

Abia State Government Domestic Expenditure Arrears Clearance Framework

SECTION 1: Introduction

Abia State Government domestic expenditure arrears are financial obligations that have been incurred by the government of the state, for which payments have not been made by the due date. Accumulation of expenditure arrears by governments can have a serious negative effect on the domestic economy; a large flow of arrears may disguise the true size of government deficit, significantly reduce the impact of fiscal policy on aggregate demand and potentially undermine macro-economic stability. Therefore, the control, management and clearance of these arrears must be given a priority.

This framework summarises the planned actions the domestic expenditure arrears clearance, designed to be consistent with maintaining macroeconomic stability, anchored on inclusive growth and transparent implementation.

1.1 Coverage and Scope of the Framework

This document covers the policies guidelines and procedures for managing and settling domestic expenditure arrears for the government of Abia State. The framework is set on the premise of gradual settlement of accumulated arrears of the government of Abia State, while also preventing further additions. Thus, the arrears clearance framework sets out the procedures for managing and settling the domestic expenditure arrears of the State Government.

Payments may be overdue based on a legal obligation (such as payment of social security benefits, or salaries), a specific contractual commitment (such as payment for construction of a road), or a continuing service arrangement (such as payment for electricity supply).

The main categories of expenditure arrears are as follows:

- Contractors' arrears.
- Pension and gratuity arrears
- Salary arrears and other staff claims.

1.2 Purpose of the Framework

This framework document is aimed at providing practical guidance for the identification, recording and management of domestic expenditure arrears the State. Thus the framework will achieve the following:

- Assist the State to establish processes and systems to reduce her stock of domestic arrears,
- Providing room for feedback mechanism from the contractors and interested parties
- Stimulate and improve public participation in governance.

1.3 Users of the Framework Document

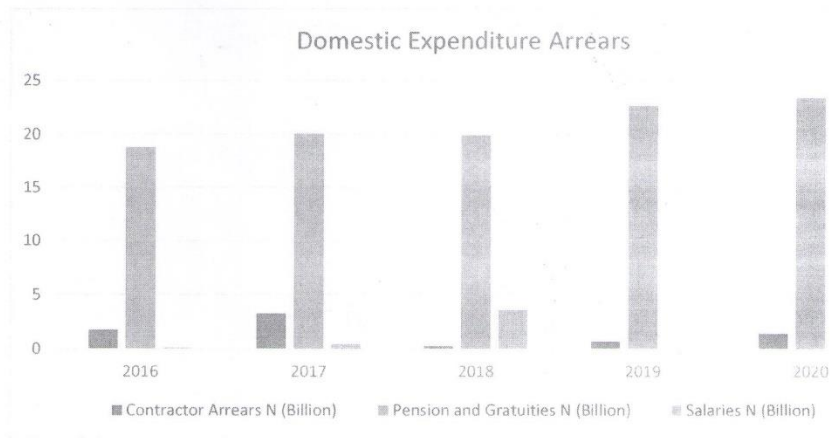
The framework document is developed mainly for the government of Abia State. The framework is thus useful to the staff of state MDAs such as

- Ministry of Finance,
- Office of the Accountant-General,
- Ministry of Budget and Planning/State Planning Commission,
- Debt Management Department,
- Abia State Pensions Boards/Commission,
- Office of the State Auditor-General,
- State Bureau of Public Procurement,
- Ministry of Works and Transport and other line MDAs,

1.4 Total Stock of State's Domestic Expenditure Arrears

Table 1: Domestic Expenditure Arrears

Arrears Type	2016	2017	2018	2019	2020
	NGN	NGN	NGN	NGN	NGN
Contractor Arrears	1745218632	3277899404	276298671. 9	734357826. 7	1430722671
Pension and Gratuities	1879844195 9	2010601383 5	1988860189 4	2268832631 9	2343499842 1
Salaries	132492054. 4	486144816. 1	3640968585	11895293.6	64826354.5 8



Abia State domestic expenditure arrears have been on the increase hence the need for the arrears clearance framework. While salaries arrears have been decreasing, pension and gratuities obligation have been rising in recent years, reaching 23 billion in 2020.

1.5 Description of General Policy on Arrears

The State Government shall adopt the following measures to clear her existing arrears and prevent accumulation of new ones:

- Strengthen legal and regulatory framework.
- Enhance the credibility and realism of the State's budget. The state's budget shall be a realistic plan for expenditures based on conservatively estimated revenues. The borrowing limit shall include a margin to handle the situation of revenue shortfalls.
- Improve accounting and reporting.
- The State shall facilitate improved and integrated cash and debt management.
- Establishment of Treasury Single Account (TSA) to reduce the State's reliance on commercial bank loans.
- Payment shall be centralized to the State's Treasury to prevent arrears as a result of administrative hurdles;
- Upgrading the government's financial management information systems. The system should handle the entire expenditure chain, including the release of budget funds, commitments against the budget funds, production of purchase orders, receipt of goods and services claimed in the invoices, and payment or non-payment of invoices;

- Quarterly Cash management meeting shall be held to guide the government decision on budget and fund releases.

SECTION 2: Planned Actions for Settlement of Domestic Expenditure

Arrears

Abia state government will use the arrears clearance framework to settle the accumulated domestic expenditure arrears. The ACF will communicate to stakeholders the government's plan, timetable and criteria for the liquidation of arrears. This will ensure transparency of the process.

Abia State multi-years' funding plan is the financial plan of the State for the clearance of the stock of arrears based on the total fund available in the State's current budget year and the budget years to come. The state planning commission with inputs from ministry of finance, 3year Medium Term Expenditure Profile (MTEF) every year where budget provisions are made for MDAs to execute projects and to pay debts that may emanate from such projects. Similarly, the MDAs prepares a multi-year funding plan taking into account the stock of debt, priorities and available/expecting cash inflow of the state.

The multi year funding plan are used to record, verify and report the domestic arrears. In addition to the multi-year funding plan, an online comprehensive domestic expenditure arrears register shall be maintained by the MDAs with the database residing in the DMO.

Rate of arrears reduction: The 2020 arrears clearance framework is set on the target of a reduction of domestic expenditure arrears of 5% in 2021 and 20% in the years that follow. It is also based on the assumption that there will be no new domestic expenditure arrears for the next five years. This rate of reduction is the computational mechanism for the multi-year funding plan.

Major Sources of Funds for Settling Arrears

There are two major sources of funds available for settling the arrears. The state's estimate of total funds available to clear arrears will include any or all these sources:

- I. The Internally Generated Revenue (IGR), Federal Transfers, Grants and a one-off revenues such as the Paris Club refund. The proportion of the fund available to clear the arrears will depend on how much comes into the state purse from the above and the

ability to control other competing state's expenditures e.g. personnel costs, pensions and gratuities. As the country recovers from the covid19 induces recession, the state is projecting strong growth in IGR. Such growth could reach 50% in the first two years (2021 and 2022). The ACF is however based on a moderate projection of 25% IGR growth rate. Growth in IGR will expand the fiscal space for the state to meet up with the commitment of clearing the domestic expenditure arrears as shown in tables below.

II. Borrowings

- a. Such as Federal government financial assistance in form of loans to states for the purpose of settling accumulated and backlogs of domestic arrears.
- b. Commercial bank loans: the DMO will enters into negotiation with commercial banks to obtain loans at competitive market rates to fund infrastructural developmental projects. This will reduce pressure on the IGR and allows for payment of domestic arrears.
- c. Bond Issue: Another funding alternative that is available to the government is issuance of state bond to finance capital projects and to fund budget gap. However, proceeds from such bond issue can only be used for specified projects and arrears that might accrued from such projects as approved by Security and Exchange Commission (SEC)

III. Verification: Verification of the debt is another strategy for reducing those arrears and auditing. The exercise will lead to a clean database of those owed by the state. Pension numbers stood at 7,819 in February 2019. The verification exercise being carried out is likely to reduce the number significantly. This verification is being extended to the civil service, hence reduction in personnel cost of the state and thus reduce general recurrent expenditures.

Based on the above processes, the Multi-Year Funding Plan for clearing the domestic arrears for Abia State for the years 2020 – 2025 is as shown in the table below.

STATE Simplified Multi-year funding plan for clearing domestic expenditure arrears

NOTES All numbers are presented in billion naira
All input cells are coloured pink
All calculation cells are coloured yellow
All linked cells are coloured blue

Domestic Arrears Clearance Financing Targets	Value	Notes
Finance (some) clearance of arrears from budget surplus?	Yes	
Finance (some) clearance of arrears through formal debt	Yes	
Target domestic expenditure arrears percentage decline (minimum)	10.0 %	State Target - shown here is the basic target of the SFTAS DLI#8

Fiscal Projection Assumptions [IF NO STATE MTEF FIGURES AVAILABLE]	Value	Notes
Annual percentage growth in revenue - FAAC and VAT (nominal)	5.0 %	State MTEF - shown here is national nominal GDP growth
Annual percentage growth in revenue - IGR (nominal)	25.0 %	State MTEF/IGR Policy - shown here is basic target for SFTAS DLI#4 on IGR
Annual percentage growth in recurrent expenditure - non interest (nominal)	3.0 %	State MTEF/Fiscal Policy
Annual percentage growth in capital expenditure (nominal)	5.0 %	State MTEF/Fiscal Policy - shown here is national nominal GDP growth
Balanced Budget i.e. no budget deficit in the future (budget surplus allowed)	Yes	State MTEF/Fiscal Policy

SUMMARY BUDGET FRAMEWORK	Fiscal Year					
Billion Naira	2020 Actual	2021 Proj	2022 Proj	2023 Proj	2024 Proj	2025 Proj
Total Budget Revenue and Grants	94.24	103.10	105.87	116.14	94.79	107.31
<i>Total Net FAAC allocation exc VAT</i>	32.11	33.71	35.40	37.17	39.03	40.98
<i>VAT</i>	13.90	14.59	15.32	16.09	16.89	17.74
<i>IGR</i>	15.92	19.90	24.88	31.10	38.87	48.59
<i>Grants and Other Revenue (inc. one-off items such as Paris Club refund)</i>	32.31	34.89	30.27	31.78	0.00	0.00
Total Budget Expenditure	105.37	87.06	90.42	93.91	97.55	101.34
<i>Personnel Cost and Pensions</i>	32.35	33.33	34.32	35.35	36.42	37.51
<i>Other Recurrent (Overheads, Transfers) exc. interest payments</i>	15.94	16.42	16.92	17.42	17.95	18.48
<i>Interest Payments & other recurrent debt charges</i>	21.53	0.00	0.00	0.00	0.00	0.00
<i>Capital expenditures</i>	35.53	37.31	39.18	41.13	43.19	45.35
<i>Expenditure adjustments (to achieve budget target)</i>	0.00	0.00	0.00	0.00	0.00	0.00
Overall Balance	-11.13	16.04	15.45	22.22	-2.76	5.96

SUMMARY Borrowing, Financing and Debt Stock	Fiscal Year					

Total Debt Stock	30.87	23.68	18.95	15.16	12.13	9.70
Total Debt Stock annual change	0.00	-7.18	-4.74	-3.79	-3.03	-2.43

	2020 Actual	2021 Proj	2022 Proj	2023 Proj	2024 Proj	2025 Proj
Domestic Arrears Dynamics						
Annual change in domestic arrears stock (naira billion)	0.00	-1.25	-4.74	-3.79	-3.03	-2.43
Annual percentage in domestic arrears stock (%)	0%	5%	20%	20%	20%	20%

SECTION 3: PRIORITIZATION CRITERIA FOR ARREARS TO BE SETTLED

Once a database of valid claims on government has been established, a set of criteria for prioritizing their liquidation should be determined. The prioritization of arrears clearance should be based on transparent criteria; depending on the nature of the arrears, these might include the following:

- Socioeconomic impact: Arrears to economically sensitive or vulnerable sectors, such as salaries of low-income workers, pensions, and social benefits, will be prioritized.
- Age of Debts: Older obligations will be priority over newer obligations.
- Cost: Arrears that accrue interest and penalty charges will be priority.
- Risk: Arrears that may result in legal action, disruption of essential services, or cost escalation of future supplies to government will be prioritized.
- Creditor: The government will prioritize the clearance of intra government debts, as this can be done administratively through the annual budget at minimal net cost

There are two approaches to prioritisation:

- Approach 1: Allocation of available fund among the types of the arrears in proportion to their share of the total outstanding stock of arrears.
- Approach 2: Allocation of available funds to a particular type of arrears at a time or one after the other.

The two approaches is combined to great effect in the clearance of the state arrears. Details of how this is to happen in the coming years is presented below.

Table 3: Approach to Prioritisation of the State Domestic Arrear

Criteria	Rationale	Data Required*
CONTRACTORS		
Smallest first	This will allow many individual arrears to be paid immediately and focuses funds on small firms that may be vulnerable to cash flow problems.	Value of outstanding arrear
PENSIONS AND GRATUITIES		
Oldest first	Largest injury (in terms of delay) is addressed first	Date missed payment was due
SALARIES		
Oldest first	Largest injury (in terms of delay) is addressed first	Date missed payment was due

SECTION 4: ORGANIZATIONAL/INSTITUTIONAL ARRANGEMENT

4.1 Description of the Organizational/Institutional Arrangement for Implementation of the Framework

In order to ensure proper implementation of the framework, Abia State set up a Domestic Arrear Clearance Committee as an institutional arrangement saddled with the main responsibility of arrears clearance process, including recording, verification, classification, reporting, prioritization and clearance of the state government's domestic expenditure arrears as well as oversee the work of the state government towards actualizing the SFTAS DLI 8. The committee is guided by the terms of reference as stated below.

4.2 Objective and Responsibilities of the Committee

The Domestic Arrears Clearance Committee will support the Accountant-General of the state in its responsibility for accurate recording, verification, and reporting of domestic arrears across all types. The committee shall discharge the following specific duties, but not limited to them:

1. Establishment of specific guidelines setting out the roles and responsibilities of individuals and institutions for recording of domestic arrears (the roles and responsibilities of each Primary Record Holder, i.e. the entity primarily responsible for keeping the records for each type of arrears). This will include specific reporting requirements, i.e. the use of agreed timelines for submission to the Committee, for instance monthly.
2. Establishment of specific guidelines setting out the roles and responsibilities of individuals and institutions for the verification of domestic arrears balances (the roles of designated officers or verifiers). This will include reporting requirements, that is, a validated copy of the agreed recording templates and any supporting schedules and timelines for submission to the Committee, for instance monthly.

3. Setting up, maintenance and regular monthly update of an accurate internal domestic expenditure arrears database and the publicly accessible online version of the database with a feedback mechanism in place.
4. Oversight of the overall recording, verification and reporting processes for domestic expenditure arrears to ensure that they meet the requirements of DLI 8 as described in the SFTAS Verification Protocols.
5. Ensure adequate classification of the arrears for prioritization purposes.
6. Develop the State's Arrears Clearance Framework (ACF), including policies on prioritization and clearance arrears.
7. Ensure accurate monthly, quarterly and annual reports that present the true position for verified domestic arrears and the progress made in implementing the State's ACF.
8. Provide data/documentation to support the verification of SFTAS DLI 8, including the State's Arrears Recording, Verification and Clearance Report.

4.3 Monitoring and Reporting of the Arrangement

The Committee will report directly to the State's Governor through the Honourable Commissioner for Finance. Table 1 shows the composition of committee members.

Table 1: Membership of the Committee

S/N	TITLE	POSITION
1	Commissioner for Finance	Chairman
2	Economic Adviser to the Governor	Alternate Chairman
3	Commissioner for Local Government and Chieftaincy Affairs	Member
4	State Accountant General	Member
5	Executive/Permanent Secretary – Abia State Planning Commission	Member
6	Permanent Secretary Establishment and Pensions	Member
7	Executive Secretary – Abia State Pensions Boards/Commission	Member
8	Director General, Abia State Bureau of Public Procurement	Member
9	Director General, Debt Management Office	Member
10	SFTAS Focal Person Technical Assistant Component	Secretary
11	SFTAS Focal Person Program for Result	Member
12	Auditor General for State	Observer
13	Auditor General for Local Government	Observer

4.4 Committee Secretariat

The Committee shall establish a Secretariat to support its work using existing Staff or Units within the Office of the Accountant General and State's Debt Management Office

4.5 Power and Authorities of the Committee

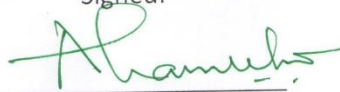
The Committee shall have delegated authority to request any and every information it requires from the MDAs in order to carry out its functions.

The Committee will be able to incur expenditures, including the engagement of professional assistance while executing its role. All expenditures must be incurred through the procurement systems of the selected institution.

4.6 Tenure of the Committee:

The Committee will operate in perpetuity and may be disbanded or reconstituted on the directive of the State Executive Governor.

Signed:



Dr. Aham Uko

*Commissioner for Finance
Abia State*