	Average Execution Percentage
Current Expenditure	103.3	70.9	78.6	78.7	82.8
Personnel	79.8	70.8	91.9	82.7	81.3
Overhead	98.3	74.9	71.8	70.8	78.9
Capital Expenditure	34.0	46.0	66.0	66.0	53.0
Total Expenditure	74.0	59.0	72.0	71.0	69.0

Source: Lagos State Government**Budget Monitoring and Evaluation**

73. **There have been improvements in in-year budget monitoring with recent efforts focusing on output monitoring.** New formats for monitoring revenue and expenditure performance were introduced and several monitoring reports were issued in 2009 in the new format to reflect on in-year budget implementation. The state government also set up an inter-ministerial committee on budget tracking whose work has brought about additional improvements in expenditure reporting. More recently, the Governor has directed that all MDAs start submitting output monitoring reports in order to assess the effectiveness of public expenditures.

74. **However, considerable discrepancies between actual and budgeted expenditures imply that expenditure monitoring is also not effective.** Improvements in expenditure monitoring should among other things ensure that problems in implementation are identified in good time so that corrective measures are taken in order to increase the chances of adherence to the approved budget. It appears that currently, expenditure monitoring reports do not result in any remedial measures where findings raise concerns.

75. **Further, weaknesses remain in keeping track of certain financial information.** For example, because of gaps in coverage and reporting of real and contingent liabilities by State parastatals, there is little information with respect to government explicit (and implicit) liabilities. Similarly, it is still not possible to promptly track unreported government revenue, and unretired payment vouchers. The large number of bank accounts maintained by the Lagos State Government coupled with the fact that the bank statements are not received on timely basis results in the preparation of bank reconciliation statements falling into arrears by several months. This loophole makes the system prone to errors and irregularities.

76. **Financial statements are prepared in a timely manner, conform to national reporting formats, but fall short of international standards.** The automated financial management system, “Oracle Financials” and its progressive implementation have improved accounting and financial reporting. Accounting officers have also recently been deployed to strengthen the MDAs, accelerate the budget execution process and strengthen internal controls and financial reporting. However, the software is yet to be optimally utilized as a sizeable

number of the modules are yet to be made operational. In addition, reconciliation of fiscal data held in the government's ledgers with government bank account data held by commercial banks, as well as internal accounts are not regularly undertaken. Where they are carried out, there is no evidence of independent reviews to ensure that reconciling differences are explained.

77. **There is generally wide coverage of internal audit across the public sector.** The Central Internal Audit Directorate deploys Internal Auditors to all MDAs of the LASG excluding parastatals. In line with the recommendations of the LSFAA 2004 report, an Internal Audit Charter has been drawn up detailing the Role of Internal Audit, Responsibilities of Internal Audit, Scope and Authority of internal audit work, amongst others. Also, an annual work programme is prepared to give direction to Internal Audit staff on activities and tasks required to be carried out. However, there are certain weaknesses identified that affect Internal Audit function. For example, there are not enough computers for staff to work with. There is also a problem of high staff turnover for reasons such as slow promotion, promotion bar on getting to level 10 (progression is tied to further academic\professional qualification which is not sponsored or subsidized by government), and lack of specialized salary structure/financial motivation considering the nature of the work.

78. **Similarly, external audit reports have generally been comprehensive and wide in coverage, although quality could be improved.** The State Auditor General audits all Ministries, Departments and Agencies (MDAs) except parastatals in respect of which different audit arrangements subsist. The annual audit reports include separate section on audit of MDAs and that of parastatals which are extracts from the audit reports of private external auditors of the various parastatals. The audit report contains detailed analysis and comments on revenue and expenditures, the level of performance of particular projects, contract specifications, and payments made and required remedial action. The audit report also covers weaknesses in internal controls. Notwithstanding the fact that the audit opinions were qualified for the fiscal years 2006, 2007 and 2008, a major challenge is the absence of generally accepted financial reporting standards to provide guidance in significant accounting areas as well as the non-existence of an applicable financial reporting framework under which the public sector audits are conducted.

79. **The Audit Reports are submitted to the State House of Assembly in a timely manner but follow-up on audit recommendations remains a challenge.** The constitution of the Federal Republic of Nigeria, 1999 requires the Auditor General to submit the audited report to the legislature within three months of receipt of financial statements from the Accountant General. The office of the Auditor General in Lagos state met this requirement for years 2006, 2007 and 2008 (See Table 10). The Public Accounts Committee of the State House of Assembly has been efficient in scrutinizing the audit reports. However, follow-up on the committee's recommendations as well as those of the Auditor General remains a challenge as several of the identified issues reoccur in subsequent audit reports.

Table 10: Submission times for Financial Statements and Audit Report

Year	Date of receipt of financial statement	Date of submission of Audit Report to Legislature	Time frame
2006	20 th June,2007	7 th September,2007	Two and half months
2007	17 th May,2008	19 th June,2008	One month
2008	10 th March,2009	4 th May,2009	Two months

Source: Report of the Auditor General of Lagos State, 2006, 2007 and 2008

Efficiency of the Public Investment System

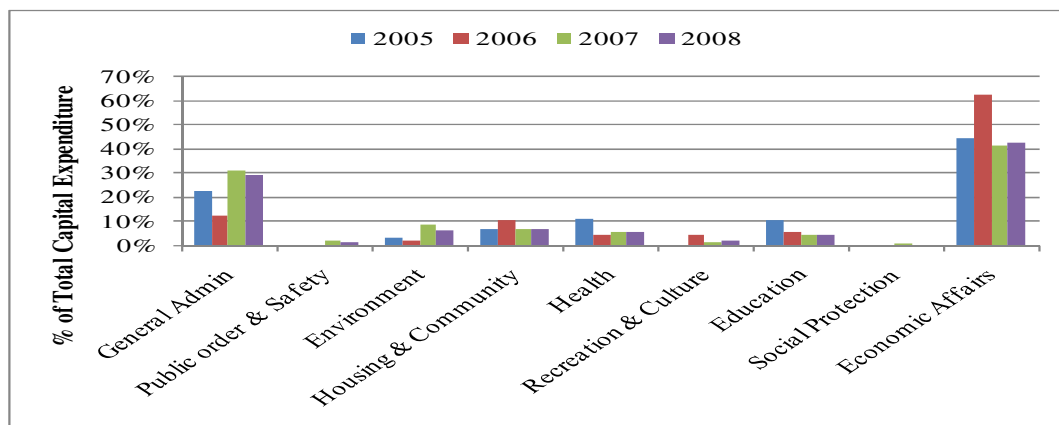
80. **The assessment of the public investment system for Lagos is done by examining the performance of the State in managing the capital budget process.** In particular, the assessment looks at the extent to which selected projects derive from the State's strategic development policies and priorities, appraisal of individual projects, procurement process, efficiency in implementation, monitoring, evaluation, and asset maintenance.

Strategic guidance for investment

81. **In Lagos, the ten-point agenda (TPA) is the State's strategic policy document for guiding the prioritization of resource allocation by sector.** As mentioned earlier, the strategy has identified ten areas of focus for Lagos: roads, transportation, power and water supply, environment and physical planning, shelter, health, education, food security, employment, and revenue enhancement. The question is whether in practice, the initial screening of capital projects takes into account these strategic areas.

82. **At broad level, priority capital spending explains an average of 73 percent of total spending between 2005 and 2008.** Figure 9 illustrates the capital spending pattern of Lagos State between 2005 and 2008 by functional classification. The analysis shows that the priority functions of economic affairs (which includes roads, transportation, power, water supply, and food security), education, health, environmental services, and housing (which includes physical planning) account for an average of 73 percent of total capital spending between 2005 and 2008. Therefore at broad level, this evidence suggests that actual Government capital spending closely aligns with defined priorities.

Figure 8: Composition of Capital Spending by Functional Classification, 2005 – 2008



Source: Staff Calculations

83. **While the TPA provides a framework for first level of screening of capital projects, it has a limitation.** The document provides strategic guidance only at sector level. It does not provide comprehensive strategic guidance on priority areas within sectors. Although the document outlining the TPA mentions some of the priorities within each sector, the TPA is not a fully fledged development policy strategy as is the case with traditional poverty reduction strategy papers (PRSPs). As a result, it is not detailed enough as a strategy. Therefore, it is easy for many types of capital projects to be justified on the basis of the TPA.

Project Appraisal and Review

84. **Most capital projects in Lagos do not go through a formal appraisal and review process.** A Directorate exists in the Debt Management Office of the Ministry of Finance that is responsible for investment appraisal, research, and project monitoring. Although it was set up to focus mainly on projects financed through loans, MDAs are free to utilize its services for all other projects as well. In practice, most projects, including those financed through borrowed funds, are not formally appraised. There is no mandatory requirement that all projects should be appraised before they are included in the budget, and the capacity of the office to conduct cost-benefit analysis appears to be weak. Although the Government considers various options before settling on a particular project, such options are usually not subjected to formal cost-benefit analysis. Nevertheless, the Government has sometimes engaged consultants to advise on the viability of certain large capital commercial projects. Otherwise political considerations tend to override selection and location of most public capital projects. The general attitude toward formal appraisal processes is that they unnecessarily slow down progress, and that they are limited in their ability to capture non-economic benefits, which can sometimes be substantial.

Project Selection and Budgeting

85. **The budgeting process currently focuses on the need to admit projects that are ready for implementation.** As reported earlier, the execution rate of the Lagos State capital budget has been low due to projects being included in the budget long before they are ready for implementation. As a result, more stringent criteria have been put in place for admitting projects into the budget. Projects to be included in the capital budget must now meet the following documentation requirements: (i) evidence of site acquisition with a view to ensuring that the project fits into the Master Plan for the area, (ii) the sign-off by the Ministry of Physical Planning & Urban Development, evidencing (i) above as well as approval of specific building plan, (iii) established right of way in the case of road construction, accompanied with preliminary designs, showing concrete drains, utilities duct, walkways, bicycle lanes and street lights, as well as the programme for demolitions where applicable, (iv) bill of quantities, (v) any other document necessary to prove the preparedness of the agency to execute the proposed project. Proposals on such projects should include costs, timing, benefits as well as challenges in their implementation.

86. **Although capital projects admitted into the budget are costed, MDA level budgets do not incorporate future recurrent implications of projects.** This is however a weakness of the budgeting framework in general where the budget is not prepared in a multi-year perspective. This situation is therefore bound to change now with recent efforts to introduce an MTEF in the State's budgeting system.

Project Implementation

87. **Although some competitive bidding is practiced in the selection of contractors for projects, the procurement process is beset with weaknesses.** For example, non-registration for pre-qualification does not prevent a bidder from being evaluated. Further, advertisement in newspaper is seldom done, with the high cost of advertisement in the national newspaper given as an obstacle to advertising. The existing procurement guidelines do not require that procuring entities pre-disclose bid evaluation criteria. In addition, the guidelines require that preference be given to State agencies that participate in a bid exercise. In most cases, criteria not specified in the advertisement (for example, indigenous considerations as well as past working relations with the procuring entity) are taken into account when determining the award of contract. There is also no public bid opening. Finally, Lagos State does not have a complaints review mechanism for aggrieved bidders.

88. **Actual implementation of capital projects has been characterized by delays and non-completion, although the state is ahead most other states.** As mentioned earlier, this has in the past mainly been due to inclusion of projects in the budget that are not ready for implementation. Other factors include lack of work and procurement plans to guide implementation of projects. Ineffective monitoring of projects has also been a major factor. Every MDA has a project monitoring committee and the Ministry of Economic Planning and Budget (MEPB) also has a unit charged with the responsibility of monitoring State-wide projects. However, most of these monitoring committees are not effective enough because of inadequacies in staffing, equipment, motivation, and authority. Finally, while the provision of large advances to contractors was meant to speed up implementation of projects, it has had the

opposite effect. In the majority of contracts, advance payments have been as large as 70 percent. However, the 2006 Audit found that in spite of the large advance payments, there was widespread underperformance of contracts.

89. **However, measures recently introduced are yielding noticeable improvements in execution rates of capital projects.** As mentioned earlier, there is now strict adherence to readiness criteria for admission of capital projects into the budget. Second, the LASG has recently instituted a system whereby advance payment is made to the Bank of the contractor rather than the contractor himself/herself and the Bank releases the money to the contractor only after satisfying itself that the contractor has completed the work for which the advance is supposed to be paid. Finally, there has been greater involvement of the public by the state in the monitoring of projects.

Project Adjustment

90. **Implementation of capital projects is often characterized by revisions, leading to changes in project scope and to significant increases in project cost above what was anticipated at the time of planning and budgeting.** The procurement guidelines stipulate that no government agency shall entertain any price variation, except if such variations arise as a result of government's fiscal measures or a change in the quantum of work. In this context, any variation in the original contract sum of less than 25 percent shall be approved by the Chief Executive of the State (the Governor), while variations in excess of 25 percent must be considered by the STB before being forwarded to the EXCO. While the system provides for adjustments to be made to projects, the envisaged changes are only in response to changes in project costs and not expected benefits.

Facility Operation

91. **There is no registry in place for current assets and their physical condition.** No separate department exists for keeping a record of assets for the State, whether at MDA level or at the central Ministry of Economic Planning and Budget. As such, there is no inventory of existing assets to show asset type, value, title, history, and their physical condition. Some of the legal titles to properties can therefore not be traced, resulting in loss of State properties in certain cases. Like elsewhere in Nigeria's public sector, the State of Lagos uses the cash basis of accounting, which records asset values only in the year of cash outflows. The State has not yet modified the system to carry forward asset values from year to year and determine their balance sheet/book values at the time of disposal. This leads to undervaluing of assets during disposal. Finally, there is currently no system of assessing the extent to which individual facilities are actually improving service delivery. Monitoring of service delivery is taking place at a much broader level.

Project Evaluation

92. **Like in most States in Nigeria, ex-post evaluation of project implementation does not take place in Lagos.** Although final payment to contractors is contingent on the issuance of a certificate of completion, no systematic evaluation of projects is done at completion. Therefore

there is no opportunity to compare the final outputs and outcomes with original projections and expectations and obtain lessons for the future. It is one of those tasks that are not seen as a priority in the capital budget process.

Conclusion and recommendations

93. **The performance of the Lagos State Budget system in general has been mixed.** There have been improvements in some areas while weaknesses remain in others. On the positive side, efforts are underway to enact new legislation to govern public financial management. Similarly, a reform process is also underway to improve budget planning and preparation through the introduction of a multi-year perspective to budgeting and sector strategies that will improve alignment of the budget to the state's strategic priorities. There is also broad based participation in the budget preparation process with the State House of Assembly able to effectively influence the substance of the budget. There has also been improvement in the monitoring of budget implementation. The introduction of Oracle has improved timeliness in the production of financial reports and subsequently, of audit reports. Coverage of internal and external auditing has also significantly improved. In spite of these strengths and positive developments, weaknesses remain in the budget system. First, revenue forecasting is a challenge. Second, there is a missing link between the newly developed MTSSs and the annual budget. Third, in spite of improvements in the monitoring of budget implementation, huge discrepancies between the actual and approved budget undermine the credibility of the budget. Fourth, financial and audit reports conform to national standards but still fall below international standards in certain respects. Further, follow-up on audit recommendations is weak.

94. **The capital budget system is much weaker than the budget system in general.** In light of the broad alignment of the budget to the State's main priority areas, the first level of project screening appears to be working. However, beyond the first level of screening, there is no mandatory and routine system of conducting formal appraisal of projects before final decisions are made. Once admitted into the budget, implementation has been very slow, hence current measures to ensure that proposed projects meet strict readiness requirements before they are admitted into the budget. The system provides for adjustments to be made to projects. However, in view of the fact that formal appraisals are rare, it appears that most changes are arbitrary. There is no formal project evaluation upon completion and central registry of all assets is not in place.

95. **In light of these findings, the following recommendations are suggested:**

- Strengthen the capacity of the newly formed EIU in undertaking revenue forecasts;
- Further upgrade the MTSSs by strengthening their link to service delivery and integrating recurrent expenditures;
- Put in place a mechanism for developing MDA-level work plans that would help them translate MTSSs into operational annual budgets;
- Given that it will take time for the sophisticated approaches to budgeting (MTEF, MTSS) and project selection (cost-benefit analysis) to take root in the system, there is need to strengthen even further the stakeholder consultations currently

being employed to determine priorities for the budget. Even if the identified projects and programs are not underpinned by rigorous analysis, there is still some level of confidence in a budget that is based on extensive and meaningful stakeholder consultations.

- Take steps to utilize all the functionalities of the Oracle system;
- Strengthen current measures for dealing with under-performance of the budget in general and of capital projects in particular;
- Develop a mechanism for ensuring follow-up on audit recommendations;
- Strengthen the institutional framework for undertaking formal project appraisal, monitoring, evaluation, and maintenance of records for all State assets created.

CHAPTER 4: REVIEW OF THE PUBLIC PROCUREMENT SYSTEM

96. **This chapter assesses the performance of public procurement in Lagos against four basic pillars of a well-functioning procurement as defined by OECD-DAC/World Bank.** The four pillars are as follows: existence of a comprehensive and transparent Legislative and Regulatory Framework, Institutional Framework and Management Capacity, Procurement Operations and Market Practices, and Integrity and Transparency of the Public Procurement System.

Legislative and Regulatory Framework

97. **There is currently no public procurement law in Lagos State but a Procurement Bill has been prepared.** Public procurement is regulated by financial regulations and memoranda as well as administrative guidelines and circulars. These are administrative documents which could be easily amended without taking into account the fundamental rights of suppliers, contractors, and consultants. Following the Recommendations of the 2003 LSPAR, a draft Procurement Bill was prepared but is yet to be enacted into law. While awaiting enactment of a procurement law, on November 26, 2007, the State Tenders Board issued a Circular⁷ containing interim procedures that were intended to incorporate the recommendations of the LSPAR. The 2007 Circular is applicable to the Lagos State Government, and parastatals. Its main objective is to improve transparency of the procurement system along the lines proposed in the LSPAR. Although the Circular is an improvement on the Financial Regulations and the 2000 Circular, it lacks significant provisions that a good law would have, hence the urgent need to finalize discussions on the Procurement Bill.

98. **Once passed, the Procurement Law will go a long way towards improving the State's procurement system.** The draft bill has a broader coverage that includes Ministries, Departments, Bureaus, Offices and Agencies including State Universities and Colleges, Government-owned and controlled Corporations, and Local Government. As mentioned in the previous chapter, among other things, the Procurement Bill promotes value for money, open and effective competition, ethics and fair dealing, accountability and reporting, equity and the establishment and securing of procurement records. The draft bill also contains a comprehensive complaints review mechanism which Lagos does not currently have. The Bill clearly defines the levels of appeal, the time a decision must be taken and the appeal process to be used. Finally, the bill also has provisions on concession contracts which have been absent in the current procurement guidelines.

⁷ Review of Tender Procedures and Regulations in Lagos State, Ref. No. CD/STB/S.177/133, dd 26 November 2007

Institutional Framework and Management Capacity

99. **The organization of the public procurement system in the State of Lagos is decentralized to the extent that each department, parastatal, and Local Government have their own tender boards.** However, the tender boards in Lagos State and the Local Councils are mere recommending bodies for contracts above certain thresholds. Tender boards (TBs) have a limited mandate, with the power to decide contract awards above thresholds de facto resting with the Governor of the State in most cases.

100. **The limited power of TBs leads to the perception of a nontransparent process, political interference, unfairness, non-competitiveness, and corruption.** In a situation where the Governor decides most contract awards, besides causing delay, makes the tender boards inefficient and ineffective and can make procurement unnecessarily expensive. The tender board organization, therefore, is characterized by the lack of responsibility and accountability of the contracting authorities to manage their own resources. There is also an imbalance between contracting parties—the State and the private sector—as there is no complaint mechanism for aggrieved bidders.

101. **The State Tenders Board (STB) comprises of political appointees.** It is made up of seven members appointed by the Governor, four of whom are permanent members: the Commissioner for Economic Planning and Budget, who acts as Chairman, and the Commissioners for Works and Infrastructure, for Finance, and for Justice. The three other members are selected on rotational basis. The Commissioners of the STB, are political appointees and are directly involved in contract award process. These same officials are responsible for the allocation of resources and are also involved in the oversight of how these resources are spent. In a well functioning system, the responsibility to manage these resources would be left to the ministry concerned and the control mechanism given to nonpolitical appointees. Once a law on public procurement is enacted and regulations, manuals and standard bidding documents issued, carrying out public procurement including contract award will clearly be a professionally administrative function the mechanics of which should be disengaged from political appointees.

102. **According to the November 2007 Circular, the Ministries' Tender Boards (MTBs) should comprise of the following members:** the Permanent Secretary (or their representatives) of the Ministries of Works and Infrastructure, Finance, Economic Planning and Budget, Justice; the Permanent Secretary of the procuring ministry/agency; and all Directors or Heads of Directorates in the procuring ministry/Agency. The MTBs are chaired by the Permanent Secretary of the procuring ministry. The MTBs approve contracts below N10 million.

103. **Each State Parastatal has its own Tenders Board, Parastatal Tenders Board (PTB)** comprised of: the Chairman of the Governing Council/Board as its Chairman; two Board Members (on rotational basis); the General Manager of the Parastatal; Head of Finance and Administration; Head of Accounts; Heads of Department/Directorate involved in the project to be considered; representatives from the Parastatal Monitoring Office and Supervising Ministry. A Secretary is provided by the agencies. The PTBs approve contracts below N10 million.

Approval of tendering goes directly to the TBs of the parastatals and those that have Governing Boards constituted for them. Tendering processing follows the same procedure as at the MTB. Approval of recommendations for contract award from the PTB comes from the Governor of the State. Parastatals play a significant role in public procurement in Lagos State because of their number, size, and scope of operations.

104. **A State Consultancy Board (SCB) exists to recommend procurement of consultants, but their value added is not significant.** The Board is made up of 9 members under the Chairmanship of the Commissioner for Works. Its functions are to review appraisals on proposals relating to Consultant services, negotiate with consultants in respect of submitted proposals for consultant services, and recommends fees and other terms of engagement. However, a review of available documentation does not show any value added to the Government resulting from the function of the SCB. Agencies/ministries whose project execution demands the use of consultant services are required to seek and obtain the approval of the Governor of Lagos State and thereafter to advise the SCB for further processing of their request. It should be noted that there are no regulations guiding the whole process of appointing consultants in Lagos State.

105. **Currently, the procurement function is not generally performed by professionally qualified staff.** Procurement officials previously rose to the level of Chief Supply Assistants in the Civil Service hierarchy. Nowadays, procurement functions have been taken over and performed by administrators, and opinions of procurement specialists are usually not sought before contract award decisions are taken. The result is that the few procurement specialists available in the system are not recognized and have not been trained over the years. There is an immediate need to raise the professional standing of procurement staff, their skills, and their reward system to enhance the quality of procurement practice in the State and make it more efficient and effective.

106. **Provisions for staff training are usually included in departmental/ministerial budgets, but funding is inadequate.** Such training is carried out by the Lagos State Public Service Staff Development Centre (PSSDC). Training for officers on grade levels GL 13 and above is funded through a central training budget included in the budget for the Ministry of Establishments. Senior officers sometimes attend custom designed courses run by external consultants, public courses by the Administrative Staff College of Nigeria (ASCON), or workshops/annual conferences mounted by PSSDC or other external bodies. The high cost of training and capacity building, which the proposed reforms entail, should be weighed against the benefits of enhanced capacity and reduction in corrupt practices.

107. **The public service reform is another area that is needed to assure successful procurement reform.** While salaries and benefits of procurement specialists in the public sector compare well with other professionals in the Civil Service, they are not adequate for basic living, and they are much lower than the private sector by approximately 80 percent. The lack of efficiency and low morale of staff are attributed mainly to low salary. Low salaries are believed to be one of the main reasons for fraudulent activity and mismanagement of public funds. The essential aspect of public service reform required in Nigeria (both at the Federal and State Government levels) is rationalization to achieve a leaner, better paid work force, while at the

same time freeing up some of the resources that are at present expended on a bloated public sector.

Procurement Operations and Market Practices

108. **The current thresholds in Lagos State Government, Local Government Authorities, and Parastatal Organizations are considered very low and have a direct impact on the level of efficiency.** While the financial regulations prohibit contract splitting and the procurement guidelines contained in the 2007 Circular are silent on this subject, it was observed that, in some instances, contracts were split to avoid clearance by higher authority—an action that may lose the economy of scale. At present, there is a strong demand from users to increase thresholds to improve the efficiency and effectiveness of the procurement process. Moreover, there is no adjustment mechanism (inflation/price indexing) in the current legislation to compensate for inflation. This situation undermines the authority, power, and potency of the tender boards.

109. **The registration process is purely a money-making exercise for procuring entities and does not serve the purpose of determining the capacity of a supplier, contractor, or a consultant.** The 2007 Circular requires all firms wishing to engage in government contracts to register with the relevant Ministries/Offices/Bureaus and/or Parastatal Organizations. In practice, non-registration does not prevent a bidder from being evaluated. However, the bidder must register immediately after winning the contract. Therefore, registration does not add value to the procurement process. Moreover, there is a lot of confusion among contracting authorities as to whether registration with the State central Registration Board in the Ministry of Works, which was mandatory under a 1995 Circular, still applies.

110. **The regulations and circulars are silent on the use of blacklists.** However, in practice, government establishments take note of contractors who have bad records of performance. Local Governments do the same.

111. **The 2007 Circular requires advertizing for all tenders with estimated contract value of N500,000 (US\$3,300 equivalent) and above in one medium or another. In practice, advertisement in newspaper is seldom done.** The high cost of advertisement in the national newspaper at N100,000 (approximately \$760, full page) has been raised as an obstacle to advertising. Contracts estimated to cost between N500,000 and N5 million (US\$3,330-33,300 equivalent) are advertized at the notice boards of the procuring entities; contracts estimated to cost between N5 million and N10 million (US\$33,300-66,600 equivalent) are advertized at the notice boards of the procuring entities, Alausa Alert and one national newspaper; contracts estimated to cost between N10 million and N50 million (US\$66,600-333,000 equivalent) are advertized at the notice boards of the procuring entities, Alausa Alert, one national newspaper and LASG website. Contracts estimated to cost above N50 million are advertized at the notice boards of the procuring entities, Alausa Alert, two national newspapers and LSG Website.

112. **With regard to the Local Government Authorities, the Financial Memoranda (FM) provides in Section 17.13 that tender shall be invited by open advertisement in the form determined by the Council.** There is no requirement to advertise tendering opportunities in the local media. According to the current practice, tenders are advertised on the notice boards of all

Local Government offices. Advertisement is therefore done at the discretion of the procuring entity.

113. **The 2007 Circular does not require that procuring entities pre-disclose bid evaluation criteria.** In addition, the Circular requires that preference be given to State agencies that participate in a bid exercise. In most cases, criteria not specified in the advertisement (for example, indigenous considerations as well as past working relations with the procuring entity) are taken into account when determining the award of contract. A merit point evaluation system is often used but this is never pre-disclosed. Merit point system can be very subjective and is recommended only for special complex procurements such as information systems. As a result, fairness and transparency of the public procurement process in the State has been greatly undermined. The same situation is true for the Local Governments.

114. **Although the FR and the 2007 Circular provide that bid opening shall be done on the date and the hour at which a particular tender closes, it does not require that bidders or their representatives be present at the bid opening.** The Circular merely states that bidders or their representatives and members of the public may be invited to attend.

115. **In practice, evaluation of bids consists of a simple combination of price and non-price factors including experience on the job, performance, competence, and ability to negotiate on a variety of issues in the case of works, and price and quality in the case of consultant services.** The State Government usually has its price, which is used as a benchmark for negotiating the price of any given contract. There are no specific regulations guiding the determination of profit. Thus, bidders do not know the criterion used by a TB. Information from the State Ministry of Works indicates that between 25 percent and 40 percent profit margin over the government price is usually allowed, given the procurement entities' discretionary power. The implementing agency then compares the price of each bid with the estimated government price and profit margin, and on this basis determines whether a bid is low or high. The 2007 Circular states that TBs should be free, when the need arises, to appoint an ad-hoc technical subcommittee. The subcommittee should comprise experts from the public service and, when necessary, receive technical advice from private consultants. The subcommittee prepares and submits an appraisal report to the tender board that appoints it. Section 17.15 of the FM requires local authorities to award contracts to the lowest priced tender. Basing contract award on the lowest price only is not advisable because the lowest priced bidder may not necessarily be competent or might have incorrectly priced the bid.

116. **The selection of consultants at the State Government or Local authorities level does not prohibit conflict of interest with prior or existing obligations to clients.** Under Section 1 of the Code of Conduct for Public Officers, which is contained in Part 1 of the Fifth Schedule to the Federal Constitution, public officers are required not to put themselves in a position that conflicts with their duties and responsibilities. However, circumstances that may lead to a conflict of interest situation are not spelled out in the Code. There are no provisions either in the State FR or the 2007 Circular requiring a member of a tender board or a Tender Evaluation Committee to declare any conflict of interest in regard to any tender that is to be deliberated upon. Due to the lack of the requirement to declare a conflict of interest, decisions on tenders are sometimes made by people whose judgment is clouded by the interest that they have in the

tender before them, and this bias makes the procurement process most unfair and uncompetitive. In Local Government Authorities, there are no such provisions either.

117. **Award of contracts in Lagos is highly centralized.** As indicated earlier, contract award for competitive bidding above Naira 50 million is the sole responsibility of the State Executive Council under the chairmanship of the Governor. The tender boards are mere recommending bodies, and the procuring entity has no means to appeal the decision of the Governor. The relevant tender board recommends to the procuring entity which tender must be awarded subject to the approval of the Governor of the State. The requirement that the Chief Executive of the State approve contract awards gives room for political interference in the procurement process. Political interference often clouds the procurement process leading to unfairness as well as non-competitiveness, both of which can make procurement unnecessarily expensive. The time that the Governor spends on the day to day approval of contract awards may deprive him of the opportunity to address strategic matters which are of much more importance to the people of Lagos. For instance, for every contract above N10 million (equivalent to about US\$70,000), the Governor makes three different approvals: (i) at the initiation of the procurement process; (ii) at the recommendation of contract award by the procuring entity; and (iii) at final recommendation of the STB. While this appears as a tight control mechanism, there is no evidence that it reduces corruption. At the Local Government Authority level, the FM in Section 17.11(c) provides that it shall no longer be necessary to refer any contract, whatever the size, to any organ or functionary of the State. However, the Administrative Guidelines for Local Governments issued by the State Ministry of Local Government states that, for expenses exceeding N1 million, such approvals should be sought from the Governor. The former provision is a Federal instruction while the latter is a State instruction. There is controversy as to which should supersede.

118. **One of the main reasons given for not shifting the contract award responsibilities from the Governor’s office to the procuring entities is this lack of capacity and the need to build such capacity before shifting the responsibilities.** Due to lack of a procurement professional cadre in the service, procurement capacity at the ministries and parastatals is limited. In this context, the Government has indicated that it would introduce a decentralized procurement system if development partners were to assist in building capacity at the MDA level.

119. **Current practice on contract agreement leads to unnecessary increases in contract prices.** As stated in the 2007 Circular, payment of an agreement fee, based on the contract value, is required prior to a contract agreement signature. The payment rate is set by the Ministry of Justice. The Circular also states that the rates can be revised by the procuring entity without prior notice. Table 11 shows how the various rates are applied:

Table 11: Agreement Fee Percentages

<i>Value of contract</i>	<i>Agreement fee (%)</i>
5m–20m	0.25
21m–50m	0.50
51m–100m	0.75
101m–above	1.0

120. **There is no obligation in the FM or the Administrative Guidelines requiring Local Government Authorities to publish contract awards.** Section 4018 of the FR provides that, after a contract has been entered into, the name of the successful tenderer and the nature of services to be rendered will be published in the official Gazette. The Circular is silent on this matter. In practice, as the official Gazette is not published regularly and, when published, is not readily available, the public hardly can have information on contract awards in the State.

121. **However, the Government has recently published contracts awarded between 2007 and 2009 on the website.** The contract awards have been published on the website of the Lagos State Tenders Board showing the winning bidder, contract value, and percentage share of the contract value that was paid in advance. This sends a strong signal about the Government's commitment to transparency and accountability.

122. **Beyond the publication of contract awards, it would be useful in the near future to conduct a comparative analysis of unit costs.** Such an analysis would show, for example, how the cost of constructing a kilometer of road in Lagos compares to Mumbai or Nairobi. Its findings would then lead towards a determination of whether any unusually high unit costs are due to economy-wide factors such as inflation, inadequate competition during the procurement process, or delays in the commencement and implementation of projects that result in cost overruns. Ultimately, such information is useful as it helps to determine if taxpayers are getting value for money and what measures need to be undertaken especially in the area of procurement, in order to improve efficiency in the delivery of public services.

123. **Large advances are paid to contractors which are usually difficult to recover in the event of non-performance.** Advance payment generally ranges between 30 percent and 70 percent, depending on the nature of the contract. In the large majority of the contracts reviewed, the advance payment was 70 percent.⁸ However, there have been cases of defaulting contractors after the payment of mobilization. In addition, it has been difficult to recover the advance payment from defaulting contractors because the guarantees used are insurance bonds and, in most cases, the insurance company used is controlled by the Lagos State Government. In cases where private insurance companies have been used, it was possible for the State Government to recover the advance payment by recourse to, or invoking of, the advance payment bond.⁹ However, this remedy was reported to have been used only in isolated cases.

124. **A new system in the administration of advance payments has led to improvements in the execution of projects.** The case made for large advance payments is that they speed up execution if properly administered. Indeed, the LASG has recently instituted a system whereby advance payment is made to the Bank of the contractor rather than the contractor himself/herself. The Bank releases the money to the contractor only after satisfying itself that the contractor has completed the work for which the advance is supposed to be paid. Indications are that this system has worked very well and the State has noticed a marked improvement in the timely completion of contracts. The draft Procurement Bill stipulates an advance payment of 20 percent

⁸ Unnecessary tie-up of public funds in the private sector.

⁹ After a long time and enormous effort was put in by government.

but gives authority to the Regulatory Authority to define higher rates, subject to the Governor's approval.

125. Contractors who have completed their jobs experience delays in payments because of the problem of "cash backing." The cash backing problem arises because of the decision to pay out large advance payments to contractors. As a result, some contractors do face delayed payments on completion of their projects because Government funds are tied up as advance payments to other contracts. There are no guidelines in the FR regarding late payments, but the 2007 states that delayed payment shall be viewed with all seriousness and should be prevented.¹⁰ Since there are no regulations providing remedies for delayed payments, contractors sometimes add 30 percent to 40 percent to the bid price as a "compensation" for delayed payment. The consequence is that bid prices are higher than they would otherwise be.

126. Project monitoring can be said to be undertaken on a regular basis for public sector procurement in Lagos State, as payment at each stage of the contract is contingent on the issuance of a certificate of performance based on the report of this monitoring exercise. The 2007 Circular provides that tender boards must monitor contract execution to ensure that there is no default by the contracting firm. Although the process and level of sanction are not defined in the Circular, it states further that nonperformance with the agreed schedule of work would also be viewed seriously and lead to sanctioning of the contractor as appropriate. The Financial Memorandum (FM) of the Local Government has no provision for contract monitoring. In practice, each agency has a project monitoring committee while the MEPB has a unit charged with the responsibility of monitoring State-wide projects. However, most of these monitoring committees are not effective enough because of inadequacies in staffing, equipment, motivation, and authority.

127. In Lagos State and the Local Councils, recordkeeping is done manually, thereby making it tedious to operate, difficult to store and retrieve, and easy to manipulate. An important ingredient of public procurement is good recordkeeping and management. It is an important basis for ensuring transparency and accountability. The quality of records varies from one department/unit to the other. Generally, the staff handling filing activities are not trained in information management and archiving activities. Furthermore, recordkeeping facilities, such as cabinets and binders, are inadequate. These inadequacies explain why it is very difficult to retrieve records and information on past activities. Colossal numbers of staff hours are spent searching for documents, which time could be used for more productive purposes.

Integrity and Transparency of the Public Procurement System

128. Audit arrears of the States' Financial Account have been cleared and the audit of the LSG accounts is current. As mentioned earlier, Lagos State has over the last three years met the constitutional requirement on the Auditor General to submit the audited reports to the Legislature within 90 days of receipt of the financial statement from the Accountant General. This has mainly been due to the installation of the Oracle system which has enabled timely preparation of final accounts and hence timely auditing.

¹⁰ There are no clear guidelines/process for dealing with such issues in the Circular.

129. **Although the Auditor General has been mandated to carry out procurement audits, this has not been sufficiently done because of capacity constraints.** According to the guidelines, the Auditor General is responsible for auditing of all public expenditure¹¹ and shall report on this to the Assembly. The functions of the Auditor General include auditing of the procurement function to verify compliance with procurement procedures. However, at the moment, there is no capacity in the Auditor General's office to undertake comprehensive procurement audits.

130. **As reported earlier, there is no provision for administrative review of bidders' complaints at State and Local Government levels, but this will change once the new bill has been passed into law and the relevant provisions are operational.** Currently, bidders who want to complain are directed to address their complaints to the procuring entity concerned. Many bidders shy away from complaining for fear of never being awarded a government contract again. The reason is that award of government contracts is perceived to be part of the sociopolitical reward system and the prerogative of those in power. Most contractors would rather wait their turns to win rather than be seen as working against the government by complaining the loss of contracts.

131. **Overall, procurement carries a high risk of providing fertile ground for corruption in Lagos State, as is usually the case elsewhere.** It is estimated that 90 percent of corruption cases are related to procurement. These cases are detected through observing blatant violations of laid down procedures. Legislation at the Federal level has had positive impact on reducing corruption. Unfortunately, many cases taken to court using this legislation have been unsuccessful due to antiquated court procedures. Out of a total of 200 cases prosecuted, only 13 cases were convicted. In a Survey¹² of Private Sector Perception of Public Sector Procurement Reforms, in 2007/2008, the following observations were made on the performance and integrity of government procurement institutions and factors that play an important role in winning government contracts. "Most of the firms (62.5 percent) had the perception that contracts were pre-determined and won by paying a bribe. These firms believed they had no chance of winning. More specifically when asked about the underlying reasons, about half of the surveyed firms indicated that companies with influence and power repeatedly won contracts and those with connections are favored by government procurement policies and procedures. About 40 percent of the respondents felt that government procurement policies and procedures favor only the large and medium firms. About 37 percent of the respondents believe that the policies favor firms of all sizes. A majority of the respondents believed that both foreign and indigenous firms are favored by present government procurement policies. Even more so than the fact that tendering is burdensome and costly for contractors, firms without any of those perceived qualities to win bids are to express interest in government procurement.

132. **There is no exclusive anticorruption legislation in Lagos State similar to the Independent Corrupt Practices and other Related offences (ICPC) Act, although the criminal provisions in the Criminal Code address some of these issues.** However, Section 98 of the Criminal Code prohibits official corruption and bribery. Section 209 of the Federal Constitution requires that all persons in the public service of a State observe and conform to the

¹¹ PFA Article 30 (1)

¹² Bayo Awosemusi - Survey of Private Sectors' Perception of Public Sector Procurement Reforms, April 20, 2008

Code of Conduct for Public Officers, which is contained in the Fifth Schedule to the Constitution.

133. **Efforts are now at an advanced stage to set up relevant institutions in Lagos State for curbing procurement related corruption.** The ICPC act provides for an Independent Corrupt Practice Commission to which citizens can report instances of corruption, which the Commission can investigate. The Commission has recently set up office in Lagos State. One of ICPC's anticorruption initiatives is to set up Anticorruption and Transparency Monitoring Units in every MDAs. This arrangement seems to have produced positive results at the Federal level. The LSG Head of Service has already approved this proposal and the process of setting up these units has started.

Conclusion and recommendations

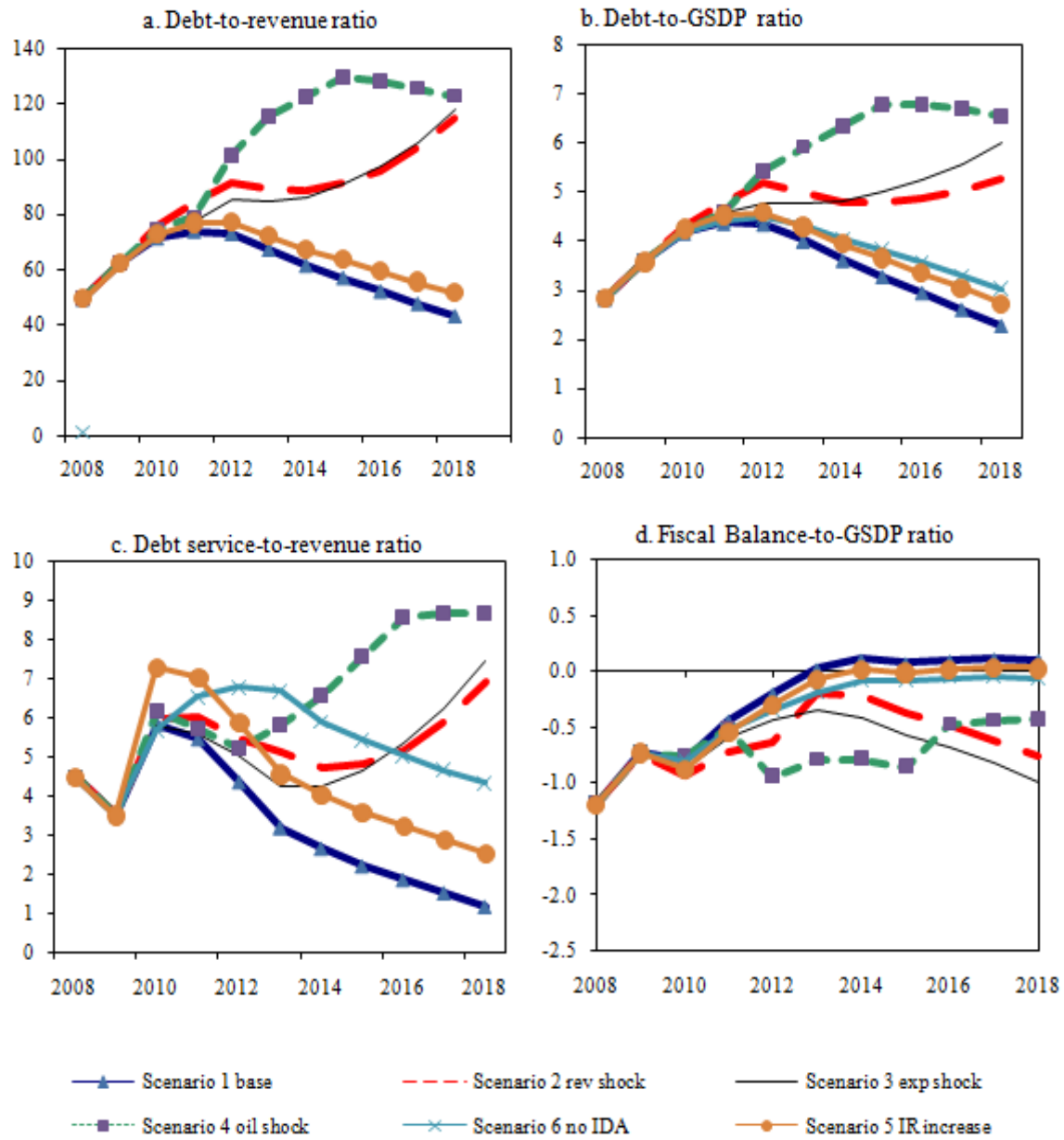
134. **It is clear from the foregoing analysis that the Lagos State procurement system is beset with many weaknesses and will therefore require far-reaching reforms.** The absence of a state procurement law is a major handicap that has led to reliance on administrative guidelines that do not conform to best practice. In spite of Government efforts to curb procurement related corruption, the high centralization of the procurement process renders it inefficient and susceptible to perceptions of corruption and political interference. It is also clear that capacity challenges at the technical level are immense and responsible for current procurement practices.

135. **In this context, the following recommendations are suggested:**

- Finalize the Procurement Bill and ensure that it conforms to international best practice. One such best practice needs to be decentralization of the procurement function to Procuring Entities (PEs) in ministries and parastatals, and the establishment of a state-level office with regulatory and oversight functions;
- Speed up the process of passing the Procurement Bill into law;
- Develop and implement a procurement reform program based on the new procurement law. The reform program must include a capacity building plan based on a comprehensive assessment of training and material support needs;
- Undertake an analysis of unit costs on major projects across sectors and compare them with other cities.

ANNEXES

Figure 9: Lagos Fiscal and Debt Indicators under Alternatives Scenarios, 2008-2018



Sources: LASG authorities; and staff estimates and projections.
 1/ Revenues are defined inclusive of federal transfers

Table 13: Lagos Projections for Key Fiscal and Debt Indicators 2008-2018 under Alternative Scenarios

	Projections										
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Debt-to-Revenue Ratio											
1. Baseline	49	62	71	74	73	67	62	57	52	48	43
2. Revenue growth at 50 percent of base	49	62	75	84	91	89	89	91	96	104	115
3. Increase in non-interest recurrent expenditure by 2.5 of base	49	62	73	77	85	85	86	91	97	106	118
4. Drop in oil prices to \$40 per barrel	49	62	75	79	101	116	123	130	128	126	123
5. Higher Real Interest Rates	49	62	73	77	77	72	67	64	59	55	52
6. No IDA financing	49	62	71	75	80	77	73	70	66	63	60
Debt-to-GDP Ratio											
1. Baseline	3	4	4	4	4	4	4	3	3	3	2
2. Revenue growth at 50 percent of base	3	4	4	5	5	5	5	5	5	5	5
3. Increase in non-interest recurrent expenditure by 2.5 of base	3	4	4	5	5	5	5	5	5	6	6.0
4. Drop in oil prices to \$40 per barrel	3	4	4	5	5	6	6	7	7	7	7
5. Higher Real Interest Rates	3	4	4	5	5	4	4	4	3	3	3
6. No IDA financing	3	4	4	4	4	4	4	4	4	3	3
Debt Service-to-Revenue Ratio, Interest only											
1. Baseline	4	4	6	5	4	3	3	2	2	2	1
2. Revenue growth at 50 percent of base	4	4	6	6	5	5	5	5	5	6	7
3. Increase in non-interest recurrent expenditure by 2.5 of base	4	4	6	6	5	4	4	5	5	6	7
4. Drop in oil prices to \$40 per barrel	4	4	6	6	5	6	7	8	9	9	9
5. Higher Real Interest Rates	4	4	7	7	6	5	4	4	3	3	3
6. No IDA financing	4	4	6	7	7	7	6	5	5	5	4
Fiscal Balance-to-GSDP Ratio											
1. Baseline	-1.19	-0.73	-0.80	-0.45	-0.21	0.02	0.10	0.07	0.09	0.11	0.10
2. Revenue growth at 50 percent of base	-1.19	-0.73	-0.94	-0.73	-0.63	-0.20	-0.22	-0.37	-0.48	-0.61	-0.76
3. Increase in non-interest recurrent expenditure by 2.5 of base	-1.19	-0.73	-0.87	-0.59	-0.43	-0.34	-0.42	-0.57	-0.69	-0.82	-1.00
4. Drop in oil prices to \$40 per barrel	-1.19	-0.73	-0.76	-0.51	-0.94	-0.79	-0.78	-0.85	-0.47	-0.43	-0.42
5. Higher Real Interest Rates	-1.19	-0.73	-0.88	-0.54	-0.30	-0.07	0.02	-0.01	0.01	0.03	0.03
6. No IDA financing	-1.19	-0.73	-0.80	-0.53	-0.35	-0.19	-0.08	-0.09	-0.05	-0.04	-0.06

Table 14: Lagos FSA Sensitivity Analysis: Assumptions for Alternative Scenarios

	Actual		Projections						
	2008	2009	2010	2011	2012	2013	2014	2015	2016
Assumptions									
Baseline									
Real GSDP growth, %	-2.8	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Oil price, \$	97.0	62.0	70.0	74.0	77.0	79.0	82.0	83.0	85.0
Oil production, mn bpd	2.1	2.2	2.1	2.2	2.3	2.5	2.6	2.7	2.8
Real growth in IGR, %	18.4	19.9	8.0	7.0	7.0	7.0	6.0	6.0	6.0
Real growth in federal transfers, %	25.5	-17.5	9.9	9.7	7.5	4.8	2.0	-0.7	0.3
Real growth in recurrent non-interest expenditure, %	3.7	0.1	2.0	2.0	2.0	3.0	3.5	3.5	3.5
Real growth in capital expenditure, %	70.0	-0.1	9.8	1.7	4.7	3.2	3.6	5.6	4.4
Lower revenue growth (at 50 percent of base)									
Real GSDP growth, %	-2.8	6.0	5.4	5.4	5.4	5.4	5.4	5.4	5.4
Oil price, \$	97.0	62.0	70.0	74.0	77.0	79.0	82.0	83.0	85.0
Oil production, mn bpd	2.1	2.2	2.1	2.2	2.3	2.5	2.6	2.7	2.8
Real growth in IGR, %	18.4	19.9	4.0	3.5	3.5	3.5	3.0	3.0	3.0
Real growth in federal transfers, %	25.5	-17.5	9.9	9.7	7.5	4.8	2.0	-0.7	0.3
Real growth in recurrent non-interest expenditure, %	3.7	0.1	2.0	2.0	2.0	3.0	3.5	3.5	3.5
Real growth in capital expenditure, %	70.0	-0.1	9.8	1.7	4.7	-7.1	3.6	5.6	4.4
Higher growth in non-interest recurrent expenditure (2.5 times of base)									
Real GSDP growth, %	-2.8	6.0	6.0	6.0	5.4	5.4	5.4	5.4	5.4
Oil price, \$	97.0	62.0	70.0	74.0	77.0	79.0	82.0	83.0	85.0
Oil production, mn bpd	2.1	2.2	2.1	2.2	2.3	2.5	2.6	2.7	2.8
Real growth in IGR, %	18.4	19.9	8.0	7.0	7.0	7.0	6.0	6.0	6.0
Real growth in federal transfers, %	25.5	-17.5	9.9	9.7	7.5	4.8	2.0	-0.7	0.3
Real growth in recurrent non-interest expenditure, %	3.7	0.1	5.0	5.0	5.0	7.5	8.8	7.0	7.0
Real growth in capital expenditure, %	70.0	-0.1	9.8	1.7	(5.8)	3.2	3.6	5.6	4.4
Drop in oil prices to \$40 per barrel									
Real GSDP growth, %	-2.8	6.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Oil price, \$	97.0	62.0	40.0	40.0	40.0	40.0	40.0	40.0	40.0
Oil production, mn bpd	2.1	2.2	2.1	2.2	2.3	2.5	2.6	2.7	2.8
Real growth in IGR, %	18.4	19.9	8.0	7.0	7.0	7.0	6.0	6.0	6.0
Real growth in federal transfers, %	25.5	-17.5	-37.2	3.8	3.3	2.1	-1.7	-1.9	-2.1
Real growth in recurrent non-interest expenditure, %	3.7	0.1	2.0	2.0	2.0	2.5	2.5	2.5	3.0
Real growth in capital expenditure, %	70.0	-0.1	-1.1	1.7	4.7	-8.3	3.6	5.6	-8.7
Higher Real Interest Rate									
Real GSDP growth, %	-2.8	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
Oil price, \$	97.0	62.0	70.0	74.0	77.0	79.0	82.0	83.0	85.0
Oil production, mn bpd	2.1	2.2	2.1	2.2	2.3	2.5	2.6	2.7	2.8
Real growth in IGR, %	18.4	19.9	8.0	7.0	7.0	7.0	6.0	6.0	6.0

REFERENCES

- DFID (2009), *PFM Performance Measurement: Public Expenditure and Financial Assessment*
- International Management Consultants Limited (2009), *Development of Capacity to Prepare and Implement Budgets in a Medium Term Expenditure Framework*, Lagos Metropolitan Development and Governance Project
- Lagos State Government (2009), *Abridged Annual Budget: Budget of Accelerated Growth*
- Lagos State Government (2005, 2006, 2007, 2008), *Report of the Accountant-General: Financial Statement*
- Nigeria Federal Government, *Sub-national Borrowing Guidelines 2008-2012*, Debt Management Office
- UNDP (2009), *Human Development Report Nigeria 2008-2009: Achieving Growth with Equity*, UNDP
- World Bank, *PREM Note Number 64: Monitoring Fiscal Risks of Sub-national Governments*
- World Bank (2007), *Lagos State: State Finances Review and Agenda for Action*