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**INTERNATIONAL DEVELOPMENT ASSOCIATION**

# PROGRAM DOCUMENT

# FOR A PROPOSED DEVELOPMENT POLICY CREDIT

# IN THE AMOUNT OF SDR 53.3 MILLION

# (US$75 MILLION EQUIVALENT)

# TO THE

# FEDERAL REPUBLIC OF NIGERIA

# FOR A

# EDO STATE FISCAL IMPROVEMENT AND SERVICE DELIVERY DEVELOPMENT POLICY OPERATION

**April 6, 2015**

**Global Practice -- Macroeconomics and Fiscal Management, GMFDR**
**Country Department: AFCW2**
**Africa Region**

**FEDERAL REPUBLIC OF NIGERIA – FISCAL YEAR**
*January 1- December 31*

**CURRENCY EQUIVALENTS**

Currency Unit: Nigeria Naira

US$1 = 198 Naira
US$1 = SDR 0.71053510

(Exchange rate effective as of February 28, 2015)

## ABBREVIATIONS AND ACRONYMS

| | |
|---|---|
| AIDS | Acquired Immune Deficiency Syndrome |
| AMCON | Asset Management Company of Nigeria |
| APC | All Progressives Congress |
| CBN | Central Bank of Nigeria |
| CFAA | Country Financial Accountability Assessment |
| CPS | Country Partnership Strategy |
| CRR | Cash Reserve Requirement |
| CSDP | Community and Social Development Project |
| DHS | Demographic and Health Surveys |
| DMB | Deposit Money Bank |
| DMO | Debt Management Office |
| DPC | Development Policy Credit |
| ESFISDO | Edo State Fiscal Improvement and Service Delivery Development Policy Operation |
| ECA | Excess Crude Account |
| EDBMS | Electronic Database Management System |
| EDSG | Edo State Government |
| EFCC | Economic and Financial Crimes Commission |
| EGIS | Edo Geographic Information System |
| EIRS | Edo Internal Revenue Service |
| EITI | Extractive Industry Transparency Initiative |
| EMIS | Education Management Information System |
| EU | European Union |
| FMF | Federal Ministry of Finance |
| FSAP | Financial Sector Assessment Program |
| GDP | Gross Domestic Product |
| GEMS | Growth, Employment and Market in States |
| GFS | Government Finance Statistics |
| GIS | Geographic Information System |
| GNP | Gross National Product |
| HIPC | Heavily Indebted Poor Countries |
| HIV | Human Immunodeficiency Virus |
| HNLSS | Harmonized Nigeria Living Standards Survey |
| IBRD | International Bank for Reconstruction and Development |
| ICT | Information & Communication Technology |
| IDA | International Development Agency |
| IFC | International Finance Corporation |
| IGR | Internally Generated Revenue |
| IFMIS | Integrated Financial Management Information System |
| INTOSAI | International Organization of Supreme Audit Institutions |

| | |
|---|---|
| IMF | International Monetary Fund |
| INEC | Independent National Electoral Commission |
| IPPIS | Integrated Personnel and Payroll Information System |
| IPSAS | International Public Sector Accounting Standards |
| LDP | Letter of Development Policy |
| LGA | Local Government Area |
| LIS | Land Information System |
| MDA | Ministry, Department and Agency |
| MDGs | Millennium Development Goals |
| MBPED | Ministry of Budget, Planning & Economic Development |
| MOE | Ministry of Education |
| MOF | Ministry of Finance |
| MSME | Micro, Small and Medium Enterprises |
| MTEF | Medium-Term Expenditure Framework |
| MTFF | Medium-Term Fiscal Framework |
| MTSS | Medium-Term Sector Strategies |
| NDSA | Niger Delta Social Accountability |
| NEWMAP | Nigeria Erosion Watershed Management Project |
| NIFOR | Nigerian Institute for Oil palm Research |
| NLC | Nigerian Labor Congress |
| PAYE | Pay As You Earn |
| PDP | People's Democratic Party |
| PEMFAR | Public Expenditure Management and Financial Accountability Review |
| PER | Public Expenditure Review |
| PFM | Public Financial Management |
| PIB | Petroleum Industry Bill |
| POS | Point of Sale |
| PPG | Public and Publicly Guaranteed |
| PPP | Public-Private Partnership |
| PSI | Policy Support Instrument |
| PSIA | Poverty and Social Impact Assessment |
| NIFOR | Nigerian Institute for Oil palm Research |
| ROSC | Report on the Observation of Standards & Codes |
| RRA | Rapid Response Agency |
| RRIN | Rubber Research Institute of Nigeria |
| SBMC | School Based Management Committee |
| SDR | Special Drawing Right |
| SEEFOR | State Expenditure and Employment for Results |
| SHoA | State House of Assembly |
| SIFMIS | State Integrated Financial Management Information System |
| SSP | State Strategic Plan |
| SUBEB | State Universal Basic Education Board |
| TVET | Technical and Vocational Education and Training |
| VAT | Value Added Tax |

| | |
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# FEDERAL REPUBLIC OF NIGERIA

## EDO STATE FISCAL IMPROVEMENT AND SERVICE DELIVERY DEVELOPMENT POLICY OPERATION

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**SUMMARY OF PROPOSED CREDIT AND PROGRAM**
**FEDERAL REPUBLIC OF NIGERIA**
**EDO STATE FISCAL IMPROVEMENT AND SERVICE DELIVERY DEVELOPMENT POLICY OPERATION**

| | |
|---|---|
| **Borrower** | Federal Republic of Nigeria |
| **Implementing Agency** | Edo State Government |
| **Financing Data** | IDA Credit<br>Terms: IDA hardened terms<br>Amount: SDR 53.3 million (US$75 million equivalent)<br>Tenor: 25-year maturity; including 5-year grace period; in US dollars |
| **Operation Type** | Two-year programmatic Development Policy Financing Series |
| **Program Development Objective and Pillars of the Operation** | The development objective of the Edo State Fiscal Improvement and Service Delivery Development Policy Operation (ESFISDO) is to support Edo state in the implementation of critical policy and institutional reforms to improve the management of its public resources; increase private sector access to land for investment and improve the quality of education. |
| **Results Indicators** | **Pillar 1: Ensuring Fiscal Sustainability**<br>• A1: Number of taxpayers captured in Edo state's electronic taxpayer (U-TIN) database *(Baseline (2014): 38,000; Target (2016): 120,000)*<br>• A2: Audited civil service payroll with accurate staff numbers[1] *(Baseline (2014): No; Target (2016): Yes)*<br>**Pillar 2: Improving Budget Institutions and Practices**<br>• B1: Percentage of procurement staff in Edo state public service certified *(Baseline (2014): 0%; Target (2016): 30%)*<br>• B2: Operational integrated electronic platform for budget preparation, execution, and reporting *(Baseline (2014): No; Target (2016):Yes)*<br>• B3: Expenditure arrears in relation to total expenditure: *(Baseline (end-2013): 25.6%; Target (end-2016): No more than 10%)*<br>• B4: Number of MDAs for which Medium Term Sector Strategies (MTSSs) are prepared and reflected in the annual budget in consistency with fiscal stability goals *(Baseline (2014): 0; Target (2016): 6)*<br>• B5: Number of months between end of fiscal year and the publication of the state's audited financial statements *(Baseline (2014): 9; Target (2016): 7)*<br>**Pillar 3: Improving Access to Land for Investment**<br>• C1: Land Transfer Fees[2] as a percentage of land value in Edo state *(Baseline (2014):26.4%; Target (2016): 20.4%*<br>**Pillar 4: Improving the Quality of Education[3]**<br>• D1: Number of partnership agreements executed between TVET colleges and private sector actors *(Baseline (2014): 0; Target (2016): 3)*<br>• D2: Percentage of eligible female students in TVET colleges benefitting from TVET- Private sector partnership arrangements *(Baseline (2014): 0%; Target (2016): 50%)*<br>• D3: Percentage of SBMCs monitoring and reporting on teacher and pupil attendance (disaggregated by gender) at basic education level (*Baseline (2014): 0%; Target (2016): 60%)* |
| **Overall Risk Rating** | High |
| **Climate and Disaster Risks** | (i) Are there short and long term climate and disaster risks relevant to the operation (as identified as part of the SORT environmental and social risk rating)? Yes __ No __X__ |
| **Operation ID** | P151480 |

[1] The audited payroll will be devoid of any ghost workers.
[2] Otherwise called "Governor's Consent Fees".
[3] Improvements in accountability at the basic education level as well as improvements in the functionality of TVET education have been used here to proxy improvement in the quality of education.

**IDA PROGRAM DOCUMENT FOR A PROPOSED EDO STATE FISCAL IMPROVEMENT AND SERVICE DELIVERY DEVELOPMENT POLICY OPERATION TO THE FEDERAL REPUBLIC OF NIGERIA**

## 1. INTRODUCTION AND COUNTRY CONTEXT

1. **This proposed Edo State Fiscal Improvement and Service Delivery Development Policy Operation is the first in a new series of two programmatic development policy operations that supports Edo state's medium term strategic plan focused on inclusive growth, employment creation and poverty reduction.** Edo is one of 36 states in Nigeria's federal structure. Like the average Nigerian state, Edo has a population of approximately 4 million people[4]. It is situated in the south-south geo-political zone of the country and is one of the nine oil-producing states, albeit a marginal one. Since 2008, the current administration in Edo has vigorously pursued an infrastructure-oriented growth and employment agenda. The World Bank has supported Edo with a number of different operations during this period[5]. From 2012, the collaboration deepened with budget support in the form of a programmatic series of three development policy operations, each for the sum of US$75 million. The Bank began to provide Edo with development policy support due to the progress Edo had made on its own in implementing its development strategy and its commitment to undertake policy and institutional reforms to support its development agenda. The first operation, which was approved in March 2012 and closed in June 2014, supported Edo's earlier development strategy articulated in the 2009 Edo Vision 2020, which identified high poverty, unemployment, flooding and dilapidated infrastructure as main development challenges. Edo also suffered from weak governance structures, particularly in the management of public finances. The state made appreciable reform gains under that operation in the areas of building a stronger public financial management system, improving institutional arrangements for land registration and strengthening the delivery of technical and vocational education; and it remains committed to an agenda of progressive reforms in these and other areas. There was however a long interval between approval of the first operation and preparation of this one due to a delay in obtaining federal parliamentary approval for the 2011/12 national external borrowing plan. Thus, the original series of three has lapsed and this operation begins a new series of two operations. This operation supports Edo state in the implementation of critical policy and institutional reforms to improve the management of its public resources; increase private sector access to land for investment and improve the quality of education.

2. **Nigeria's economic growth has been relatively stable over the last decade; however this has not always translated into commensurate gains in socio-economic outcomes.** Although growth rates averaged 5 percent in the last couple of years, Nigeria is still making slow progress towards improvements in living standards. Progress towards the achievement of the Millennium Development Goals (MDGs) is slow and at its current pace, Nigeria is unlikely to meet the targets for eradicating extreme poverty and hunger and reducing child and maternal

[4] Lagos and Kano states are the exceptions, each with populations of over 9 million. Most recently, Lagos state has been estimated to have a population of 16 – 21 million.

[5] This includes: NEWMAP, SEEFOR, and NDSA. *Fadama* III, CSDP, and HIV/AIDS have been operational in the state earlier than 2008.

mortality. Based on official poverty numbers[6], progress was made in reducing absolute poverty between 2004 and 2010 but these gains were outstripped by population growth. Inequality is on the rise and there is widening income disparity between the Northern and Southern parts of the country. The rising North-South disparity is exacerbated by the conflict in the North which has curtailed business activities in the North and led to the loss of lives and property. Fiscal pressures have also emerged in view of the increase in illegal oil bunkering in the Niger Delta and the precipitous decline in oil prices in the last quarter of 2014, which has resulted in a decline in oil revenues.

3. **Despite the pressing security and socio-economic challenges in Nigeria, the economy is undergoing structural transformation, which has potential for diversified growth.** The recent rebasing of Gross Domestic Product (GDP) which entailed updating the base year from 1990 to 2010 has provided a more accurate picture of the structure of the economy. By increasing the coverage of emergent sectors of the economy such as services and telecommunications and covering a larger sample size in enterprise surveys, the non-oil sector is revealed to be playing a bigger role than previously estimated. Based on the new GDP numbers, Nigeria is now ranked as the largest economy in Africa and the 26th largest in the world. Aside from the impressive growth rates, inflation has reduced to single digits and the Federal Government has made significant progress in rationalizing spending and maintaining the fiscal balance below 3 percent of GDP as recommended by the Fiscal Responsibility Act (FRA), 2007.

4. **Nigeria's 36 states, which account for over 50 percent of consolidated government revenues and expenditure, play a major role in Nigeria's development.** Each federating unit in Nigeria is guided by the 1999 Constitution which provides rules on revenue sharing and administrative responsibilities. State and local governments combined receive 47 percent of centrally shared oil and gas, customs and corporate tax revenues, and collect independently generated revenues as mandated by government tax laws and are responsible for delivering most of the basic social and infrastructure services in their respective states. State-level initiatives are thus very important for the country's development. A lower administrative level of 774 local governments exists below the states.

5. **Governance is however a major development challenge across all tiers of government in Nigeria.** This is evident in the weak welfare gains accruing to Nigeria's population in spite of considerable resource wealth shared by all tiers of government. Edo, like Lagos, is however one of the Nigerian states that has embraced important governance reforms; particularly transparency, accountability and value-for-money initiatives to support improved service delivery. Bank support through the first DPO and other engagements[7] has been important in this regard. Edo has made good progress in transforming the livelihoods of its citizens following the adoption of its Vision 2020 in 2009 and the successor Edo State Strategic Plan. Prior to 2008, the state had suffered from considerable infrastructure neglect and weak governance structures, particularly in the

[6] The official poverty numbers are from the 2003/4 and 2009/10 Harmonized Nigeria Living Standards Survey (HNLSS). Panel data from two smaller General Household Surveys in 2010/11 and 2012/13 based on a smaller sample which is not representative at the state level indicate that poverty rates in Nigeria are most likely lower than estimated from the HNLSS. This will be confirmed in the 2015/16 HNLSS.

[7] These include the State Employment and Expenditure for Results (SEEFOR), the Niger Delta Social Accountability (NDSA) and the Open Data Operations.

management of public finances. In the last six years however, the state has made great strides in rehabilitating and widening the road network as part of its urban renewal efforts which include improvements in drainage and waste management. The PFM system has also been strengthened and revenue generation efforts have yielded good results. The state has also invested in school rehabilitation, is improving incentives for teachers and is engaged in the redistribution of teachers to rural areas to address skills gaps. It is important that the reform momentum is sustained to entail further improvements in the use of public resources for service delivery. This operation builds on these initial reform efforts and it is expected that the choice of a reform leader like Edo for a DPO would have a demonstration effect on other states of the federation to adopt and nurture important reforms.

# 2. MACROECONOMIC POLICY FRAMEWORK

## 2.1 RECENT ECONOMIC DEVELOPMENTS IN NIGERIA

### Real Sector

6. **The non-oil sector (agriculture, industry and services combined) continues to be the main driver of growth in Nigeria, growing by 7.3 percent in 2014 while total GDP grew by 6.3 percent[8]**. A more realistic assessment of the oil sector's contribution to GDP has emerged with its share dropping from about 40 percent to less than 15 percent of GDP in 2013. The growth of the oil sector has been dampened by the loss in oil output due to breaches of oil infrastructure in the Niger Delta region of the country and more recently the sharp decline in oil prices. This led to a decline in oil sector growth (from -4.9 percent in 2012 to -13.1 percent in 2013). Although growth recovered in 2014 (-1.3 percent in 2014), the drop in prices and slowing demand for Nigerian crude oil has no doubt adversely affected the performance of the sector. This will continue to have broad implications for the economy given the importance of crude oil as the main export commodity and revenue source in Nigeria.

### External Sector

7. **Nigeria's balance of payments position stabilized in mid-2014, but the subsequent sharp decline in oil prices pushed the external balance back into deficit.** Prior to June 2013, the balance of payments had been in surplus for about two years in tandem with strong oil prices. Higher interest rates relative to international standards also attracted a large amount of portfolio capital in late 2012 and early 2013 and increased gross international reserves to US$48 billion in April 2013. However, declines in oil production, the even sharper decline in oil prices and the more cautious attitude of investors in view of these factors has placed downward pressure on the

[8] These growth numbers are based on the outcome of a GDP rebasing exercise concluded in April 2014 and have resulted in the emergence of a more diversified view of the Nigerian economy. The exercise focused not only on updating the base year for measuring Nigeria's GDP from 1990 to 2010 but also included a reclassification of programs and activities in line with the International Standard Industrial Classification (ISIC), the adoption of a larger survey frame with a tenfold increase in the number of firms surveyed and an increase in the coverage of economic activities from 33 to 46. On the basis of the new numbers, the services, industry and agriculture sectors contribute the largest share to GDP.

balance of payments, thus causing a decline in gross foreign reserves to about US$30.3 billion in March 2015.

**Monetary, Exchange Rate, and Financial Sector Policies**

8. **Monetary policy has further tightened in response to increased pressures on external reserves and the exchange rate**. The sustained decline in oil prices since the latter part of 2014 placed the Naira under considerable pressure and resulted in a further tightening of monetary policy. In light of assessed high systemic banking sector liquidity, due to fiscal operations both from budgets and the Excess Crude Account (ECA), and its attendant impact on foreign exchange demand and thus external reserves, the key policy interest rate which had remained unchanged at 12 percent since September 2011 was raised by 100 basis points in November, 2014. In tandem, the Central Bank devalued the Naira on November 25, moving the official exchange rate band from Naira 155 (+/-3%) to the US dollar to Naira 168 (+/-5%); however, it was still trading with a significant premium on the parallel market. Thus, on February 18, 2015, the Central Bank of Nigeria (CBN) closed the official foreign exchange window and now supplies foreign exchange to the markets only through the interbank window. This, in effect, led to a convergence of the official rate and the interbank rate, and the Naira was trading at close to 200 to the US dollar on this market in mid-March. Price and exchange rate stability have been broad goals pursued by the monetary authorities and the main policy tool used to maintain liquidity levels at required rates continues to be reserve requirements rather than open market operations. This is due to the CBN's perception that financial markets are not always rational and a blunt instrument, such as the Cash Reserve Requirement (CRR), is more effective in the case of Nigeria. A separate reserve requirement of 50 percent was introduced for public sector funds in July 2013, which was raised to 75 percent in January 2014 and has been maintained at this level. This was introduced to curb liquidity levels given an over-reliance of Deposit Money Banks (DMBs) on public sector deposits. In response to increased liquidity in the banking system, the CRR on private deposits was increased from 12 percent in January 2014 to 15 percent in March and further to 20 percent in November 2014.

9. **Inflationary pressures have moderated in the last few years, with core inflation dropping to 7.0 percent in February 2015 from 9.9 percent in 2012.** This is in line with the monetary authorities' goal of single digit inflation. The CBN remains committed to maintaining a stable exchange rate and continued to do so in the period following the suspension of the previous CBN governor when the demand for foreign exchange spiked in the context of a sharp decline in monetary reserves and uncertainty about future monetary policy direction. The CBN showed its resolve to defend the Naira, and stability returned to the market within a short period.

10. **The banking sector remains stable and the Nigerian authorities adopted many of the recommendations made in the 2012 Financial Sector Assessment Program (FSAP)**. This includes closer supervision of DMB operations as they expand to other countries within Africa and the proposed winding down of the Asset Management Corporation of Nigeria (AMCON), a Stressed Asset Fund that purchased problematic loans of DMBs during the banking crisis. Increased foreign liability exposure by DMBs and the adequacy of bank equity also require close monitoring. Credit to the private sector is expanding slowly and net domestic credit to the private

sector expanded by 11.3 percent in nominal terms in 2013, higher than the inflation rate of 8 percent, an improvement over nominal growth of 7.4 percent the previous year.

**Table 1: Key Macroeconomic Indicators (2012-2017)**

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|---|
| | Act. | | Projections | | | |
| **National income and prices** | | | | | | |
| Real GDP (at 2010 market prices) | 4.3 | 5.4 | 6.3 | 4.8 | 5.0 | 5.3 |
| Oil and Gas GDP | -4.9 | -13.1 | -1.3 | -1.6 | -1.4 | 0.1 |
| Non-oil GDP | 5.9 | 8.3 | 7.3 | 5.5 | 5.6 | 5.8 |
| Production of crude oil (million barrels per day) | 2.34 | 2.19 | 2.20 | 2.28 | 2.33 | 2.41 |
| Nominal GDP at market prices (trillions of naira) | 72.6 | 81.0 | 90.2 | 95.4 | 111.1 | 128.5 |
| Nominal non-oil GDP (trillions of naira) | 61.3 | 70.7 | 80.6 | 89.2 | 102.8 | 118.3 |
| Nominal GDP per capita (US$) | 2,835 | 3,082 | 3,302 | 2,894 | 2,880 | 3,008 |
| GDP deflator | 9.3 | 5.9 | 4.9 | 0.9 | 11.0 | 9.8 |
| Non-oil GDP deflator | 9.9 | 6.6 | 6.3 | 5.0 | 9.0 | 8.9 |
| Consumer price index (annual average) | 12.2 | 8.5 | 8.1 | 9.5 | 10.2 | 8.5 |
| Consumer price index (end of period) | 12.0 | 7.9 | 7.9 | 11.5 | 9.0 | 8.0 |
| FGN gross debt (percent of GDP) | 10.4 | 10.5 | 10.5 | 11.9 | 11.8 | 11.4 |
| *Of which* : domestic debt (percent of GDP) | 9.0 | 8.8 | 8.8 | 9.9 | 9.8 | 9.5 |
| **Investment and savings** | | | | | | |
| Gross national savings | 19.3 | 18.6 | 17.4 | 16.0 | 17.0 | 17.4 |
| Public | 4.5 | 1.7 | 1.2 | 0.4 | 1.0 | 1.4 |
| Private | 14.8 | 16.8 | 16.1 | 15.6 | 16.0 | 16.0 |
| Investment | 14.6 | 14.5 | 14.9 | 15.5 | 15.9 | 16.2 |
| Public | 1.2 | 1.4 | 1.1 | 0.4 | 0.8 | 1.0 |
| Private | 13.4 | 13.0 | 13.8 | 15.1 | 15.1 | 15.2 |
| Current account balance | 4.4 | 3.9 | 2.2 | 0.2 | 0.8 | 0.9 |
| public net saving | 3.2 | 0.3 | 0.1 | 0.0 | 0.2 | 0.4 |
| private net saving | 1.4 | 3.8 | 2.3 | 0.5 | 0.9 | 0.8 |
| **Consolidated government operations** [1] | | | | | | |
| Total revenues and grants | 14.3 | 11.0 | 9.9 | 7.7 | 8.4 | 8.7 |
| *Of which:* oil and gas revenue | 10.4 | 7.1 | 5.8 | 3.4 | 4.1 | 4.4 |
| Total expenditure and net lending | 14.7 | 13.4 | 12.3 | 10.6 | 11.2 | 11.2 |
| *Of which* : fuel subsidies[2] | 2.2 | 0.9 | 0.7 | 0.0 | 0.3 | 0.5 |
| Overall balance | -0.3 | -2.4 | -2.5 | -2.8 | -2.8 | -2.5 |
| Non-oil primary balance (percent of non-oil GDP) | -11.6 | -9.7 | -8.1 | -5.5 | -6.2 | -6.3 |
| ECA (US$ billions) | 10.0 | 2.8 | 2.5 | 0.0 | 0.0 | 0.0 |
| SWF (US$ billion) | 1.0 | 1.0 | 1.5 | 1.5 | 1.5 | 1.5 |
| **Money and credit** | | | | | | |
| Broad money (percent change; end of period) | 29.1 | 0.9 | 7.3 | 10.8 | 15.3 | 15.2 |
| Net foreign assets | 15.9 | -3.4 | -7.4 | -0.1 | -0.2 | 2.8 |
| Net domestic assets | 2.3 | 4.3 | 14.6 | 10.9 | 15.5 | 12.5 |
| Claims on consolidated government | -14.4 | 7.3 | -4.1 | 9.6 | 11.0 | 9.4 |
| Claims on the rest of the economy | 8.1 | 8.5 | 10.3 | 10.2 | 8.0 | 5.4 |
| Velocity of broad money (ratio; end of period) | 3.9 | 4.5 | 4.8 | 4.8 | 4.8 | 4.8 |
| Treasury bill rate (percent; end of period) | 13.3 | 11.5 | 13.0 | ... | ... | ... |
| **External sector** | (Annual percentage change, unless otherwise specified) | | | | | |
| Current account balance (percent of GDP) | 4.4 | 3.9 | 2.2 | 0.2 | 0.8 | 0.9 |
| Exports of goods and services | 1.8 | -0.9 | -5.1 | -37.4 | 15.5 | 10.9 |
| Imports of goods and services | -10.6 | -4.9 | 9.7 | -16.6 | 7.0 | 7.7 |
| Terms of trade | 1.0 | 0.4 | -2.6 | -25.6 | 7.5 | 3.8 |
| Price of Nigerian oil (US dollar per barrel) | 110.0 | 109.0 | 100.6 | 52.8 | 61.6 | 66.9 |
| Nominal effective exchange rate (end of period) | 81.4 | 83.1 | ... | ... | ... | ... |
| Real effective exchange rate (end of period) | 135.6 | 150.1 | ... | ... | ... | ... |
| External debt outstanding (US$ billions) | 6.5 | 8.8 | 9.9 | 10.4 | 10.8 | 11.1 |
| Gross international reserves (US$ billions) | 43.8 | 42.8 | 34.3 | 28.4 | 26.5 | 27.8 |
| (equivalent months of imports of G&Ss) | 7.1 | 6.3 | 6.1 | 4.7 | 4.1 | 4.0 |

*Source: Nigerian authorities, IMF staff estimates and projections, February 2015*

[1] *Consists of federal, state and local government.*

[2] *For 2012, includes one-off payment of about 1 percent of GDP to settle arrears accrued in 2011.*

## Fiscal Policy

11. **The Federal Government has maintained a tight fiscal policy stance in the pre-election period but the drop in oil revenues remains challenging.** The 2014-2016 Medium Term Fiscal Framework (MTFF) was based on an oil benchmark price of US$77.5 per barrel and oil production of 2.39 million barrels per day, both reduced from the benchmarks set in the previous year. The estimated fiscal deficit for 2014 at 1.6 percent of GDP was well below the 3 percent of GDP prescribed by the 2007 FRA. Oil revenues have not grown as fast as implied by high oil prices over the last four years. In 2013, total oil revenues, at an average oil market price of US$110 per barrel, fell 12 percent below the oil revenue target set in the 2013-2015 MTFF, which was based on an oil benchmark price of US$79 per barrel. This was attributed to a drop in oil production due to illegal oil bunkering that resulted in a loss of about 16 percent of total daily production in the 2nd quarter of 2013. Oil revenues began to recover in February 2014 and this was ascribed to success in curtailing production losses. Outflows from the ECA became less frequent thereby assisting the gradual buildup of fiscal buffers that rose from US$2.1 billion in January 2014 to US$4.1 billion in August 2014. Non-oil revenues as a share of GDP have remained relatively flat since 2010. However, the decline in oil prices from mid-2014 into 2015 has led the government to revise its 2015-2017 Medium Term Fiscal Framework and 2015 budget. The benchmark oil price was revised thrice from an initial US$78 to US$73, then to US$65 and most recently to US$53. Oil output has been assumed at 2.27 million barrels per day (mbd). By end-January, 2015 the ECA had been drawn down to US$2.5 billion (US$1.6 billion in four months).

12. **As a direct consequence of reduced revenues, expenditures have also been on a declining trend.** The Federal Government cut planned expenditures in 2014 by 7 percent with capital expenditures receiving the largest cut of 32 percent. Actual federal capital budget implementation has never exceeded N1 trillion, thus the reduced allocation also reflects an acknowledgment of overestimation of the planned capital budget in previous years given limited implementation capacity. As of early December 2014, only N465 billion of the capital budget of N1.119 trillion had been made available to Ministries, Departments and Agencies (MDAs) for spending. Recurrent spending has remained more or less unchanged due to the successful roll out of the Integrated Personnel and Payroll Information System (IPPIS) and other efforts to contain spending. State governments have made greater efforts to improve independent revenues as they have also been impacted by lower federation account revenues. Lagos and Edo states are among the lead states making progress in this regard. For 2015, the federal government's planned budget expenditure of N4.5 trillion represents a 4.8 percent decline from the 2014 budgeted expenditure of N4.7 trillion. In view of lower projected revenues and a desire to maintain a low fiscal deficit, capital expenditure is billed to suffer the highest decline of 53 percent, while recurrent expenditure is projected to grow by 5.6 percent in nominal terms. The government intends to focus the significantly reduced capital budget on growth-promoting critical infrastructure, social sectors as well as defense and security. Critical infrastructure sectors to be protected include works, power, and transport; while the growth-promoting and job-creating sectors are agriculture and water resources. Health and education interventions also continue to be prioritized.

**Table 2: Key Fiscal Indicators – General Government (2012-2017)**

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|---|
| | *As percent of GDP* | | | | | |
| | *Actual* | | *Projections* | | | |
| Total revenue | 14.3 | 11.0 | 9.9 | 7.7 | 8.4 | 8.7 |
| Oil revenue | 10.4 | 7.1 | 5.8 | 3.4 | 4.1 | 4.4 |
| *Of which* : implicit fuel subsidy | 0.9 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Non-oil revenue | 3.9 | 3.9 | 4.1 | 4.3 | 4.3 | 4.4 |
| Import and excise duties | 0.7 | 0.5 | 0.6 | 0.6 | 0.6 | 0.6 |
| Companies' income tax | 1.2 | 1.2 | 1.4 | 1.5 | 1.5 | 1.5 |
| Value Added Tax | 1.0 | 1.0 | 0.9 | 1.0 | 1.0 | 1.0 |
| Other (education tax and customs levies) | 0.4 | 0.5 | 0.4 | 0.4 | 0.4 | 0.4 |
| Federal government independent revenue | 0.3 | 0.3 | 0.4 | 0.4 | 0.4 | 0.4 |
| SLGs independent revenue | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.3 |
| | | | | | | |
| Total expenditure | 14.7 | 13.4 | 12.3 | 10.6 | 11.2 | 11.2 |
| Federal government | 5.7 | 5.5 | 4.7 | 4.7 | 4.6 | 4.3 |
| Extrabudgetary funds[1] | 2.5 | 1.7 | 2.0 | 1.0 | 1.3 | 1.5 |
| *Of which:* Implicit fuel subsidy | 0.9 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| State and local government | 6.2 | 5.9 | 5.2 | 4.6 | 5.0 | 5.1 |
| Spending from ECA/SWF | 0.6 | 1.1 | 1.0 | 0.4 | 0.4 | 0.3 |
| *Of which* : explicit fuel subsidy | 0.4 | 0.9 | 0.8 | 0.3 | 0.3 | 0.2 |
| Shared infrastructure and social spending | 0.2 | 0.2 | 0.2 | 0.1 | 0.1 | 0.1 |
| Foreign-financed capital spending | 0.2 | 0.4 | 0.3 | 0.4 | 0.3 | 0.3 |
| | | | | | | |
| Overall balance | -0.3 | -2.4 | -2.5 | -2.8 | -2.8 | -2.5 |
| | | | | | | |
| Financing | 0.4 | 2.6 | 2.1 | 2.8 | 2.8 | 2.5 |
| External | 0.2 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 |
| Borrowing [2] | 0.2 | 0.4 | 0.3 | 0.4 | 0.3 | 0.3 |
| Amortization | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Foreign asset acquisition (ECA/SWF) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Domestic | 0.2 | 2.4 | 1.8 | 2.5 | 2.4 | 2.2 |
| Bank financing [3] | -2.4 | 1.2 | -0.3 | 1.7 | 1.7 | 1.5 |
| o/w ECA financing | 1.2 | 1.9 | 0.0 | 0.1 | 0.0 | 0.0 |
| Nonbank financing | 2.6 | 1.1 | 2.1 | 0.7 | 0.7 | 0.7 |
| Other financing | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| | | | | | | |
| Statistical discrepancy/Financing gap | -0.1 | 0.0 | 0.4 | 0.0 | 0.0 | 0.0 |

*Source: Nigerian authorities, IMF staff estimates and projections, February 2015*

[1] *Includes spending of customs levies and education tax; transfers to FIRS and NCS; spending from the ecology, stabilization, development of natural resources accounts; and FCT spending.*
[2] *Includes projects not included in the FGN budget although funds are on lent by FGN.*
[3] *Equal to the change in net claims on the consolidated government in the monetary survey, minus the change in state and local government deposits that are part of broad money.*

### 2.2 MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY IN NIGERIA

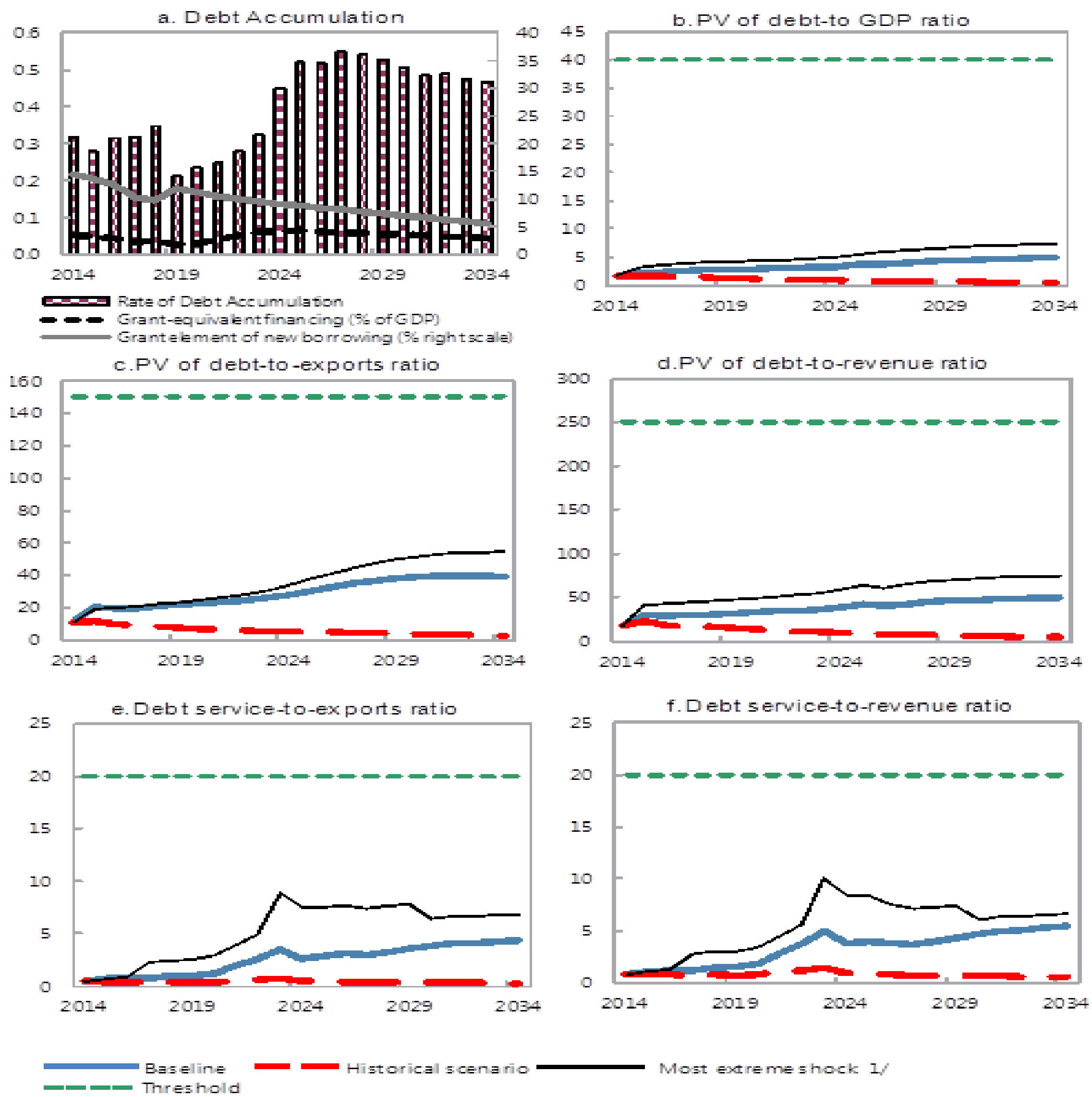
13. **The macroeconomic outlook for Nigeria is uncertain in the light of current volatilities in the international oil market.** Declining oil revenues due to falling oil prices and constrained oil production have placed pressures on the balance of payments and exchange rate. Monetary and fiscal authorities have responded to these pressures by adopting a tight monetary and fiscal policy stance; however, limited fiscal buffers and declining external reserves have placed a constraint on available policy tools. As the non-oil economy gains more prominence and structural impediments to non-oil sector growth are tackled, non-oil revenues should rise over the long term. The contingent liabilities arising from AMCON bonds issued on non- performing loans by DMBs are expected to be covered by the annual contributions by CBN and DMBs to a sinking fund[9]. N400 billion of contingent liabilities equivalent to 0.16 percent of GDP are expected to materialize in 2023. Monetary authorities are expected to continue to pursue price and exchange rate stability in the medium term. Although external debt as a percent of GDP has dropped on account of the rebased GDP numbers, this might not have a significant impact on borrowing space as government has signaled its intent to be guided by the ratio of debt service to revenues. Risks associated with the spread of the Ebola Virus to Nigeria are slightly significant but the response by the federal and state governments has been successful at containing the spread of the disease thus far. It was earlier projected that the 2015 general elections posed a significant risk to the economy (particularly the pace of capital project implementation) due to outbreaks of violence following previous elections. However, the conduct of the presidential and national assembly elections on March 28 and 29, 2015 were much more peaceful in comparison to the 2011 elections due in part to improvements in the conduct of the elections by the Independent National Electoral Commission (INEC). It is expected that the state level elections on April 11 would also be peaceful.

14. **Nigeria remains at a low risk of debt distress and although indicators deteriorate under various stress scenarios they remain below the thresholds.** The outlook is positive for both the baseline and standardized scenarios both incorporating the decline in oil prices, which assume a sustainable increase in the external debt to GDP ratio over the medium term. The baseline scenario assumes average GDP growth of 6.1 percent in 2014-34, an oil price of US$100 per barrel (pb) in 2014 which is expected to fall to US$52.8 pb in 2015 before recovering to US$73.7 pb by 2020 and a decline in the non-oil primary deficit from 8.1 percent of non-oil GDP to 4.7 percent in 2020. The outlook is less positive in the event of various alternative scenarios for Public and Publicly Guaranteed (PPG) Debt under which all indicators worsen but stay well below the threshold. The implications for both external and fiscal reserves have been discussed above and this would have implications for the ability of the federal and subnational governments to implement budgets. In view of this, Government's ability to address the challenges with oil production, revisit the Petroleum Industry Bill (PIB) whose delayed passage has limited oil sector investments and address the structural constraints to non-oil sector growth are of primary concern.

[9] According to the 2014 Joint Bank-IMF DSA, the Sinking Fund is estimated to be worth N6.1 trillion at the end of 2023 based on annual contributions of 0.5 percent of total assets by Deposit Money Banks (DMBs) (about N24 trillion at end-2013) and N50 billion annual contributions by the CBN, all accruing a 10 percent nominal return. The fund will be used to pay net interest expenses on its bonds and to fill the gap in AMCON's balance sheet (assets and liabilities were about N2.5 trillion and N6.0 trillion, respectively, as of end-2013).

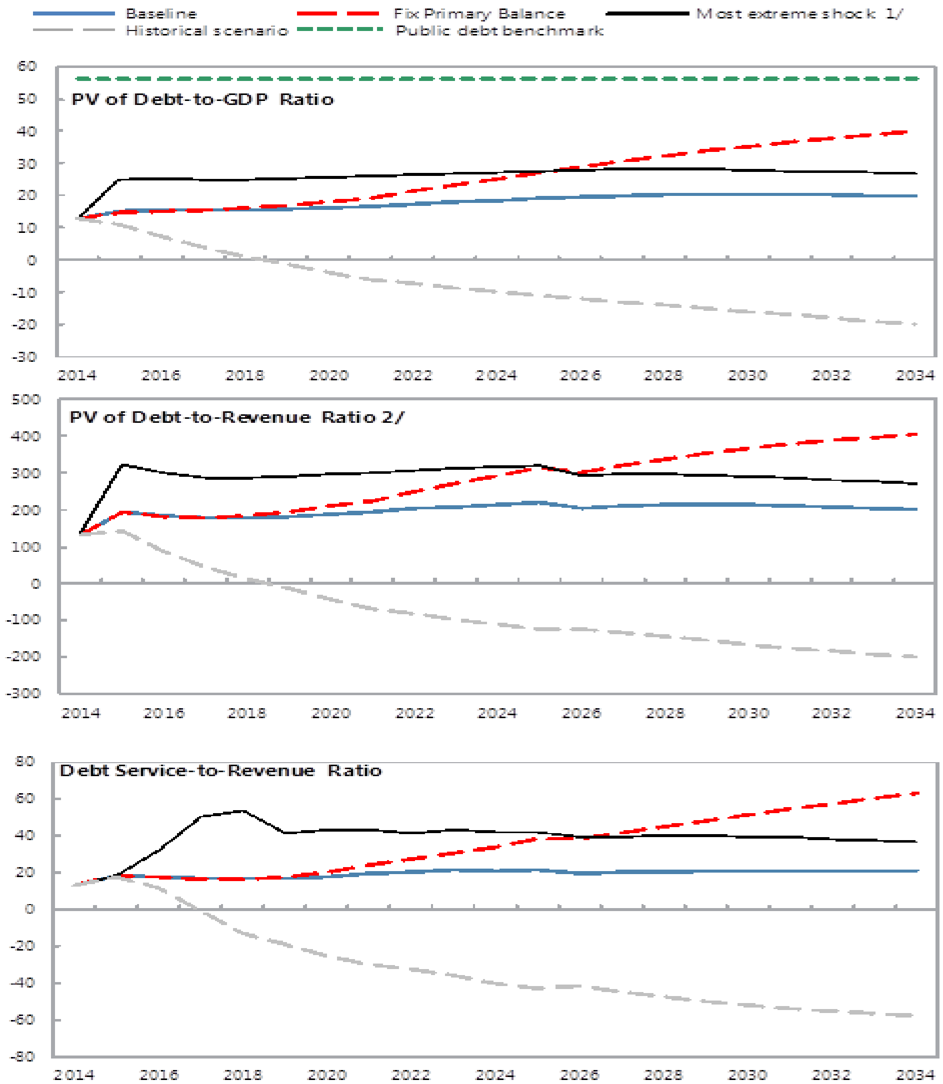
15. **With due regard to the above, the macroeconomic policy framework in Nigeria is considered adequate for the Nigeria Edo State Fiscal Improvement and Service Delivery Operation.** Both fiscal and monetary authorities are pursuing complementary policies to provide stability and curb spending given the constraints in the domestic economy. There are significant risks associated with oil sector challenges; however, the commitment to fiscal consolidation, the emergence of the non-oil economy and low debt ratios place Nigeria in a favorable position.

**Figure 1: Indicators of Public and Publicly Guaranteed External Debt under Alternative Scenarios (2014-2034)1/**




*Source: Joint IMF/World Bank Debt Sustainability Analysis, 2014*
*1/ The most extreme stress test is the test that yields the highest ratio on or before 2024. In figure b. it corresponds to a one-time depreciation shock; in c. to a lending terms shock; in d. to a one-time depreciation shock; in e. to an exports shock and in figure f. to an exports shock.*

**Figure 2: Indicators of Public Debt under Alternative Scenarios, (2014-2034) 1/**




*Source: Joint Bank-IMF DSA 2014*
*1/ The most extreme stress test is the test that yields the highest ratio on or before 2024*
*2/ Revenues are defined inclusive of grants*

## 2.3 The State Context

16. **Edo is one of the nine oil producing states in Nigeria located in the South-South geopolitical zone of the country**. The state was created in 1991 when the former Bendel state was split into Edo and Delta states. It is estimated to have a population of close to 4 million people. The present governor of Edo belongs to the main opposition party in Nigeria - the All Progressives Congress (APC) - and he is currently serving his second and final term set to end in November 2016. The 2012 Edo state elections were adjudged as free and fair with the governor securing a strong mandate by winning in all 18 Local Government Areas (LGAs) of the state with over 75 percent of the total votes polled. The governor is recognized as a former president of the Nigerian Labor Congress (NLC), Nigeria's foremost labor union.

17. **Agriculture is the mainstay of the Edo economy.** A large proportion of the state citizens depend on agricultural activities for their income. Included among the crops cultivated in the state are oil palm, rubber, cassava, rice, plantain, yam, sweet potatoes, sugar cane, cashew, groundnuts, tomatoes, cotton, and tobacco. Edo is currently Nigeria's second largest producer of rubber and oil palm. Although an oil producing state, given the enclave nature of the oil sector in Nigeria and the revenue sharing arrangements for oil revenues, few local citizens have the opportunity to benefit from and work directly in the oil sector. A number of agro-processing businesses in the oil palm and rubber processing industry like Okomu Oil Palm Plc and Presco Nigeria Plc and several agricultural research institutes such as the Nigerian Institute for Oil palm Research (NIFOR) and the Rubber Research Institute of Nigeria (RRIN) are located in the state. Based on its abundant land and water resources, Edo has a great potential to expand agriculture activities and thus improve livelihoods in the state.

18. **Socio economic indicators in Edo are largely above the national and regional averages, but poverty incidence rates are closer to the national average.** The net primary school enrollment rate increased from 70.6 in 2008 to 76.6 percent in 2013 according to the latest Nigeria Demographic Health Survey and the population using an improved water source improved to 72.8 percent from 59.3 percent in 2008. The percentage of literate men and women, proportion of births attended by a skilled health care provider are well above both the National and South-South regional average; however, the population with access to improved sanitation facilities is only slightly above national and regional averages. Poverty data from the recent General Household Panel Surveys of 2010/11 and 2012/13 is representative at the macro-regional level and not the state level; the poverty headcount in the South-South region improved from 27.7 in 2003/4 to 24.4 percent of the population in 2009/10; however, it increased from 36.9 to 43.5 percent in Edo during the same time period, still below the 46 percent at the national level[10].

**Table 3: Selected Socio-Economic Indicators for Edo State**

| Indicators | Edo | South-South Nigeria | North East Nigeria | Nigeria-National | Source |
|---|---|---|---|---|---|
| Net primary school attendance ratio | 76.6 | 74.9 | 44.1 | 59.1 | *2013 DHS* |
| Percentage of children delivered by a skilled health provider | 78.3 | 55.4 | 19.9 | 38.1 | *2013 DHS* |
| Percentage of children under 5 classified as underweight | 9.8 | 15.7 | 35.5 | 33.3 | *2013 DHS* |
| Percentage of literate women | 84.1 | 81.0 | 28.3 | 53.1 | *2013 DHS* |
| Percentage of literate men | 92.5 | 93.1 | 51.0 | 75.2 | *2013 DHS* |
| Population using improved water source | 72.8 | 68.6 | 48.8 | 59.6 | *2013 DHS* |
| Percentage of population using improved sanitation facilities | 37.9 | 28.5 | 38.1 | 34.0 | *2013 DHS* |
| Poverty incidence (2003/4) | 36.9 | … | … | 48.4 | *2003/4 HNLSS* |
| Poverty incidence (2009/10) | 43.5 | … | … | 46.0 | *2009/10 HNLSS* |

*Sources: Nigeria Demographic Health Survey (DHS) 2013; HNLSS 2003/04, 2009/10*

[10] Although the poverty data from the Harmonized Nigeria Living Standard Survey (HNLSS) results for Edo show an increase in poverty from 36.9 percent in the 2003/4 survey to 43.5 percent in 2009/10, these results should be interpreted with caution in light of concerns about the underestimation of consumption in the survey. The 2015 HNLSS is expected to provide more conclusive results.

19. **As part of Nigeria's federal structure, Edo benefits from centrally shared federation revenues.** Oil and gas, customs and excise and corporate income tax revenues are pooled centrally into the Federation Account. These revenues are shared on a monthly basis amongst the Federal, State and Local Governments with each tier receiving 48.5[11], 26.72 and 20.6 percent of revenues respectively. A formula is applied in allocating revenues horizontally across the different states and it applies the following criteria: equality of states (40 percent), population (30 percent), landmass and terrain (10 percent), social development factor (10 percent), and internal revenue generation effort (10 percent). Other oil-related revenue distributions from the ECA are also shared on the basis of this formula. In addition to this, oil producing states, such as Edo state share 13 percent of net oil revenues on top of their shares from the Federation Account. The Value Added Tax (VAT) pool is a separate account into which VAT revenues are collected and shared by all levels of government in the ratio of 15 percent for the Federal, 50 percent for the State and 35 percent for the Local Governments. The Federal Government and each of the states maintain a Consolidated Revenue Fund into which these revenues flow and all expenditures are made. The 1999 Constitution also requires each State to maintain a "State Joint Local Government Account" into which is paid all allocations to the local government councils of the State from the Federation Account and from the Government of the State**.**

20. **Although Edo has increased its revenues from Internally Generated Revenue (IGR) in the last 6 years, it is still largely reliant on centrally shared revenues.** Actual revenues from IGR as a share of total state revenues have grown from 17 percent in 2009 to 21 percent in 2014. Taxes represent the greatest share of IGR (68 percent) in 2014 followed by Fees and Fines (13 percent). The growth in tax revenues can be attributed to the successful efforts of the Edo State Inland Revenue Service (EIRS) in widening the tax net and increasing the efficiency of tax collection. The numbers for 2014 are based on preliminary estimates from the Ministry of Finance and actual IGR is expected to be higher when the financial statements are concluded. Centrally shared revenues from the Federation and VAT pool account are still significant in Edo and represent 79 percent of total revenues in 2014, slightly lower than 80 percent in 2009. Although oil prices began to decline significantly in the last four months of 2014, the impact of the decline on state revenues will only materialize in 2015 as oil revenues are realized with a significant lag. Given the high likelihood that Edo state will continue to rely on shared revenues in the medium term; the uncertain outlook for international oil prices will have an impact on state revenues; however, the growth of IGR is encouraging and is expected to foster greater fiscal autonomy in the state.

[11] Special Funds which include the Federal Capital Territory, Ecology and Derivation, Statutory Stabilization, and Development of National Resources receive 4.18 percent of revenues.

Table 4: Edo State Fiscal Accounts (2009-2014)[12]

| | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Actual | 2013 Actual | 2014 Estimates |
|---|---|---|---|---|---|---|
| | | | *in millions of Naira* | | | |
| **Revenue** | **49,245** | **59,166** | **88,248** | **89,514** | **96,379** | **86,479** |
| IGR | 8,219 | 12,379 | 18,084 | 16,970 | 21,631 | 18,510 |
| *as share of total revenues* | *17* | *21* | *20* | *19* | *22* | *21* |
| *taxes (as share of IGR)* | *70* | *70* | *68* | *73* | *62* | *68* |
| *fines & fees (as share of IGR)* | *13* | *9* | *14* | *11* | *13* | *13* |
| *others*[1] (as share of IGR) | *13* | *23* | *16* | *19* | *20* | *14* |
| Federal Transfers | 39,604 | 45,684 | 69,469 | 71,511 | 74,748 | 67,968 |
| *as share of total revenues* | *80* | *77* | *79* | *80* | *78* | *79* |
| Grants and other Capital Receipts | 1,421 | 1,103 | 695 | 1,033 | - | - |
| **Expenditure** | **58,044** | **62,933** | **103,085** | **95,558** | **95,368** | **81,206** |
| Recurrent Expenditure | 27,639 | 33,613 | 43,935 | 51,582 | 54,744 | 59,241 |
| *as share of total expenditure* | *48* | *53* | *43* | *54* | *57* | *73* |
| Personnel Costs | 16,206 | 17,187 | 21,173 | 25,704 | 25,971 | 32,602 |
| Overhead Costs | 8,083 | 9,854 | 12,816 | 15,826 | 17,551 | 17,166 |
| Pensions & Gratuity | 2,529 | 3,173 | 3,675 | 3,692 | 4,017 | 4,560 |
| CRF charges excl. interest payments | 114 | 109 | 99 | 104 | 102 | 124 |
| Interest payments | 537 | 1,651 | 3,592 | 3,944 | 5,028 | 4,858 |
| Domestic | 385 | 1,480 | 3,548 | 3,883 | 4,975 | 4,800 |
| External | 152 | 171 | 44 | 61 | 52 | 58 |
| Other Federation Account deductions | 283 | 1,747 | 1,679 | 2,415 | 2,177 | 55 |
| Miscellaneous recurrent expenditures | 133 | - | 1,000 | 1,028 | - | - |
| Capital Expenditure | 30,405 | 29,320 | 59,150 | 43,975 | 40,624 | 21,965 |
| *as share of total expenditure* | *52* | *47* | *57* | *46* | *43* | *27* |
| **Operating Balance** | **20,184** | **24,451** | **43,618** | **36,899** | **41,635** | **27,237** |
| **Overall Fiscal Balance** | **-8,799** | **-3,767** | **-14,837** | **-6,044** | **1,011** | **5,273** |
| **Financing** | **2,345** | **7,736** | **13,855** | **-1,638** | **-7,686** | **-3,682** |
| Domestic Financing (Net) | 1,146 | 6,457 | 15,440 | -82 | -16,118 | -2,719 |
| Bonds | - | - | 21,726 | -3,571 | -3,571 | -3,313 |
| Commercial Banks | -499 | 8,764 | -3,847 | 8,763 | -8,635 | 4,162 |
| Clearance of irregular liabilities | -98 | -431 | -1,708 | -6,108 | -4,854 | -3,568 |
| Changes in cash position (-= increase/+ decrease) | 1,743 | -1,876 | -730 | 834 | 942 | - |
| External loans | 1,199 | 1,279 | 693 | 1,475 | 11,677 | 2,459 |
| **Statistical Discrepancy/Financing Gap** | **-6,454** | **3,969** | **-982** | **-7,682** | **-6,675** | **1,591** |
| **Memorandum items** | | | | | | |
| Operating Balance (in % of total revenues) | *41* | *41* | *49* | *41* | *43* | *31* |
| Overall Fiscal Balance (in % of total revenues) | *-18* | *-6* | *-17* | *-7* | *1* | *6* |
| **Debt stock, of which:** | **16,278** | **30,163** | **52,750** | **64,834** | **74,053** | **76,018** |
| Domestic (including bonds) | 10,243 | 23,347 | 45,791 | 56,250 | 51,627 | 51,134 |
| External | 6,035 | 6,816 | 6,959 | 8,584 | 22,426 | 24,884 |
| **Debt Service** | 1,823 | 7,102 | 12,948 | 20,401 | 23,702 | 14,010 |
| *in percent of total revenue* | *4* | *12* | *15* | *23* | *25* | *16* |

*Source: Edo State Annual Financial Statements, 2009-2013; Edo State Government Authorities, 2015.*
*[1]Others includes earnings and sales, rent on government property, interest, repayment and dividends, reimbursements and other miscellaneous revenue items.*

[12] Large statistical discrepancies exist due to the non-conventional approach previously adopted by Edo in presenting its financial statements. Edo's adoption of GFS-compliant budget classification, commencing with 2014 accounts, is expected to improve the preparation of accounts.

21. **The share of capital expenditure in total spending has remained in line with the state's focus on infrastructure spending.** The share rose as high as 57 percent in 2011 but dropped to 27 percent in 2014. The state's plan for higher capital expenditure in 2014 was disrupted by the need to postpone the issuance of a state bond in 2014 and the non-realization of the DPO financing which had been programmed into the 2014 budget. Thus, capital spending was significantly squeezed. As a result it is expected that capital spending in 2015 will rise sharply in comparison to 2014 but decline subsequently. The increase in recurrent expenditures in 2014, in particular, personnel costs, was due to the implementation of a salary review for health officers which was eventually extended to the rest of the civil service. As part of the review, salary arrears were paid in 2014 and it is expected that the sharp rise in personnel costs as a result will smoothen out from 2015. Overhead costs, which are tied to both capital and personnel costs, have risen in tandem with the growth of expenditures over the 2009 to 2014 period. The largest share of the state's resources has been allocated to infrastructure MDAs namely Works, Transport and Environment in line with the state's focus on improving physical infrastructure; as well as to infrastructure in the education and health sectors. Expenditures have largely followed an increasing path from 2009 to 2013.

22. **The state has relied mainly on commercial borrowing to finance its fiscal deficit; however, there has been a move towards less costly forms of borrowing such as external borrowing and the issuance of bonds.** It is expected that this shift will significantly increase the diversity of debt instruments utilized by the state and facilitate the spread of debt servicing costs over longer repayment periods. The large statistical discrepancies in the presentation of Edo's fiscal accounts are due to the non-conventional approach previously adopted in presenting the state's financial statements. Edo state has however adopted a new chart of accounts/budget classification system starting with the 2014 budget. This system is far more comprehensive than the previous system and is compliant with IMF's 2001 Government Finance Statistics (GFS). This now forms the basis for Edo state's budget preparation, execution and reporting, and is expected to lead to improvements in the preparation of the state's financial accounts. In addition, emphasis will be placed on providing assistance to the relevant agencies such as the Office of the Accountant General and the Ministry of Finance through the DPO and the State Employment and Expenditure for Results (SEEFOR) project to address these shortcomings. A detailed analysis of Edo's fiscal and debt sustainability follows in the next section.

**Table 5: Spending in Selected MDAs (2010-2013)**

| **MDA** | **2010** | **2011** | **2012** | **2013** |
|---|---|---|---|---|
| | *percentage share in total budget* | | | |
| Agriculture | 1.9 | 1.5 | 0.9 | 1.1 |
| Education | 18.7 | 19.0 | 18.7 | 20.0 |
| Health | 6.4 | 4.4 | 4.9 | 5.2 |
| Water | 1.7 | 1.4 | 0.7 | 0.5 |
| Drainage, Environment & Waste Management | 4.8 | 10.8 | 9.3 | 9.6 |
| Works, Housing & Transport | 27.5 | 26.8 | 22.5 | 16.8 |
| Others | 39.0 | 36.2 | 42.9 | 46.7 |
| **Total** | **100.0** | **100.0** | **100.0** | **100.0** |

*Source: Edo State Annual Financial Statements, 2010-2013*

*'Others' include the Office of the Governor, Finance, Energy, Justice, Youth and Sports Development, Oil & Gas, Information and Orientation and Community Development Ministries and Agencies amongst others.*

## Edo State Debt and Fiscal Sustainability

23. **The fiscal sustainability analysis for Edo has been prepared against a backdrop of declining oil prices.** Oil prices declined sharply in the last few months of 2014, from an average of US$110 per barrel in the first 3 quarters of the year to about US$56 per barrel by December 2014. Oil production volumes, even though in recovery, were lower than budget in 2014 due to challenges with oil theft and delayed investments in the oil sector owing to non-passage of the PIB. The medium-term outlook for oil prices indicates that prices will likely remain under US$100 per barrel and this has implications for expenditure given that oil revenues account for about 70 percent of federation revenues. This Edo state fiscal sustainability analysis is based on the assumption that GDP moderates to about 5 percent over the period; non-oil GDP remains the main driver of growth while oil and gas GDP recovers slowly over the period. The expectation is that inflation will rise in 2015 and decline thereafter to single-digit levels as the effect of the contraction in oil revenues recedes.

**Table 6: Baseline Macroeconomic Assumptions**

| | Actual 2013 | Proj. 2014 | Proj. 2015 | Proj. 2016 | Proj. 2017-2023 |
|---|---|---|---|---|---|
| | *(annual percentage change, unless otherwise specified)* | | | | |
| Real GDP | 5.4 | 6.1 | 4.8 | 5.0 | 5.6 |
| Oil & Gas GDP | -13.1 | -2.5 | -1.6 | -1.4 | 0.1 |
| Non-oil & gas GDP | 8.3 | 7.2 | 5.5 | 5.6 | 5.8 |
| Inflation (period average) | 8.5 | 7.9 | 11.5 | 9.0 | 8.0 |
| World oil price (US$ per barrel) | 109.0 | 100.6 | 52.8 | 61.6 | 70.8 |

*Source: IMF Selected Economic Indicators, 2014*

24. **The base case scenario assumes that federation account transfers will decline in 2015 and recover gradually over the medium term.** Given that growth in Edo's IGR will be insufficient to cover the shortfall; recurrent expenditures will be rationalized to an extent; taking into consideration the constraints associated with reducing certain categories of recurrent expenditure. Thus recurrent expenditures, both in absolute terms and as a share of total expenditures are expected to remain relatively flat over the period. Capital expenditures are expected to grow by 43 percent in 2015 as some of the postponed investments from 2014 due to the deferment of a planned N30 billion state bonds and non-realization of budget support, are reintroduced into the budget. If the state accesses the bonds market, it is expected that the financing realized from this source would replace the commercial bank financing on its books. Capital expenditure growth between 2016 and 2023 is projected to slow to an average of 6 percent. Although the total public debt stock is projected to rise from N74 billion in 2013 to N93 billion in 2017, it is expected to decline to N66 billion by 2023. Subnational borrowing guidelines issued by the Federal Debt Management Office (DMO) require that the projected debt service of a sub-national for the succeeding 12 months should not exceed 40 percent of its federation accounts allocation of the preceding 12 months and Edo remains well within these limits. This ratio is projected at 12 percent in 2015; declining to 10 percent in 2018. This scenario places constraints on the state government's desire to carry out more significant capital investments in 2015 and 2016 as planned prior to the decline in oil prices and reiterates the need for an increased emphasis on diversifying revenues and increasing IGR. A recovery in oil prices would provide greater room for spending on physical infrastructure, a stated priority of the state government.

## Table 7: Edo State Fiscal Account Projections (2013-2023)

| | 2013 Actual | 2014 Estimates | 2015 Projected | 2016 Projected | 2017 Projected | 2018 Projected | 2019 Projected | 2020 Projected | 2021 Projected | 2022 Projected | 2023 Projected |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | *in millions of Naira* | | | | | | | | | | |
| **Revenue** | **96,379** | **86,479** | **80,318** | **89,076** | **96,866** | **99,582** | **102,386** | **104,656** | **107,473** | **109,662** | **111,662** |
| IGR | 21,631 | 18,510 | 22,512 | 24,913 | 27,262 | 28,675 | 30,158 | 31,093 | 32,537 | 33,326 | 33,899 |
| *as share of total revenues* | *22* | *21* | *28* | *28* | *28* | *29* | *29* | *30* | *30* | *30* | *30* |
| *taxes (as share of IGR)* | *62* | *68* | *76* | *75* | *72* | *72* | *72* | *72* | *73* | *73* | *73* |
| *fines & fees (as share of IGR)* | *13* | *13* | *24* | *12* | *15* | *15* | *15* | *15* | *15* | *15* | *14* |
| *others*[1] (as share of IGR) | *20* | *14* | *14* | *20* | *16* | *16* | *17* | *16* | *17* | *17* | *16* |
| Federal Transfers | 74,748 | 67,968 | 49,071 | 59,163 | 64,604 | 65,908 | 67,228 | 68,564 | 69,936 | 71,335 | 72,763 |
| *as share of total revenues* | *78* | *79* | *61* | *66* | *67* | *66* | *66* | *66* | *65* | *65* | *65* |
| Grants and other Capital Receipts | - | - | 8,735 | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 |
| **Expenditure** | **95,368** | **81,206** | **86,774** | **94,782** | **94,243** | **96,873** | **99,284** | **101,515** | **103,193** | **104,704** | **105,535** |
| Recurrent Expenditure | 54,744 | 59,241 | 55,362 | 59,427 | 58,706 | 58,828 | 58,849 | 58,839 | 58,157 | 57,232 | 55,465 |
| *as share of total expenditure* | *57* | *73* | *64* | *63* | *62* | *61* | *59* | *58* | *56* | *55* | *53* |
| Personnel Costs | 25,971 | 32,602 | 28,045 | 34,012 | 33,860 | 33,563 | 33,284 | 32,835 | 32,428 | 32,009 | 31,588 |
| Overhead Costs | 17,551 | 17,166 | 17,772 | 16,510 | 16,421 | 16,261 | 16,110 | 15,875 | 15,662 | 15,447 | 15,231 |
| Pensions & Gratuity | 4,017 | 4,560 | 4,501 | 4,001 | 3,501 | 2,954 | 2,411 | 1,833 | 1,264 | 1,000 | 845 |
| CRF charges excl. interest payments | 102 | 124 | - | - | - | - | - | - | - | - | - |
| Interest payments | 5,028 | 4,858 | 2,983 | 2,269 | 1,852 | 2,522 | 3,060 | 3,945 | 4,003 | 3,821 | 2,801 |
| Domestic | 4,975 | 4,800 | 2,880 | 2,143 | 1,727 | 2,400 | 2,940 | 3,540 | 3,600 | 3,420 | 2,400 |
| External | 52 | 58 | 103 | 126 | 126 | 122 | 120 | 405 | 403 | 401 | 401 |
| Other Federation Account deductions | 2,177 | 55 | 61 | 67 | 72 | 78 | 84 | - | - | - | - |
| Miscellaneous recurrent expenditures | - | - | - | - | - | - | - | - | - | - | - |
| Capital Expenditure | 40,624 | 21,965 | 31,412 | 35,355 | 35,537 | 38,045 | 40,435 | 42,677 | 45,035 | 47,472 | 50,070 |
| *as share of total expenditure* | *43* | *27* | *36* | *37* | *38* | *39* | *41* | *42* | *44* | *45* | *47* |
| **Operating Balance** | **41,635** | **27,237** | **16,220** | **24,649** | **33,160** | **35,754** | **38,537** | **40,817** | **44,316** | **47,430** | **51,197** |
| **Overall Fiscal Balance** | **1,011** | **5,273** | **-6,456** | **-5,706** | **2,623** | **2,710** | **3,102** | **3,141** | **4,280** | **4,958** | **6,127** |
| **Financing** | **-7,686** | **-3,682** | **6,457** | **5,706** | **-2,623** | **-2,709** | **-3,103** | **-3,141** | **-4,280** | **-4,958** | **-6,128** |
| Domestic Financing (Net) | -16,118 | -2,719 | -6,009 | -4,856 | -24,737 | -2,511 | -2,983 | -3,023 | -4,051 | -4,247 | -5,431 |
| Bonds | -3,571 | -3,313 | -3,947 | -4,702 | -30,601 | - | - | - | - | - | - |
| Commercial Banks | -8,635 | 4,162 | 628 | 2,537 | 8,554 | 180 | -292 | -1,552 | -2,580 | -2,776 | -3,960 |
| Clearance of irregular liabilities | -4,854 | -3,568 | -2,691 | -2,691 | -2,691 | -2,691 | -2,691 | -1,471 | -1,471 | -1,471 | -1,471 |
| Changes in cash position (-= increase/+ decrease) | 942 | - | - | - | - | - | - | - | - | - | - |
| External loans | 11,677 | 2,459 | 16,334 | 14,731 | 1,605 | -199 | -120 | -118 | -229 | -711 | -697 |
| **Statistical Discrepancy/Financing Gap** | **-6,675** | **1,591** | **0** | **0** | **0** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Memorandum items** | | | | | | | | | | | |
| Operating Balance (in % of total revenues) | *43* | *31* | *20* | *28* | *34* | *36* | *38* | *39* | *41* | *43* | *46* |
| Overall Fiscal Balance (in % of total revenues) | *1* | *6* | *-8* | *-6* | *3* | *3* | *3* | *3* | *4* | *5* | *5* |
| **Debt stock, of which:** | **74,053** | **76,018** | **84,158** | **91,637** | **93,046** | **88,102** | **85,000** | **81,859** | **70,523** | **72,621** | **66,493** |
| Domestic (including bonds) | 51,627 | 51,134 | 38,972 | 32,975 | 32,780 | 29,757 | 26,774 | 23,751 | 12,645 | 15,454 | 10,023 |
| External | 22,426 | 24,884 | 45,186 | 58,662 | 60,266 | 58,346 | 58,226 | 58,107 | 57,878 | 57,167 | 56,470 |
| **Debt Service** | 23,702 | 14,010 | 9,256 | 7,604 | 7,171 | 9,731 | 11,163 | 11,586 | 11,783 | 11,279 | 8,929 |
| *in percent of gross federal transfers* | *32* | *21* | *19* | *13* | *11* | *15* | *17* | *17* | *17* | *16* | *12* |
| *in percent of total revenue* | *25* | *16* | *12* | *9* | *7* | *10* | *11* | *11* | *11* | *10* | *8* |

*Source: Edo State Annual Financial Statements, 2013; Federal DMO and World Bank staff estimates, 2015.*

[1]*Others includes earnings and sales, rent on government property, interest, repayment and dividends, reimbursements and other miscellaneous revenue items.*

25. **Under <u>an alternative scenario</u>, assuming a more substantial increase in Edo expenditures, all fiscal indicators deteriorate significantly.** This is based on the assumption that commercial bank borrowing would finance any arising fiscal deficit. Such an increase in expenditures would be in line with Edo's fiscal plans prior to the sharp drop in oil revenues. Dependence on commercial borrowing would raise debt levels to unsustainable levels due to high commercial borrowing interest rates and short repayment periods. The debt stock would rise to N210 billion in 2023 due to soaring interest and amortization payments while debt service alone would be higher than total state revenues at the end of the projection period. In order to finance expenditure of this level, it would be necessary to obtain highly concessionary sources of financing and/or raise IGR levels substantially. Regardless of the state's ability to close the financing gap, this would be an untenable fiscal position for Edo state.

**Table 8: Alternative Scenario Assuming Higher Expenditures**

| | Actual 2013 | Est 2014 | Proj 2015 | Proj 2016 | Proj 2017 | Proj 2023 |
|---|---|---|---|---|---|---|
| | | | *in millions of Naira* | | | |
| **Total Revenue** | 96,379 | 86,479 | 80,318 | 89,076 | 96,866 | 111,662 |
| Internally Generated Revenue | 21,631 | 18,510 | 22,512 | 24,913 | 27,262 | 33,899 |
| Federation Transfers | 74,748 | 67,968 | 49,071 | 59,163 | 64,604 | 72,763 |
| Others | - | - | 8,735 | 5,000 | 5,000 | 5,000 |
| **Higher expenditures case:** | | | | | | |
| Total Expenditure | 95,368 | 81,206 | 127,774 | 107,927 | 111,635 | 147,574 |
| Recurrent Expenditure | 54,744 | 59,241 | 57,909 | 66,876 | 68,782 | 96,802 |
| Of which interest | 5,028 | 4,858 | 2,983 | 7,189 | 9,412 | 41,801 |
| Capital Expenditure | 40,624 | 21,965 | 69,865 | 41,051 | 42,853 | 50,772 |
| Fiscal Balance | 1,011 | 5,273 | -47,457 | -18,851 | -14,769 | -35,912 |
| **Debt stock, of which:** | 74,053 | 76,018 | 125,158 | 145,781 | 164,582 | 210,701 |
| Domestic (including bonds) | 51,627 | 51,134 | 79,972 | 87,119 | 104,316 | 154,231 |
| External | 22,426 | 24,884 | 45,186 | 58,662 | 60,266 | 56,470 |
| **Debt Service** | 23,702 | 14,010 | 9,256 | 21,380 | 28,339 | 114,889 |
| *in percent of total revenue* | *25* | *16* | *12* | *24* | *29* | *103* |
| **Memorandum:** | | | | | | |
| Wage bill | 29,988 | 37,162 | 35,118 | 41,275 | 41,052 | 38,078 |
| of which, Pensions & Gratuities | 4,017 | 4,560 | 6,501 | 6,569 | 6,501 | 5,845 |

*Source: Edo State Annual Financial Statements, 2013; Federal DMO and World Bank staff estimates, 2015.*

26. **A sensitivity analysis based on a 20 percent decline in federation transfers would also weaken Edo's fiscal position significantly.** If volatilities in the international oil market and challenges with domestic production persist and the state intends to maintain the same level of spending as in the base case, commercial borrowing would grow out of proportion to other indicators. With commercial lending as the residual, the outcome would bear similarity to the case of higher capital expenditures and the debt burden would become unsustainable over time.

**Table 9: Alternative Scenario Assuming 20 percent Decline in Federation Revenues**

| | Actual 2013 | Est 2014 | Proj 2015 | Proj 2016 | Proj 2017 | Proj 2023 |
|---|---|---|---|---|---|---|
| | | | *in millions of Naira* | | | |
| **Total Revenue** | 96,379 | 86,479 | 70,504 | 77,243 | 83,945 | 97,110 |
| Internally Generated Revenue | 21,631 | 18,510 | 22,512 | 24,913 | 27,262 | 33,899 |
| Federation Transfers | 74,748 | 67,968 | 39,257 | 47,331 | 51,683 | 58,211 |
| Others | - | - | 8,735 | 5,000 | 5,000 | 5,000 |
| **Lower oil revenues:** | | | | | | |
| Total Expenditure | 95,368 | 81,206 | 86,760 | 95,933 | 97,204 | 137,246 |
| Recurrent Expenditure | 54,744 | 59,241 | 55,362 | 60,603 | 61,694 | 87,149 |
| Of which interest | 5,028 | 4,858 | 2,983 | 3,445 | 4,840 | 34,485 |
| Capital Expenditure | 40,624 | 21,965 | 31,398 | 35,330 | 35,510 | 50,097 |
| Fiscal Balance | 1,011 | 5,273 | -16,257 | -18,690 | -13,259 | -40,137 |
| **Debt stock, of which:** | 74,053 | 76,018 | 93,958 | 114,420 | 131,711 | 190,053 |
| Domestic (including bonds) | 51,627 | 51,134 | 48,772 | 55,758 | 71,445 | 133,582 |
| External | 22,426 | 24,884 | 45,186 | 58,662 | 60,266 | 56,470 |
| **Debt Service** | 23,702 | 14,010 | 9,256 | 10,897 | 15,537 | 95,349 |
| *in percent of total revenue* | *25* | *16* | *13* | *14* | *19* | *98* |
| **Memorandum:** | | | | | | |
| Wage bill | 29,988 | 37,162 | 34,546 | 40,581 | 40,361 | 37,433 |
| of which, Pensions & Gratuities | 4,017 | 4,560 | 6,501 | 6,569 | 6,501 | 5,845 |

*Source: Edo State financial statements, 2013; Federal DMO and World Bank staff estimates, 2015.*

27. **Despite the current decline in oil revenues, Edo's fiscal situation as outlined in the base case is appraised as sustainable over the projection period.** In view of current fiscal realities in Nigeria, Edo is taking steps to manage its finances by scaling back planned expenditures; pursuing growth in internally-generated revenues as outlined under this operation and diversifying sources of borrowing. Debt levels would remain at sustainable levels under a base case scenario given Edo's commitment to fiscal responsibility. Rapid increases in capital spending or more significant reductions in oil prices would lead to a ballooning debt profile, which would be unsustainable over the medium term. In recognition of the state's achievements in maintaining fiscal stability under the first operation and ongoing efforts to continue on this path, the fiscal position of Edo is deemed adequate for this operation.

## 3. EDO STATE GOVERNMENT'S PROGRAM

28. **In 2010, Edo finalized and adopted the Edo State Strategic Plan (Edo SSP) which runs through the year 2020, anchored on three key pillars**. These pillars are: *People* (building the human capacity of Edo citizens with emphasis on Water, Health and Education), *Infrastructure* (with an emphasis on Power, Housing, Transport, Tourism, Roads and Drainage), and *Production* (emphasis on Agriculture, Industry and Commerce). The Edo SSP seeks to position the Edo economy on a sustainable growth trajectory and prioritizes plans to significantly increase internally generated revenue (IGR) in order to reduce dependence on largely oil revenue-based federal allocations as well as ensure fiscal sustainability. The SSP builds on many of the objectives previously articulated in the 2009 Medium Term Development Strategy (Report of the Vision 2020

Stakeholder Committee). The vision behind the SSP is to transform Edo into a leading economic center in Nigeria where the people live in dignity, powered by a government that is responsive to the people.

- Under the *People* Pillar, the Strategy prioritizes improvement of access to potable water, improved health planning and access to quality health care services, access to better quality of education including through provision of high quality and sufficient infrastructure in schools (building and renovation of school facilities, including the rehabilitation of technical education institutions and establishment of one vocational center per Local Government Area (LGA)), as well as recruitment of qualified teachers and enhancing their competence and performance.

- Under the *Infrastructure* Pillar, the Strategy prioritizes the development of solar energy, including installation of solar powered traffic lights and construction of bus stops; urban reconstruction and facilitating access to land for development of affordable housing; development of mass transit; provision of incentives for private sector participation in the development of the tourism sector; construction and rehabilitation of roads; and study, design and construction of drainage and flood control structures.

- The *Production* Pillar places priority on the development of tree crops, improved availability of fertilizers and other agricultural inputs, as well as agricultural credit to farmers, development of agro-allied industries; soft loans and microcredit to young industrialists, upgrade of investment promotion apparatus, revival of ailing industries, promotion of tax relief to pioneer investors, development of industrial clusters; exports of locally produced goods and development of the solid minerals sector.

- The underlying economic and fiscal policy strategy prioritizes efforts to increase internally generated revenue and diversify the revenue base of the state; efforts to strengthen expenditure control and value-for-money by implementing the provisions of the Edo State Public Procurement Act at the State and local government levels; adoption of measures to improve budget implementation through strengthening the quality of project planning, timely passage of budgets, adequate funding of projects, and monitoring of project implementation; improvement in the efficiency of public spending through stronger accountability and transparency arrangements for the utilization of public funds.

29. **In the first phase of implementing the State Strategic Plan, emphasis was placed on a few key sectors.** Implementation of the plan was scheduled in three phases with the first spanning 2010 to 2012. The sectors which received specific focus during this period include Education, Health, Environment, Works, Energy, Water Resources, and Transport. Large investments were made in infrastructure development, in particular roads, drainage and sewage system construction and rehabilitation, renovation and construction of schools and health facilities, electricity and water projects, and urban beautification. Some of the specific achievements under the first phase include the introduction of a Mass Transit Program to address transportation challenges in the state, linking of towns and villages to interstate roads, a Total School Transformation Program through which about 435 classrooms across all the state LGAs have been renovated and equipped. A significant amount of hospital reconstruction has been undertaken including the Central Hospital in Benin which has been upgraded to a full scale tertiary hospital.

30. **Job creation, particularly among youths, was also high on the state's agenda under the first phase.** Over 15,000 youths were employed in the last 5 years through the Rapid Response Agency (RRA), the ICT Agency and the Youth Employment Scheme (YES). Of this number, over 1,200 youths were employed in public works schemes and waste management programs. An agribusiness investment framework and an agriculture out grower scheme in cooperation with large scale farm companies like Okomu, Presco, and Rubber Estates has been developed to provide additional jobs and serve as a pilot for the framework. Most recently, a large multinational group[13] has expressed its interest and commitment to implementing a domestic out grower scheme in rice production. Furthermore, to support informal sector job creation, an Edo Empowerment Committee was set up by the state executive council to develop a Micro Credit framework for Micro, Small and Medium Enterprises (MSMEs). The committee has now completed initial work on this framework and intends to also leverage the Central Bank of Nigeria (CBN) MSME funding window.

31. **The government remains committed to these priority areas; as reflected in its budgetary allocations.** Infrastructure requirements of agricultural investors, rural based MSMEs & Primary Health Care agencies are given priority in fresh allocations to capital expenditure. The state government continues to make significant investments in infrastructure and faculty development at the primary and secondary school levels. This is now being extended to the Technical and Vocational Education and Training (TVET) institutions, where investments are being made in infrastructure, learning equipment and faculty development (partly funded by the Bank-assisted SEEFOR project). The state is further developing and expanding its Education Management Information System (EMIS) and is due to launch an electronic Application for the EMIS – the EduApp[14]. This is being done to facilitate stakeholder engagement and improved policymaking for the sector. The state has secured commitments from the major agricultural companies to engage TVET students and graduates as interns and/or full time employees. Currently, the state is in discussions with Dangote Group to establish a rice institute at the Edo state college of agriculture technology. Edo state government also continues to invest heavily in health infrastructure and rehabilitation of Primary Health Centres (in conjunction with the federal MDGs office) and General Hospitals. The state has also commenced the procurement process for a suitable Hospital Management System through which the Hospitals Management Board will coordinate operations of all state owned hospitals. In the area of industrial development, an executive-level decision has been taken to establish an industrial park (via Public-Private Partnership (PPP)) on the outskirts of Benin City. Arrangements are being finalized to conduct a feasibility study (including site analysis) and development of a business case. The studies are due to commence before end of 2014. Investments in roads, drainage, water, and rural electrification continue to receive priority.

[13] In 2014, this multinational group applied for, and has been allocated 50,000 hectares of land to set up a rice farm and mill in Edo state.

[14] The Edo State EduApp is an application being designed to give a visual representation of the government's investment in education, school infrastructure, teachers, students and pupils statistics.

# 4. THE PROPOSED OPERATION

## 4.1 OPERATION DESCRIPTION AND LINK TO GOVERNMENT PROGRAM

32. **A first Edo state Development Policy Credit was prepared in 2011 – 2012 and envisaged a three-year programmatic operation through 2013 – 2014.** There was however a wide interval between approval of the first operation and its effectiveness due to unanticipated delays in securing federal parliamentary approval for the country's 2011/12 borrowing plan. Thus, whilst the first DPO was approved in March 2012, it became effective only in June 2013 and closed in June 2014. Nonetheless, implementation of the program since achievement of the first DPO prior actions was generally promising, with major reform gains recorded especially in public financial management.

33. **Although this proposed operation builds on of the program of reform started under the earlier DPO engagement, it represents the first in a new series of two operations.** It continues in the line of support to the government's efforts to improve the management of its resources; improve the state's investment climate with a focus on land transactions as well as improve the quality of education. However, reflecting progress already made and the specific reform requirements at this point in time, the operation has been reformulated in certain areas. In this context, a number of the earlier-envisaged policy actions and result indicators for the planned second operation have been changed. The operation is structured across four main pillars: (i) ensuring fiscal sustainability; (ii) improving budget institutions and practices; (iii) improving access to land for investment; and (iv) improving the quality of education. The policy matrix for the first operation included prior actions for the first DPO and indicative actions (triggers) for a second and third. The policy matrix for this operation includes prior actions for this and triggers for a follow-on operation.

34. **The program of reform supported under this engagement corresponds with areas of priority in Edo's Strategic Plan described earlier.** In particular, the economic and fiscal strategy of the State Strategic Plan prioritizes efforts to diversify the revenue base of the state and increase internally generated revenue; efforts to strengthen expenditure control and value-for-money by implementing the provisions of Edo's Public Procurement Act at the state and local government levels; adoption of measures to improve budget implementation through strengthening the quality of project planning, timely passage of budgets, adequate funding of projects, and monitoring of project implementation; improvement in the efficiency of public spending through stronger accountability and transparency arrangements for the utilization of public funds. These are all areas of emphasis under the first two pillars of the DPO. Furthermore, the SSP places emphasis on improvements to education, including Science education as well as technical and vocational education as a means of strengthening the quality of its labor force. Similarly, it emphasizes the creation of an enabling environment for the private sector to play a greater role in the state economy and be the engine for job creation and poverty reduction. These are the areas of focus of the third and fourth pillars of the DPO.

35. **Experience from the previous DPO engagement suggests that the DPO is an effective and appropriate instrument for supporting Edo.** The ealier DPO program for Edo played a strong catalytic role in helping the government of Edo move forward on its reform agenda -

thriving on the back of the state government's own strong determination and commitment to pursuing its development objectives along with necessary reform. Under this engagement, as part of public financial management reforms to improve its overall economic governance, Edo commenced a process of strengthening its public procurement practices through increased competition and transparency. The government introduced a system of making public information on contract awards above specified thresholds for transparency and social accountability purposes. Edo also enacted a modern public procurement law that defines the principles and procedures to be applied in the public procurement of goods, works and services. Further, it established a Public Procurement Regulatory Agency responsible for regulating the implementation of the public procurement law as well as inaugurated a state Procurement Council responsible for public procurement policy directions. All public contracts above threshold are now competitively awarded. Edo also began building a modern, computerized budget and treasury management system across its budget process. In this regard, the state has achieved a strong leadership among Nigerian states in ensuring that its expenditure management systems, including the implementation of a commitment control system, are progressively robust and all budget expenditures are transacted through this (Oracle-based) financial management system, with the required in-built controls. The timeliness of preparation of the State government's annual accounts as well as the external auditing of these accounts has also progressively improved from 15 months now to nine months. As part of investment climate reforms, Edo undertook a comprehensive workflow review of the processes and time taken to obtain land titles with the aim of streamlining these processes. The state went on to streamline its processes on this basis and it is now possible to process land certificates of occupancy within 30 days (excluding Governor's signature), compared with over 60 days previously. As part of reforms to improve the quality of education in the state, and in particular, TVET, to meet the state's requirements for high quality middle level manpower, Edo established school-based management committees for TVET institutions to improve governance of these institutions and consequently the quality of training received at this institutions.

## 4.2 PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

### 4.2.1 Pillar 1: Ensuring Fiscal Sustainability

36. **The government of Edo recognizes the importance of implementing its social and infrastructure development programs in a fiscally sustainable manner.** Currently, the bulk of state government revenues are due to transfers from the federation account which is largely oil and gas revenue based and managed at the center. Oil revenues are notoriously volatile; hence, longer term sustainability of the state's expenditure program is at risk. To this extent, the state is keen to improve its internally generated revenue and at the same time, control public spending in a way that eliminates wastage. The earlier DPO supported a first line of reforms in these areas and this operation builds on those initial reforms.

*(i) Improving Internally-Generated Revenue (IGR)*

37. **First of all, Edo is also prioritizing collections from other sources besides direct income taxes.** The EIRS introduced the Land Use Charge Law in 2012 (incorporating the Ground Rent, Tenement Rate and the Property Tax) to consolidate all land related charges under one single charge for ease of administration and collection. Administration of this tax handle, however, commenced only in 2014 but promises to deliver considerable tax returns as the state adopts

measures to expand its land use tax base. Second, the state enacted the Hotels and Events Centers Occupancy and Restaurant Consumption Law in 2011 and thereby introduced a consumption tax targeted at the hospitality industry which ensures that a minimum tax of 5 percent on goods and services consumed at these facilities accrues to the state government. Full implementation of this law commenced in 2013. Furthermore, the EIRS is in the process of reviewing the Entertainment tax law and has recently issued new regulations for conduct of Lottery, Pools Betting, Casino and Gaming activities in the state, with a view to optimizing tax revenue collection from these activities. Regulations for online lottery, casino and gaming activities are about to be finalized. A significant amount of IGR is expected to accrue from this source given the vibrant market that exists as a result of the large youth population in the state.

***Prior action #1:*** *Deployment of Unique Tax Identification Number (U-TIN) registration kits at EIRS and all tax offices across Edo state*

38. **As a key to ensuring fiscal sustainability, Edo intends to continue to strengthen efforts aimed at improving its ability to generate internal revenue.** Since 2008, the state was able to increase its IGR significantly by over 250 percent between 2008 and 2011 as the administration implemented measures to eliminate inefficiencies in revenue collection and plug many sources of leakage. Tax audits were conducted and a sizeable amount of the increased collections were tax arrears accruing from back tax assessments. The Edo Internal Revenue Service (EIRS) recognizes and acknowledges that there is a huge potential to improve IGR further as there are potential tax handles that are not currently assessed. Also, Edo estimates that the number of tax payers captured in the tax net is much below potential. IGR in proportion of total state revenue was only 22 percent in 2013. Collections from PAYE, which comprise the bulk (about 60 percent) of IGR were negatively affected by the 2011 amendment to the Personal Income Tax Act which granted huge tax reliefs to majority of taxpayers and consequently resulted in a significant real decline in tax revenue accruable to the state in 2012 – another reason the state considers it a priority to further improve its tax-net capture across other tax handles, especially the *Direct Assessment* handle under which self-employed persons are captured. In this regard, the EIRS is finalizing plans to undertake a state-wide electronic taxpayer enumeration survey. In parallel, the state has gone ahead to deploy electronic taxpayer registration kits at the Internal Revenue Service headquarters in Benin City and at all its tax offices across the 18 local government areas of the state; and will subsequently establish an Electronic Data Base Management System (EDBMS) of identified taxpayers. This is geared towards maximum tax net capture, especially for the informal sector as well as better enforcement. The EDBMS will constitute a reliable, transparent and efficient system to enable the state better track, monitor and manage taxpayer activity as each taxpayer will be identifiable by a unique taxpayer number with their biometric data captured. Edo expects to capture an additional 82,000 taxpayers in the minimum, in this database by the end of 2016; thereby expanding its tax base and consequently its internal revenue.

39. **To strengthen the revenue authority itself, the state enacted a new revenue administration law in 2012.** The law establishes the EIRS as an autonomous revenue service anchored on strict professionalism, transparency, integrity and results. Concurrent to these tax policy reforms, the EIRS is also strengthening its tax administration capacity. In this regard, the agency has embarked on a major organizational structure and business process re-engineering for improved service delivery and full automation of processes. It is undertaking service-wide

training/capacity needs assessment to guide capacity development for EIRS staff. Furthermore, in order to boost tax compliance, Edo State Internal Revenue Service intends to provide adequate support to tax payers by establishing a specialized tax payer services unit at its headquarters in Benin-City as well as continue to provide tax payer services through its other offices throughout the state. Further, the state is leveraging ICT for better taxpayer service delivery. The state has deployed Point of Sale (POS) terminals at all the collecting banks linked to the IGR accounts and is also on the verge of launching a new and dedicated website that supports online tax payment as well as other taxpayer services like TIN registration.

**Table 10: Actual and Projected Revenue Collections by Edo State Internal Revenue Service**[15]

| *(Millions of Naira)* | *Actual* 2012 | *Actual* 2013 | *Estimate* 2014 | *Projected* 2015 | *Projected* 2016 | *Projected* 2017 |
|---|---|---|---|---|---|---|
| Pay-As-You-Earn (PAYE) | 8,539.75 | 8,774.70 | 9,712.95 | 10,629.70 | 11,479.70 | 11,879.70 |
| *as share of total EIRS revenues* | *50.59* | *41.99* | *52.47* | *53.76* | *52.21* | *48.37* |
| Witholding Tax | 1,522.26 | 1,463.66 | 1,686.18 | 1,526.66 | 1,470.35 | 2,181.35 |
| *as share of total EIRS revenues* | *9.02* | *7.00* | *9.11* | *7.72* | *6.69* | *8.88* |
| Pools Betting, Gaming, Casino & Lottery | 29.36 | 23.01 | 23.25 | 223.58 | 343.58 | 473.58 |
| *as share of total EIRS revenues* | *0.17* | *0.11* | *0.13* | *1.13* | *1.56* | *1.93* |
| Capital Gains Tax | 9.22 | 9.21 | 14.46 | 49.21 | 73.21 | 91.21 |
| *as share of total EIRS revenues* | *0.05* | *0.04* | *0.08* | *0.25* | *0.33* | *0.37* |
| Direct Assessment | 505.71 | 675.62 | 657.48 | 981.72 | 1,201.72 | 1,461.72 |
| *as share of total EIRS revenues* | *3.00* | *3.23* | *3.55* | *4.97* | *5.47* | *5.95* |
| Motor Licensing | 591.52 | 770.40 | 840.44 | 1,047.69 | 1,297.69 | 1,587.69 |
| *as share of total EIRS revenues* | *3.50* | *3.69* | *4.54* | *5.30* | *5.90* | *6.46* |
| Stamp Duties | 18.14 | 72.13 | 31.68 | 155.74 | 190.74 | 220.74 |
| *as share of total EIRS revenues* | *0.11* | *0.35* | *0.17* | *0.79* | *0.87* | *0.90* |
| Consumption Tax | 69.96 | 77.02 | 96.83 | 262.15 | 347.15 | 409.15 |
| *as share of total EIRS revenues* | *0.41* | *0.37* | *0.52* | *1.33* | *1.58* | *1.67* |
| General Development Levy | 1,143.17 | 1,266.45 | 669.23 | 747.77 | 1,067.77 | 1,394.55 |
| *as share of total EIRS revenues* | *6.77* | *6.06* | *3.62* | *3.78* | *4.86* | *5.68* |
| Land Use Charge | - | - | 14.94 | 125.25 | 206.55 | 272.24 |
| *as share of total EIRS revenues* | | | *0.08* | *0.63* | *0.94* | *1.11* |
| Tax Audit | 3,497.55 | 2,324.04 | 351.49 | 1,287.70 | 1,422.41 | 1,635.39 |
| Others, including MDA fines & fees | 953.41 | 5,443.07 | 4,411.65 | 2,734.38 | 2,886.96 | 2,954.32 |
| **Total** | **16,880.05** | **20,899.31** | **18,510.58** | **19,771.55** | **21,987.83** | **24,561.64** |

*Source: Edo State Internal Revenue Service; 2015.*

*(ii) Improving Payroll Expenditure Control*

***Prior Action #2**: Completion of payroll verification audit of education and health sector staff*

40. **While the Edo government steps up policy and institutional reform efforts to increase IGR, it also seeks to control expenditure leakages in its bid to maintain fiscal sustainability**. In this context, reforms are focused on dealing with potential expenditure pressure points, one of which is the payroll. As a prior action for the first DPO, the government gathered relevant biometric data pertaining to public servants and transferred the data to an oracle-based human

[15] It is likely that some fines and fees accruable in 2012 were collected and recorded as 2013 collections.

resource system to enable monthly payroll calculation. This has reduced cases of ghost workers appearing on the payroll. Building on this achievement, the government, in early 2015, hired an independent consultant to conduct a verification audit of its employee and pensioner database as of end-2014 to establish their continued authenticity and integrity. This is to be done in two stages, beginning with the largest ministries – Education and Health. The audits for the Education and Health ministries have recently been completed as a prior action for this operation and the audit reports submitted to the state government. The audits will enable elimination of any identified ghost employees from the payroll of these sectors following the state government's analyses of the outcome of these audits. A trigger for the follow on operation is the completion of independent verification audits for all other MDAs.

41. **Beyond payroll auditing for accuracy, Edo is adopting a renewed strategy to contain the growth of the payroll within reasonable limits.** Edo implemented a salary review for health officers in 2014 which was eventually extended to the rest of the civil service. As part of the review, salary arrears were paid in 2014. However, the government has made a commitment to contain the growth of the state workforce within the 2014 limits into 2015 and for the foreseeable future.

***Results:*** *The expected results of the measures for ensuring fiscal sustainability are a substantial growth in the number of taxpayers captured and uniquely identified in the state's biometric database; leading to growth in Edo's IGR; as well as sanitization of the state's payroll bill (expected to remain at 25-35 percent of total expenditure); thereby creating more fiscal space.*

### 4.2.2 Pillar 2: Improving Budget Institutions and Practices

42. **Under this operation, Edo will continue to strengthen its budget institutions and practices; building on earlier achievements.** The state government recognizes that sound public financial management occurs within the context of sound budget institutions and practices that deliver good value for money and ensure that resources are allocated to the right priorities and utilized efficiently. Thus, the state is in the process of improving its budget institutions and practices and will strengthen these efforts under this operation. Consequently, the following four sub-areas will continue to be supported by the DPO:

*(i) Establishing a strong PFM institutional platform*

43. **The Edo government recognizes the importance of a strong institutional platform for its PFM reforms**. This involves strengthening of the state's PFM legal and regulatory frameworks; its human and organizational capacity for PFM; as well as its PFM information system. The state government is therefore moving ahead to entrench its improved PFM policies and practices in relevant laws in order to protect them from being easily reversible or side-stepped. For example, the State Public Procurement law has been enacted as a prior action under the earlier DPO. Furthermore, the state is strengthening the human and organizational capacity for PFM thorough a strengthened capacity building framework across central finance institutions and key MDAs. In terms of the PFM information system, the Oracle system for budget preparation, execution, accounting and reporting has been scaled up with enhanced modules for improved

financial management; and key financial management bottlenecks impacting the effectiveness and efficiency of service delivery have been expunged from the procedures without weakening internal controls.

***Prior Action #3:*** *Issuance of Circular by Edo state Head of Service to establish a procurement cadre in the public service in preparation for the professionalization of the procurement function in the MDAs*

44. **Given the importance of the public procurement process in ensuring that public expenditure delivers good value for money, Edo prioritized the enactment of a modern public procurement law in its institutional reform program.** This was a prior action under the earlier DPO. The law defines the principles and procedures to be applied in the public procurement of goods, works and services. It also defines in the regulations, respective roles of different institutions and officers in public procurement. The state has established the Public Procurement Regulatory Agency responsible for regulating the implementation of the public procurement law and inaugurated a state Procurement Council responsible for policy directions. A logical next step in the reform sequence is to operationalize the procurement units that were recently created in the respective MDAs and ensure appropriate resourcing of the procurement function. To this end, the state civil service office will institutionalize a new procurement professional cadre and this is a prior action under this operation. It is the plan to progressively build the professional capacity of this new cadre based on a Procurement certification program. This is a trigger for the subsequent operation.

45. **Beyond public procurement, Edo is in the process of strengthening its PFM institutional platform more broadly**. The state is currently preparing an organic Public Finance law along with related Financial Regulations and Instructions that would, among other things, help redefine the roles and responsibilities of both line ministries and central management agencies, the accountability of vote holders, rules on debt and the creation of special funds, accounting, internal control and financial reporting requirements, the treasury functions of the Accountant-General, powers of the legislature and rights and obligations of functionaries and citizens in the financial matters of the state. Furthermore, the state intends to establish a PFM reform coordination unit to be hosted in the Ministry of Finance, to be staffed by qualified personnel for improved PFM reform coordination. The Unit will coordinate all PFM related reform actions across the government; serve as the secretariat for the PFM Steering Committee and the Technical Committee; and monitor the State's PFM performance as custodian of the self-/independent assessment exercises on PEFA or other PFM performance assessments. The PFM reform unit will provide regular reports to the Steering Committee on progress in the implementation of the state's PFM reform action plan. Further, the state enacted a new state revenue administration law in 2012 to strengthen its revenue authority. The law establishes the EIRS as an autonomous revenue service, anchored on strict professionalism, transparency, integrity and results.

***Prior Action #4:*** *Complete systems configuration and Operational Acceptance Testing (OAT) of the SIFMIS Hyperion Budget module*

46. **In terms of building a strong PFM information system, Edo has instituted a state-of-the-art computerized system for processing financial transactions using an Oracle-based application.** The introduction of the some modules of the Oracle-based State Integrated Financial

Management Information System (SIFMIS) was a prior action under the earlier DPO. It represents a combination of hardware, Oracle software application and communication and networking technologies implemented to enable operation and management of key areas of government operations across the budget cycle. A license for ten modules and sub-modules[16] of Oracle's Enterprise Business Suite has been procured by the state. The following core modules are currently in use, albeit to varying degrees: Budget preparation sub-module, Payroll, Procure-to-Pay Solutions ('P2P')[17], General Ledger, and Accounts Payable.

47. **Adoption and implementation of the new budget classification system and chart of accounts is also a major step being undertaken by Edo to strengthen its PFM information management system and comparability of its financial data.** This new chart/classification system, which is far more comprehensive than the previous system, was adopted, starting with the 2014 budget, and is compliant with IMF's 2001 Government Finance Statistics (GFS). This now forms the basis for Edo state's budget preparation, execution and reporting. Due to the comprehensive classification of activities and transactions under the new chart/classification system, during budget preparation, it is now much easier to align the budget to development priorities; also, during execution of the budget, monitoring and control of expenditure has become easier. As a prior action for this operation, the state has completed the systems configuration and the operational acceptance testing (OAT) of the SIFMIS Hyperion Budget module in line with the new Chart of Accounts/budget classification system which is also consistent with the harmonized national chart/classification system. The 2015 budget was however centrally loaded onto the system as network connectivity to majority of MDAs is yet to be completed. Rolling-out the Oracle on-line budget preparation system to MDAs will be a subsequent action expected to be accomplished in 2015 in time for the MDAs' own use of the system for the preparation of the 2016 budget.

***Prior Action #5:*** *Introduce the Procure-to-Pay (P2P) module of SIFMIS for processing of all MDA expenditure transactions.*

48. **The state is also fine-tuning and upgrading its deployment of the Procure-to-Pay (P2P) module of the SIFMIS.** In support of transitioning to a commitment control system in the expenditure management process, Edo state had launched the P2P module of the SIFMIS for the processing of expenditure transactions in three MDAs in 2011. As a prior action for this operation, this module has now been introduced for use for processing of all MDA expenditure transactions. This activity enables the generation of more detailed budget execution reports showing appropriations, budget releases, actual expenditures, outstanding commitments, payment obligations, and balance against appropriation for each function of government. This is very useful for better monitoring of the budget. However, there is a need to fine tune and upgrade the system. Currently, network connectivity has yet to be completed for a number of MDAs. These MDAs currently use transaction processing sites to process their procurement related transactions during

[16] Oracle R12.0.6 EBS modules purchased: Hyperion Budget and Planning, General Ledger (GL), Accounts Receivable (AR), Accounts Payable (AP), Purchasing (PO), Cash Management (CE), Assets Management (FA), Core Human Resource (HR) , Payroll, and Procurement, and lately, Business Intelligence.

[17] The Oracle's Procure-to-Pay solution automates the entire procurement process, including sourcing and contract management, supplier collaboration, quoting, requisition, and invoice processing, and integrated purchasing intelligence.

budget execution. Furthermore, transition from an ex-poste transaction posting system to that of a real time, ex-ante processing of expenditure transactions (using work-flow processing arrangements) on the basis of P2P implementation needs to happen to ensure that Edo State manages its expenditures from the point of requisitions, to purchase orders, to invoices/goods received/services rendered/works delivered, to final payment. By these means, the state can monitor, manage and control its encumbrances, commitments, obligations and liquidation of obligations through final payments on a real-time basis and thus also reduce the potential for expenditure arrears arising. Currently, there remains a dual system of expenditure processing – one through manual approvals and the other through systems-based approvals. This defeats the whole purpose of an IFMIS and does, in practice, mean that hard-copies of supporting documents for expenditure commitments and obligations would have to be passed from approver to approver (based on the work-flow) before the final processing is completed. To instil efficiency and proficiency in the use of the available system, the state would need to work to ensure that invoices and goods/services received/works progress certificates are instead scanned and uploaded in the system as part of the work flow process so that the hard copies of the documents are not delivered to the approving authorities outside the system. As a trigger for the follow-on operation, the state would ensure that all MDAs are able to process their transactions, real-time, at their respective locations and the business processes would have been re-engineered to cater to the current system misalignments.

*(ii) Improving Practices in Strategic Planning and Budget Preparation*

*Multi-year Perspective to Budgeting*

***<u>Prior Action #6:</u>*** *Approval by the state executive council of the 2015 budgets of six key MDAs[18] that are based on the sector strategic priorities articulated in the State Strategic Plan (SSP)*

49. **In continued recognition of the crucial role of strategic planning and budget preparation in improving public expenditure, Edo is building on earlier progress made in aligning its annual budgets with its strategic policy priorities.** Following from its Vision 2020 document which outlined the state's medium term development priorities, the state has developed a State Strategic Plan (SSP) as the framework for the strategic planning process. The SSP consists of the government's priorities translated into sector objectives and strategies, or initiatives, which are incorporated into the annual budget preparation process. However, the state is in the process of strengthening this framework by introducing a multi-year perspective to its budgeting through the development of costed Medium Term Sector Strategies (MTSSs) with more detailed strategies and initiatives for achieving medium term sector goals and objectives within a specified medium term frame. Currently, the state is benefitting from the expertise of a PFM consulting firm presently resident in the state and supporting the relevant officials to be able to prepare MTSSs. The first of the MTSSs will cover the timeframe of 2015-2017 and would be completed in April 2015. However, this will be too late to inform the 2015 budget of the state; but it would aid the learning process of the state officials ahead of 2016 budget preparation. The preparation of the 2015 budget of all MDAs has however drawn from the sector strategies as contained in the SSP. This is a prior action for this operation and is evidenced by templates prepared by the Ministry of Budget and

[18] Namely: Basic Education; Secondary, Technical & Tertiary Education; Works; Transport; Environment & Public Utilities; and Health.

Economic Planning which map the projects in the approved 2015 sectoral budgets to the key sector strategies prioritized in the SSP. The state would build on this process by preparing its 2016 budget based on more formal, costed MTSSs covering the period 2016-2018 and which would also be published on the state's open data portal[19]. The use of MTSSs for preparation of the budgets of six key MDAs is a trigger for the subsequent operation.

*Citizen Participation in Planning & Budgeting*

50. **Edo prioritizes citizen engagement in the strategic planning and budgetary processes as part of its approach to socially accountable governance**. In this regard, the government has an established budget consultation process whereby pre-budget consultations as well as quarterly in-year budget implementation consultations are held across the state with citizens (citizen town hall meetings) to deliberate on issues of budget formulation and budget implementation vis-à-vis service delivery in key sectors of the economy. The objective of these consultations is to bring the citizenry onto the center of the development planning and budget execution process. The DPO program is supporting these mechanisms for citizen participation in planning and budgeting, especially as pertaining to capital budgeting. A benchmark under the first DPO was the commencement of preparation of guidelines for citizen participation in the identification of capital projects and an indicative trigger for the follow-on operation was the publication of such guidelines. However, this trigger has not been translated into a prior action in the current operation as the authorities consider that the current mechanism for citizen participation already functions well enough. Nonetheless, following extensive discussions with the authorities during the preparation of this operation on the need to institutionalize a process of citizen participation that would outlive the current administration, the authorities would now move ahead with the preparation of institutional guidelines to this effect. This is neither a prior action for this operation nor a trigger for the next but would be monitored throughout the program period.

*(iii) Improving Practices in Budget Execution and Monitoring*

51. **Edo continues to pursue improvements in practices relating to budget execution and monitoring in a bid to improve the efficiency of public expenditure and service delivery**. To this end, continued enhancements to procurement, cash management and budget implementation monitoring practices and mechanisms are being implemented.

*Public Procurement Practices*

52. **The public procurement reforms being implemented by Edo are geared towards the achievement of transparency, accountability, competitiveness, and value for money in the public procurement processes of the state**. To this end, the state enacted a modern public procurement law in 2012 to define the principles and procedures to be applied in the public procurement of goods, works and services. The law also defines the roles of different institutions and officers in public procurement. Further, a public procurement regulatory agency was established, and its governing council inaugurated, in 2014. Following its establishment and resourcing, the procurement agency would more systematically regulate the public procurement practices of the state in line with the law. As a next step, Procurement Regulations, Manuals and

[19] With the launch in 2013 of Edo state's open data portal, Edo state became the first sub-national government in Africa to successfully develop and launch an open data portal.

Standard Bidding Documents are being developed by the regulatory agency to be deployed to the MDAs for use. The government will continue to make public, information on contract awards above specified thresholds for transparency and social accountability purposes. Furthermore, the procurement agency would conduct annual procurement audits of a representative sample of contracts awarded and submit these reports to the state legislature. Another transparency mechanism to be built into the procurement process is the creation of an open access procurement databank and commencement of publication of procurement journals. This will enable procurement practitioners to have unhindered access to quality data on procurement. The procurement journal will be the media for procurement news and a forum for discussion and exchange of information on current procurement issues and development. In order to ensure that the procurement process delivers value for money through reduced costs, the government is designing a price database for overheads/consumables (to be updated annually). On this basis, price norms will be issued to all MDAs to be used for their procurement planning and budgeting. In order to ensure that there is responsiveness to complaints about public procurement decisions, the procurement regulatory agency would establish a complaints review mechanism for procurement decisions.

*Cash Management*

53. **This operation seeks to support Edo to improve its cash management system in order to strengthen budget implementation.** While the state has an implicit form of cash management system in place, no formal strategy exists. The government, in its quest to maintain a reliable cash planning system, has developed a database enterprise application tool that tracks all contracts, including multi-year contracts, from the point of award (commitments), to progress payments (progress certificates), and final payment (liquidation) as well as contract closure. This is a very useful system, however, it will be helpful for the state to transition to a streamlined form of Treasury Single Account whereby the treasury can ascertain government cash position on a daily basis to prioritize payments and prevent the buildup of payment arrears. Also, state revenue collecting bank accounts need to be promptly swept into the Government's consolidation bank account. Executive approval of a well-articulated and robust cash management strategy, including banking arrangements, for Edo State Government will strengthen the government's commitment in the area of cash management. Already, the state has introduced an Electronic Funds Transfer (EFT) system for the payment of all supplier bills. This is critical to reducing payment delays as well as the potential for fraud under a progressive system towards a 'cash-less' economy. The State electronically transfers payments to suppliers' bank accounts, on a general basis, rather than issuing them paper cheques.

*Budget Monitoring*

54. **The DPO program is supporting measures by the Edo government that enable all stakeholders to better monitor the implementation of the annual budgets**. This is because budget monitoring by all stakeholders is critical for transparency, accountability, and hence improved service delivery. The aforementioned database application system of monitoring capital projects is one way in which the state government keeps a tab on capital budget implementation. This system maintains detailed and comprehensive information on projects and contracts but currently covers only three major ministries: Works, Health and Environment. Ministry of Education would be the next to be covered. The system however is not yet online and accessible by MDAs and or citizens.

55. **The Government has moved beyond the generation of quarterly budget implementation reports by MDA and line item to economic and functional classification of expenditure.** These enable analyses of expenditure in a more purposeful way. The government also intends to begin to incorporate service delivery outcomes in the budget execution reports and publish these to enable citizens draw a link between government expenditure and service delivery. These will be used to inform citizens' pre-budget and in-year budget execution consultations with the government. The regular publication of quarterly budget execution reports for MDAs at economic and functional classification levels under the new CoA on the State's Open-Data web portal within 2 weeks of quarter end is an action that will be supported and monitored under the DPO program.

*(iv) Improving Practices in Internal and External Auditing*

56. **The DPO program is supporting Edo state to strengthen both its internal and external audit functions.**

*Internal Auditing*

57. **The goal of the DPO support to Edo's internal audit function is to improve internal controls from a more systemic perspective, and re-orientate the internal audit function to better strengthen the internal management of MDAs**. The current role of the state internal auditors – being staff of the State Accountant General - remains predominantly pre-auditing. This is inconsistent with the specific and general functions for internal auditors. As part of the actions supported under this operation, the internal auditors will begin to pilot the use of risk-based audit methodologies in MDAs, and focus on the systemic review of ex poste rather than ex ante transactions for both revenues and expenditures. However, the current role of the internal auditors and their added value to the accountability matrix still needs to be redefined since the existing PFM law recognizes the core internal audit role more within the pre-auditing domain.

*Timeliness & Quality of Audited Financial Statements*

***Prior Action #7:*** *Submission of FY13 annual audited financial statements of the Edo State Government to State House of Assembly within 9 months of end-FY and publication of same on the state's website or open-data web portal*

58. **Over the last few years, the government of Edo has significantly improved the timeliness of preparing its audited financial statements**. As a prior action for the first DPO, Edo state cleared a two-year audit backlog. Currently, audits are now completed within 2 months of receipt of draft accounts from the State Accountant General, and audit reports are subsequently laid at the SHoA for review by the Public Accounts Committee (PAC). The audited financial statements for the year 2013 were submitted to the SHoA within nine months – a clear case of timeliness and improved financial transparency; and the historical series of audited financial statements are also published on the state's website or open data portal. The state aims to further improve on the timeliness of submission and publication of the audit reports. Audit quality is improving although full compliance with International Organization of Supreme Audit Institutions (INTOSAI) standards will take some time. The state has now procured consultancy services to support the revision of the Edo Audit Act of 1982 and related regulations as well as to support the modernization of the State Auditor-General's Office and the PAC Secretariat, among other tasks.

Once delivered, the external audit function of the State as well as the legislative oversight Secretariat (PAC) would have been strengthened to better deliver on their mandates.

***Results***: *By the end of the program period, the expected results from these measures for improving budget institutions and practices include: (i) Public procurement capacity would be strengthened and procurement professionals in the public service would be able to implement modern procurement procedures that can ensure good value for money; (ii) the credibility of the state's budget management process improves through integration of all processes and the incidence of expenditure arrears is significantly reduced; (iii) strategic allocation of the state's resources is significantly improved; (iv) the timeliness of submission of audit reports to the SHoA and their timely publication for enhanced transparency will be improved.*

#### 4.2.3 Pillar 3: Improving Access to Investment Land

59. **The economy of Edo state has been largely public sector-driven; as government has in the past invested directly in virtually all areas of economic activity, including state government-owned breweries, transport services and retail companies.** The rationale was that the state did not have enough indigenous entrepreneurs to invest in these and other areas of the economy. But direct government ownership of such companies stifled the enterprising spirit of potential indigenous entrepreneurs. The private sector though now expanding due to recent government effort in this regard is still relatively weak and enterprises such as large, jointly owned or completely foreign-owned manufacturing enterprises, mining companies, and plantations, catering primarily to foreign markets are few and far between. The traditional subsistence sector and small-scale commercial and service activities in the informal sector dominate the industrial landscape. The educated unemployed do not find these two sectors attractive. Edo state therefore views it as very important to improve the enabling environment to increase the contribution of the private sector, especially large corporates, to economic growth and to employment generation, either in partnership with the public sector (public-private partnerships) or in parallel. Among its focus areas for policy and institutional reform in improving the investment climate, is the area of land information systems and access to investment land. As the Government services in this area improve, it is reckoned that economic agents will be incentivized to shift from informal investments to more formal private sector engagement. Equally, foreign investment would be attracted to the state. The increased and more formal business activities will result in a sustainable expansion of the tax base, and hence increase IGR in a sustainable way. This operation supports Edo's efforts to improve access to land for investment such that will attract private investment, both foreign and domestic.

60. **In order to improve access to investment land, the government in 2011 began taking steps to significantly improve the process for obtaining Certificates of Occupancy (C of O's).** A Certificate of Occupancy in Nigeria confirms title to land and it enables land transactions take place in the formal market place. It usually took a long time for property owners to obtain C of O's in Edo State. As a result, many economic agents did not have title to their property. Economic agents were therefore limited in their ability to make long term investments. It was also a disincentive for potential new investors. As a benchmark under the first DPO, the state Ministry of Lands & Survey conducted a comprehensive workflow review of the processes and time taken to obtain C of O's. Based on that, the authorities developed and have begun implementing

streamlined procedures for obtaining C of O's. The Government also published these new procedures on the state government's website. A review of land files processed by the Ministry of Lands & Survey in selected months reveals that it has been able to reduce the time taken to process applications for C of O's (apart from the Governor's approval) using its streamlined procedures to an average of 30 working days in 2013/14; down from up to 100 days in some cases, previously. Discussions are on-going to have the government also review the governor's approval procedure, with a possibility of delegating approvals for C of O to the Commissioner of Lands & Survey or the state Attorney-General with a view to minimizing the time this takes. Moving ahead, the state will complete the digitization of the stock of existing records under a planned electronic C of O program.

61. **Also in 2011, the government commenced the process of developing a new Land Information System (LIS) that is based on geo-referenced digital maps in order to improve the reliability of land information and consequently, the land registration process.** Based on the World Bank's Sub-national Doing Business Survey of 2010, it took 69 days and 15 procedures to register property in Edo State[20]. This was in part due to the poor land record-keeping system using paper maps and which were not regularly updated. The government sought to modernize this system through the development of a GIS-based LIS. As a prior action for the earlier DPO, Edo state executed an agreement with a concessionaire for devising and running the Edo GIS. The government also established a website for the Edo GIS and published the first set of land maps produced under the EGIS as a means of fostering transparency and improving public access to relevant information on land. This was also a prior action under the prior DPO. However, by late 2013, the concession agreement for the Edo GIS had suffered a setback and collapsed. Following this development, the government contracted an ICT firm to install the GIS software to be piloted, in the urban areas first, on limited basis (Benin City only); thereafter the system will be rolled out to more local governments across the state. In the meantime however, the government has taken a bold step to rationalize the procedures for transferring land titles in the state through the delegation of the governor's consent to the state attorney-general. While the 2014 *Doing Business* survey reports Edo State's land registration process to have improved only marginally to 67 days and 13 procedures[21], a more recent review of title transfer files in the Ministry of Lands and Survey reveals that it could take less than 40 days for the land title transfers to be completed (compared with as much as 70 days or more previously); provided that applicants do not stall in making the necessary fees and tax payments or tendering the required documentation. The state will continue to monitor this process to ensure minimum transaction time. Going forward, the state will publish widely, clear guidelines and procedures for the processing of land title transfers, along with related costs to simplify the process for applicants.

[20] The World Bank *Doing Business* (DB) Survey measures the full sequence of procedures needed for a business to purchase an immovable property from another business and formally transfer the property title to the buyer's name. The process starts with obtaining the required documents, such as a copy of the seller's title, and ends when the buyer is registered as the new property owner.

[21] DB 2014 data are current as of March 2014 and its measurement of time taken to transfer property includes all processes including time taken for the applicant to make payment of all the necessary fees and taxes and submit necessary documentation. Sometimes, applicants delay in making such payments or in tendering necessary documentation.

***Prior Action #8:*** *Complete an Assessment of the impact of reducing land transaction charges on the volume of formalized land transactions and state internal revenue*

62. **In addition to land transaction procedural reforms, the government seeks to mitigate the constraints imposed by assessed high land transaction charges in the state.** *Doing Business 2014* estimates that it costs 26.4 percent[22] of property value to transfer property in Edo state; one of the highest cost regimes in the country. Based on the state's own preliminary assessments, only a small percentage of land transactions (initial and subsequent) are formalized through the state Ministry of Lands and Survey. It would appear that this is in part due to the prohibitive nature of the state's land charges. This renders most land assets un-bankable or unusable as collateral to obtain loans for business. It also hampers the ability of entrepreneurs to purchase or sell a property. Furthermore, it deprives the state of optimum revenue accruable from land transactions. To this end, the government, in early 2015, established a high-level ad-hoc working group to formally assess the impact of reducing land transaction charges on the volume of formalized transactions and state internal revenue. This working group is led by the Chairman of the Edo state Economic and Strategy Team and has seven state commissioners[23] as its other members. The completion of this assessment constitutes a prior action for this DPO (verified by the Assessment Report of the working group with its recommendations) and implementation of the recommendations from this assessment is trigger for the following operation. The working group, has among other things, recommended that the government allows a six-month window of opportunity for land owners to regularize their land titles for a token fee with the aim of broadening the land transactions revenue base. The expectation is that reducing the cost of land transactions would enable a lot more transactions to be formalized which in turn, would enable more investments and at the same time constitute an expanded revenue base for the state. In essence, it would be a win-win situation for the state and its citizens, including investors. Currently, there are up to 17,000 land title applications stalled at the Ministry of Lands & Survey, presumably due to inability of applicants to pay the required fees and taxes. The government expects that up to 15,000 of these would be completed during the window period. The working group has also recommended a 9 percentage point reduction of the land transfer fees which currently add up to 16.4 percent of land value.

***Results***: *At the end of the program period, it is expected that reforms for improving access to investment land supported by the DPO will result in a reduction in the fees for processing and transferring land titles; leading to a growth in the volume of formalized land transactions and consequently, growth in the state's internal revenue.*

[22] Of this, 10 percent is the cost of a deed of assignment prepared by a private lawyer. The balance of 16.4 percent is charged by the government.

[23] These are the Commissioners for Land & Survey; Housing & Urban Development; Justice; Finance; Budget, Planning & Economic Development; Agriculture; and Works.

### 4.2.4 Pillar 4: Improving the quality of education[24]

63. **Edo state government recognizes the importance of strengthening the capacity of the youths in the state to be able to take on employment opportunities as they are created by a more active private sector.** Improving the quality of education is therefore one of the government's strategies to tackle unemployment in the state as a better educated workforce will be better equipped to take up job opportunities created within the state. In this regard, the state is working to improve the quality of education from the primary to the tertiary level; especially science education and including vocational and technical education. The earlier DPO supported three key areas in this regard: (i) improvement of the education information systems to enable better planning and monitoring of the sector; (ii) improvements in the quality of public technical and vocational educational institutions, given the role they can play in improving the employability of youth; and (iii) improving the teaching of critical subjects, especially Science, Mathematics & English Language, especially in the rural areas of the state. This DPO will build on these earlier lines of support especially support to public technical and vocational educational institutions. In addition, it will support measures to improve the management and monitoring of teacher and pupil attendance at schools; as a 2013 World Bank-commissioned study[25] identified teacher absenteeism as a critical challenge for the education sector in Edo state.

*Improving the quality of public technical and vocational education institutions*

***Prior Action #9:*** *Provision in Ministry of Education's 2015 approved budget of funding for TVET colleges based on their approved school improvement plans*

64. **The government of Edo sees vocational and technical education as critical to youth empowerment and employability.** Thus, the government has been working to revamp the system of public TVET in the state. Hitherto, most of the state-run TVET colleges were run down in terms of physical infrastructure and were not very well governed. In the State Strategic Plan, Edo state is prioritizing the rehabilitation of the state's technical colleges/schools to produce skilled technical and middle-level manpower for the state. The earlier DPO supported the establishment of School-Based Management Committees (SBMCs) in Technical and Vocational Education Institutions, with broad representation, including from civil society, to carry out some of the responsibilities decentralized to the institution level. This operation is continuing in this line of support. The established School Based Management Committees now formulate annual TVET school improvement plans (SIPs) since 2014 (which will be updated annually) for each of the TVET schools; and as a prior action for this operation, the state allocated funding in the 2015 budget of the Ministry of Education for the implementation of the 2015 school improvement plans. Further, from 2015, the state will enhance the quality of content delivered at TVET colleges by establishing collaboration mechanisms with the private sector – small-scale entrepreneurs, large-scale industrial and commercial firms, as well as relevant professional associations. These collaboration mechanisms will include transfer of expertise from industry to the colleges, apprenticeships, internships and entrepreneurship development programs for TVET students or full-time job placements for TVET graduates. A trigger for the next operation is the execution of

[24] Improvements in accountability at the basic education level as well as improvements in the functionality of TVET education have been used here to proxy improvement in the quality of education.

[25] Reboot (2013): *Addressing Teacher Absenteeism in Edo State: Summary of Findings* - Report prepared for the World Bank

a minimum of three TVET college-private sector partnership agreements which specifically create access for female students to benefit. The main aim of these arrangements will be to ensure that the skills being acquired in these institutions are indeed functional and relevant for industry. Already, the state is in discussions with Dangote Group to collaborate with the state College of Agriculture to establish a Rice Institute at the College of Agriculture Technology that will teach courses on the development of new initiatives for rice production and milling.

*Improving the monitoring of teacher (and pupil) attendance*

***Prior action #10:*** *Issuance by State Universal Basic Education Board (SUBEB) of guidelines and template for monitoring and reporting on teacher and pupil attendance by school-based management committees*

65. **Teacher absenteeism is a critical challenge for the education sector in Edo state and has recently come under the public spotlight.** A 2013 World Bank-commissioned report highlighted the need for efforts aimed at curbing the undesirable trend to address the contextual challenges that affect teacher attendance and overall performance. To its credit, the government of Edo has already spearheaded numerous reforms targeted at improving the management processes for public education; with the Governor himself spearheading efforts to sanitize the State's education system. A series of unscheduled school inspections has resulted in the dismissal of some teachers, school inspectors and local government education officers. There is however still a crucial need to ensure effectiveness of these efforts. This operation aims to support the positioning of primary and secondary school-based management committees to complement the efforts on Ministry of Education inspectors to monitor teacher attendance at schools. To this end, the State Universal Basic Education Board (SUBEB) will issue guidelines and an accompanying reporting template to ensure standardization of reporting format across schools. Pupil attendance would also be monitored and reported on. This is a prior action under this operation. The SBMCs would be required to report quarterly to SUBEB. Building on this, SUBEB's annual review reports would feature these data and information on teacher and pupil attendance, disaggregated by gender. This public issuance of the SUBEB 2015 review report that incorporates such data constitutes a trigger for the next operation.

***Results****: At the end of the program period, it is expected that reforms for improving the quality of education supported by the DPO will result in (i) the establishment of collaborative mechanisms between TVET colleges and industry to ensure functionality and relevance of TVET education; and (ii) stronger accountability at the basic education level through better monitoring and reporting of teacher and pupil attendance at schools, especially in the rural areas.*

## Table 11: DPO Prior Actions and Analytical Underpinnings

| Prior Actions | Analytical Underpinnings |
|---|---|
| ***Pillar 1: Ensuring Fiscal Sustainability*** | |
| **Prior Action #1:** Deployment of Unique Tax Identification Number (U-TIN) registration kits at EIRS and all tax offices across Edo state | Edo State Strategic Plan (2010-2020); Edo state Public Expenditure Management and Financial Accountability Review (PEMFAR) 2010 – Dominance of federation transfers (ranging between 78 and 90%) in Edo State's revenues. Internally Generated Revenues (IGR) constitutes only 10-22%. |
| **Prior Action #2:** Completion of payroll verification audit of education and health sector staff | Edo state PEMFAR 2010[26] - Finding of weak payroll controls. Payroll adjustment in cases of retirement or death relatively slow and sometimes ineffective. |
| ***Pillar 2: Budget Institutions & Practices*** | |
| **Prior Action #3:** Issuance of circular by Edo state Head of Service to establish a procurement cadre in the public service in preparation for professionalization of the procurement function in the MDAs | Edo state PEMFAR 2010 - Finding of inadequate capacity and skills to apply the existing procurement guidelines on open competitive bidding. No procurement professional cadre in the state public service. |
| **Prior Action #4:** Complete systems configuration and Operational Acceptance Testing (OAT) of the SIFMIS Hyperion Budget module | Edo state PEMFAR 2010 – Finding of weak expenditure commitment controls and lack of transparency in the process of in-year budget adjustments. |
| **Prior action #5:** Introduce the Procure-to-Pay (P2P) module of SIFMIS for processing of all MDA expenditure transactions | Edo state PEMFAR 2010- Finding of weak expenditure commitment controls and lack of transparency in the process of in-year budget adjustments, contributing to expenditure arrears. |
| **Prior Action #6:** Approval by the state executive council of the 2015 budgets of six key MDAs[27] that are based on the sector strategic priorities articulated in the State Strategic Plan (SSP) | Edo state PEMFAR 2010 - Edo State did not use a multi-year perspective in fiscal planning during the review period. There were no sector strategies; the state government still used the dual budget technique, with weak connection between investment and recurrent expenditure/programming. |
| **Prior Action #7:** Submission of FY 2013 annual audited financial statements of the Edo State Government to State House of Assembly within 9 months of end-FY and publication of same on the state's website or open-data web portal | Edo state PEMFAR 2010 - Finding of generally late audits – an average of 15 – 18 months after the end of the FY; leading to delayed consideration of audit reports by the state parliament and difficulty of following through on audit queries. |
| ***Pillar 3: Improving access to land for investment*** | |
| **Prior Action #8:** Complete an Assessment of the impact of reducing land transaction charges on the volume of formalized land transactions and state internal revenue | WB Subnational Doing Business Surveys (2010, 2014): Finding of prohibitive fees and taxes for registering property in Edo state |
| ***Pillar 4: Improving the quality of education*** | |
| **Prior Action #9:** Provision in Ministry of Education's 2015 approved budget of funding for TVET colleges based on their approved school improvement plans | Edo state Vision 2020 (2009); Edo State Strategic Plan (2010): Dilapidation of TVET facilities; Weak management and governance of TVET institutions. |
| **Prior Action #10:** Issuance by State Universal Basic Education Board (SUBEB) of guidelines and template for monitoring and reporting on teacher and pupil attendance by school-based management committees | *Addressing Teacher Absenteeism in Edo State: Summary of Findings* (Report prepared for the World Bank) –Poor retention of students in Edo schools linked to poor teacher presence in schools |

[26] The 2010 PEMFAR led to the development of an action plan drawn up by the state government with technical assistance from the Bank. The action plan corresponds with the state's own vision of building a modern and more efficient PFM system.

[27] These MDAs are those that usually constitute the largest share of the state's budget – Basic Education, Secondary, Technical & Tertiary Education, Works, Transport, Environment & Public Utilities and Health.

### 4.3 LINK TO CPS AND OTHER BANK OPERATIONS

66. **The Edo DPO program is closely linked to the FY2014-2017 Nigeria Country Partnership Strategy (CPS).** Both the earlier operation and this one have been consistent with the Bank's strategies in Nigeria. Under its second strategic cluster – effectiveness and efficiency of social service delivery at state level for greater social inclusion – the current CPS prioritizes the strengthening of public and private training institutions to respond to skills demand. In particular, the CPS seeks to promote improvements in the quality and relevance of technical and vocational education in Nigerian states. It also seeks to promote improvements in the quality of teachers and teaching. These objectives find expression in the education pillar of the DPO intervention. Additionally, the third strategic cluster of the CPS, which is also a cross-cutting cluster – governance and public sector management – prioritizes improvements in public financial management across all levels of government in Nigeria. In particular, the CPS targets up to eight states with fully functioning integrated financial management information systems promptly producing and publishing consolidated quarterly financial statements as a way of enhancing transparency in budget execution in states. The CPS envisages that the state-level DPOs would be strong vehicles for deep engagement in this regard. In addition, public procurement reforms across all levels of government in Nigeria are a special area of focus in the CPS. The budget institutions and practices pillar of this operation is fully aligned with these objectives of the CPS. Furthermore, the CPS envisions the use of social accountability mechanisms even at the project level to support greater transparency, participation and third party monitoring of government operations in key sectors; including through leveraging innovative ICT tools. These are very much aligned with the social accountability thread that cuts across this operation.

67. **This operation is also aligned with other Bank operations in Edo state**. Support to Edo state under the first and second pillars of the DPO – Ensuring fiscal sustainability and Improving budget institutions and practices – is strongly correlated with support to PFM in Edo state through the SEEFOR project. The SEEFOR provides technical and financial assistance to Edo state for PFM reforms. The SEEFOR project is co-funded by an EU grant and has two main components: a component for supporting PFM reforms and a component for supporting youth employment. The PFM component is being used for supporting the state in carrying out a wide range of reforms, including those which underpin the DPO. In addition, the youth employment component of the SEEFOR will provide TA for the implementation of education related reforms under the DPO through support to the state Ministry of Education and to the technical and vocational training institutions. Furthermore, the NDSA operation complements the DPO's support to social accountability in Edo state as it provides technical assistance to the state to improve its social accountability mechanisms around service delivery.

### 4.4 CONSULTATIONS, COLLABORATION WITH DEVELOPMENT PARTNERS

68. **In preparing this operation, the Bank is coordinating closely with the IMF on the assessment of Nigeria's macro economy and its outlook.** Beyond this, the engagement with Edo state through the Development Policy Operation is not being done in direct collaboration with other development partners. However, the European Union (EU) is providing grant co-financing for the Bank's SEEFOR project which is also providing financing and technical assistance to Edo in two areas of DPO support – public financial management and technical & vocational education. Joint implementation support missions have been undertaken by the SEEFOR team (EU and World

Bank) and the DPO team to Edo and joint discussions and collaboration on PFM and TVET reforms have usually been undertaken in this context.

# 5. OTHER DESIGN AND APPRAISAL ISSUES

## 5.1 POVERTY AND SOCIAL IMPACT

69. **This DPO support to Edo state aligns with the Bank's twin goals of eliminating extreme poverty and boosting shared prosperity.** While Edo state is one of the frontline states in terms of socioeconomic indicators[28] and governance reforms, its choice (similar to that of Lagos state) for a budget support operation was hinged on the potentially positive demonstration effect this could have on other states to adopt and nurture important reforms. The results being achieved by Edo state in terms of public financial management and socioeconomic outcomes are important not only for Edo state, but also for the entire country as Edo serves as a vanguard for what other states should be doing. The operations in Lagos and Edo would hopefully be catalytic for scale up across the other states in the country.

70. **Reforms for improving the budget institutions and practices are aimed at improving the quality of spending in Edo State, which is expected to benefit especially the poor.** As indicated earlier, a key element of the state's development strategy is employment creation and sustainable economic growth by tackling the state's main challenges which are high poverty levels, youth unemployment, and dilapidated infrastructure. The Government's strategy is to tackle these challenges by allocating more resources to the identified priority sectors of roads, and drainage, education, health, agriculture, and ICT. The PFM reforms being supported under the proposed DPO are aimed at improving the quality of public expenditure by ensuring that the budget is indeed aligned to these growth and employment creating priorities, and that all practices in the implementation, monitoring and evaluation of the budget are consistent with the principles of effectiveness, efficiency, and transparency. Therefore, once implemented, it can be expected that PFM reforms will have a positive impact on the poor.

71. **Improved quality of education will empower the poor and vulnerable and put them in a better position to take advantage of various income earning opportunities.** The reforms for improving the quality of education being supported by this operation are biased towards the poor and economically vulnerable. In particular, technical and vocational education are meant to improve the employability of those who do not have formal education, did not complete their formal education, or who have formal education qualifications but have still not been able to find employment because their qualifications are not in demand in the job market. The emphasis of the education component of the operation in ensuring that female TVET students and graduates specifically benefit from partnership arrangements between TVET colleges and the private sector will positively impact on the economic prospects of girls and women who constitute a major vulnerable population segment in the state, as elsewhere.

[28] The 2013 Nigeria Demographic and Health Survey (NDHS) indicates that Edo's socioeconomic outcomes are better than the national average. Poverty incidence in Edo state from the latest Nigeria Household Surveys (2009/10) was also slightly better than the national average, but was high at 43.5 percent.

72. **Reforms for improving the investment climate are also expected to be beneficial to the poor in Edo State through increased opportunities for self-employment and wage employment.** The reforms being supported under the proposed DPO are aimed at making it easier for potential investors to register their landed properties and obtain certificates of occupancy; as well as transfer or sell property to third parties. It is expected that these reforms will improve investment opportunities in Edo state which will translate into more employment opportunities – both self-employment and wage employment. In terms of self-employment, a boom in investments in the state will lead to the emergence of a middle class in Edo which will in turn lead to an increase in demand for goods and services provided by microenterprises, most of which are owned by the poor. At the same time, increased investment will create wage employment opportunities for the poor. For example, greater security of property rights will unlock the bottlenecks in accessing finance, not just for businesses, but for the general land owner since land is still the most common form of collateral in Nigeria. Currently, a huge percentage of Nigerians remain unbanked, and lack access to credit due to lack of collateral. Accesses to collateral will, therefore, bring more people into the financial market. Further, increased access to investment land will increase the availability of land for transaction and, therefore, make it more tradable, and in turn, bring down the exorbitant cost of land in Edo state.

## 5.2 GENDER ASPECTS

73. **A gender dimension has been explicitly incorporated in the DPO-supported reform program.** One of the DPO sub-pillars focuses on improving the quality of TVET education through the establishment of partnership arrangements between TVET colleges and the private sector. This is to ensure that TVET programs are well aligned with the requirements of industry and TVET graduates are well-groomed for employment or entrepreneurship in the private sector. A policy action has been introduced to this component and it seeks to ensure that female TVET students are specifically earmarked to benefit from these partnership arrangements, especially apprenticeships or internships to ensure they are able to compete with their male counterparts on the job market. Specifically, this action entails the reservation of private sector attachments or placements for at least 50 percent of the eligible female population. In Edo state, there is a huge male-female gap in technical and vocational education (with the female student proportion at only 18 percent) and this shows up in the world of work where there are very few females in the technical and vocational fields. This gender-affirmative action thus seeks to bridge a part of this gap. The related monitoring indicator will track the percentage of eligible female students benefitting from these programs. Further, because the state has identified that girls are more prone to drop out of school especially when families face economic challenges, the policy action to have the school-based management committees support the Ministry of Education to monitor and report on teacher attendance would also monitor and report on pupil attendance, disaggregated by gender, thus enabling the Ministry of Education to identify any gender gaps in school attendance and drop-out; and thus develop further policies to improve girl child education where necessary.

## 5.3 ENVIRONMENTAL ASPECTS

74. **The policy and institutional reforms and related prior actions supported by the proposed DPO are not expected to have any significant direct impact on the environment.** The improvements in policies and institutions for managing public resources, increasing access to investment land, and improving the quality of education as outlined in earlier sections of this

document are not likely in themselves to have any direct impact on the environment; positive or negative. However, it is not inconceivable that indirectly, the budget support funding to be provided could be spent on activities that have the potential to damage the environment thus requiring appropriate mitigation to acceptable levels. In this regard, it is expected that the state government will apply the extensive experience acquired through years of implementing World Bank investment projects which require strict adherence to environmental safeguards. Edo State has demonstrated significant goodwill and capacity to enforce the extant environmental laws in the State and in complying with World Bank Safeguards Policies in the implementation of World Bank assisted investment projects (*Fadama* III, Nigeria Erosion Watershed Management Project (NEWMAP), Community and Social Development Project (CSDP), and SEEFOR) in the state. Furthermore, due diligence conducted by the Bank on the national and Edo state policy and legal requirements relating to environment and social management indicates that there are adequate legal and institutional frameworks in Nigeria and Edo State for achieving good international practice relating to environmental and social sustainability and in fulfilling their national and international, including the World Bank, environmental and social obligations.

## 5.4 PFM, DISBURSEMENT AND AUDITING ASPECTS

### Public Financial Management System

75. **Although weaknesses and risks remain, the public finance management system in Edo can support this operation**. As indicated earlier under analytical underpinnings, a PEMFAR assessment was conducted in 2009-2010. This constituted of a PEFA assessment, a Financial Management Fiduciary Risk Assessment, and a Procurement Assessment, among others. All the studies identified areas of where the Edo PFM system was strong or where progress was being made, and areas where weaknesses and risks existed. Following these assessments, the Government put in place a comprehensive and prioritized reform action plan for dealing with areas of weakness, many of which are being supported under this DPO program. As earlier indicated in this document, major progress has been recorded in building a modern, automated and integrated financial management system, with the required in-built controls aimed at enhancing transparency, comprehensiveness, and accountability in the management of public finances in the state as well as improving commitment control; improving the timeliness of preparation of the State government's annual accounts as well as the external auditing of these accounts which continue to be progressively improved. These PFM reforms and others are being supported by TA under the Bank's SEEFOR project; contributing to the strengthening of the fiduciary environment in Edo. The fiduciary environment is certainly much stronger than at the commencement of the earlier DPO.

*Foreign Exchange Control Environment*

76. **Although the CBN's accounts are audited on an annual basis, a full safeguards assessment has not been conducted since 2001, which raises the possibility of potential risk.** Like in most countries, the foreign exchange system is controlled by the country's central bank, the CBN. The IMF conducted a full Safeguards Assessment of the CBN in 2001 with respect to the Stand-By Arrangement which expired on October 31, 2001. The assessment, which was completed on November 28, 2001, concluded that vulnerabilities existed in the areas of financial reporting and legal structure of the Central Bank. These findings and proposed recommendations

were presented in the related staff report. No further safeguards assessment has been conducted. The CBN's financial statements have been audited on an annual basis and the reports rendered timely and are made public. The latest financial statement of the CBN (December 2013) is unqualified. Drilling down the assessment to the management of foreign exchange control environment at the level of the Edo state (as Edo state maintains its consolidated fund in designated commercial banks), the due diligence assessment of the Banks in terms of which Banks can hold designated accounts for World Bank-financed projects, confirms that all the designated commercial banks qualify to hold such accounts. Nonetheless, given the absence of a more recent IMF Safeguards Assessment or equivalent information from other sources relating to the foreign exchange control environment in the CBN, the potential for risk exists. Therefore additional accountability and assurance arrangements to mitigate fiduciary risks would be required with regards to funds flow under the Program. To this end, a dedicated foreign currency bank account will be maintained at the CBN into which the credit proceeds will be deposited, and an independent audit of the movement of funds to and from the dedicated account will be conducted.

*Overall Fiduciary Environment*

77. **In spite of the mitigating measures in place, the overall fiduciary risk of this operation is considered to be substantial.** The commitment of the state Government in Edo to prudent financial management is strong as demonstrated by the actions taken since the current administration assumed office. The reform measures, most of which are supported by the SEEFOR technical assistance project, and some of which underpin this operation have significantly improved the fiduciary environment even further. Nevertheless, this operation is only the second of its type in Nigeria. Therefore, the overall fiduciary risk to the operation remains substantial.

**Disbursement and Auditing**

*Credit amount*

The Credit is a single-tranche operation embedded as the first in a planned series of two operations. This tranche is an IDA Credit in the total amount of SDR 53.3 million (US$75 million equivalent). The tranche would be made available upon Credit effectiveness.

*Recipient, Program and Financing Agreement*

78. **The Credit will be extended to the Federal Republic of Nigeria, represented by the Federal Ministry of Finance, which will in turn on-lend to the State Government of Edo.** The credit proceeds would be transferred by the Federal Government to the State Government of Edo under the same terms and conditions used for IDA investment loans on-lent by the Federal Government to a state government. The establishment of such an on-lending agreement shall constitute a condition of Credit effectiveness. A program agreement between IDA and the Government of Edo State, outlining the commitments and obligations of the Government of Edo State under the program, shall be negotiated and signed at the same time that the Financing Agreement for the Credit is negotiated and signed between IDA and the Federal Republic of Nigeria.

*Funds flow arrangements*

79. **The Government of Nigeria shall identify a dedicated Foreign Currency Account with the Central Bank of Nigeria (CBN) into which the proceeds of the credit will be disbursed on a single tranche basis upon credit effectiveness.** The account is to be used exclusively for the proceeds of the Credit and will form part of Federal Republic of Nigeria's foreign exchange reserves. The funds in the Account will, within two working days, be transferred into a dedicated account of the Government of Edo State, to be established with the CBN. The funds transferred into the dedicated Foreign Currency Account of the Government of Edo State with the CBN will form part of the Consolidated Fund Account of the Government of Edo State and will be used to finance the budgeted expenditures of the Government of Edo State. The account is to be used exclusively for the proceeds of the Credit. The Government of Edo State will make withdrawals from these accounts either directly for US$ denominated budgetary expenditure, or transfer the resources in Foreign Currency and/or local currency to dedicated accounts it maintains with any commercial bank that has met the stress test conducted by the CBN to finance budgeted expenditures in local currency. The dedicated accounts and the transactions therein will be recorded in the Government of Edo State's budget management and accounting system.

*Disbursements*

80. Disbursements and/or withdrawals from the designated Foreign Currency Account of the Government of Edo State held with the CBN, as well as the designated Local or Foreign Currency Accounts of the Government of Edo State held with commercial banks shall not be tied to any specific purchases and no special procurement requirement shall be needed. The proceeds of the Credit shall, however, not be applied to finance expenditures in the negative list as defined in Schedule 1 of the Financing Agreement. If any portion of the Credit is used to finance ineligible expenditures as so defined in the Schedule of the Financing Agreement, IDA shall require the Government to promptly, upon notice from IDA, refund an amount equal to the amount of the said payment to IDA. Amounts refunded to IDA upon such request shall be cancelled from the credit.

*Assurance Requirements*

81. **Due to the fiduciary risks associated with the program, additional fiduciary arrangements shall apply to this operation.** An audit of the flows in and out of the dedicated Foreign Currency Account of the Government of Edo State held with the CBN as well as the dedicated Accounts (Foreign Currency and Local Currency) to be established with any of the Government of Edo State's commercial banks will be carried out by independent auditors acceptable to IDA within 4 months after the end of each fiscal year (and until such time that the balances in the accounts reach zero), and the audit report shall be submitted to IDA within 6 months of the end of each relevant fiscal year. The Terms of Reference of the audit will be agreed at negotiation but will include: (a) with respect to the Foreign Currency Account held with the CBN, a full assurance that the withdrawals from the account were indeed (i) used to finance regular and legitimate budgetary expenditures of the Government of Edo State (if they represented direct payments) and these are reflected in the budget management and accounting records of the Government of Edo State, and/or (ii) transferred in foreign or local currency to the dedicated accounts established by the Government of Edo State in any of the commercial banks; and (b) with respect to the dedicated Account(s) held with any of the three Commercial Banks, a full assurance

that the withdrawals from the account(s) were indeed used to finance regular and legitimate budgetary expenditures of the Government of Edo State and these are reflected in the budget management and accounting records of the Government of Edo State. Within 30 days of disbursement of the Credit by IDA the Edo State Commissioner of Finance, jointly with the Auditor General, shall also provide a written confirmation to IDA certifying the receipt of the transfer of the Credit by the CBN into the Government of Edo State's Foreign Currency Account held with CBN.

### 5.5 MONITORING, EVALUATION AND ACCOUNTABILITY

82. **Monitoring and evaluation of the reform program will be undertaken jointly by the Bank and Government teams.** The Government has established a PFM reform steering committee that meets regularly to monitor progress in implementing the PFM reform program supported by the DPO and SEEFOR programs. This committee operates under the oversight of the Chairman of the state Economic and Strategy Team as well as the state Commissioner for Budget, Planning & Economic Development. Furthermore, the SEEFOR steering committee monitors the implementation of the SEEFOR which nicely complements the DPO in two main areas. In addition, the policy and results matrix of this operation describes expected results at the end of the program and indicators for measuring success. The relevant MDAs that are directly responsible for carrying out specific actions contained in the policy matrix will be responsible for providing data on indicators for measuring progress towards end of program outcomes. This will be coordinated by a State SEEFOR/DPO Project Coordinating Unit and monitored by the Bank team during implementation support missions.

83. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

## 6. SUMMARY OF RISKS AND MITIGATION

84. **Table 12 summarizes the ratings for nine risk categories according to the Systematic Operational Risks-rating Tool (SORT).** The overall risk rating of this operation is "high" in light of the assessed risks and mitigating factors. The macroeconomic risk in particular is assessed to be high in the light of the volatility of oil prices. The subsequent paragraphs discuss the most relevant risks to the achievement of the intended outcomes as stated in the program development objective, which include the following: (a) political and governance, (b) macroeconomic, and (c)

fiduciary. Country security risks are discussed under the "other" category. No climate change or disaster risks have been determined to exist for this operation.

**Table 12: Edo State - The Systematic Operational Risks-rating Tool (SORT)**

| Risk Categories | Rating (H, S, M or L) |
|---|---|
| 1. Political and governance | S |
| 2. Macroeconomic | H |
| 3. Sector strategies and policies | M |
| 4. Technical design of project and program | M |
| 5. Institutional capacity for implementation and sustainability | M |
| 6. Fiduciary | S |
| 7. Environment and social | M |
| 8. Stakeholders | M |
| 9. Other | S |
| **Overall** | H |

85. **Political & Governance Risk:** The leadership of the current executive regime in Edo has been invaluable in steering the state along the path of reform including those supported by the DPO program. Also, majority of the state's parliamentarians are of the same political party (APC) with the executive leadership. This has helped to smooth the path of reform, especially reforms requiring parliamentary approval. Recent strains within the APC led to the defection of up to four members of the party to the opposition party – the People's Democratic Party (PDP). While the APC still maintains a two-third majority of the state parliament, there is the risk of a shift in parliamentary might to the opposition after the 2015 state parliamentary elections. Further, while the next governorship elections in Edo would not be until June 2016 and transition in November 2016; national and state parliamentary elections in 2015 (national parliamentary elections took place on March 28, 2015 while state parliamentary elections will take place on April 11, 2015) have given rise to a lot of political activity in the state as the ruling party seeks to maintain and secure majority seats in the state and national parliaments, respectively. This has posed a risk of distracting attention from the DPO program. In practical terms however, we have not seen this happen as the coordination of the DPO program is led by a technocratic group of civil servants and consultants. Thus, this risk is mitigated. There is also a risk that the future leadership of the state may not be as reform-oriented as the current one and the pace of reforms may slow. It is however expected that the institutionalization of good PFM practices due to the PFM system reforms being supported by the DPO program would mitigate many of such governance risks as they would be difficult to reverse by successive governments.

86. **Macroeconomic Risk:** There are significant risks to Edo state's fiscal program arising from a continued sharp decline in world oil prices which began in mid-2014. There are also risks arising due to oil output shortfalls as was experienced in Nigeria in 2013 and up to early 2014 due to heightened oil theft. This is especially because oil revenue dominates the revenue profile of the Edo state. About 78 percent of Edo's fiscal revenues are due to federation account transfers; which in turn are about 70 percent due to oil and gas revenues. Oil prices have declined by up to 50 percent since mid-2014. Federation account transfers to Edo state in 2014 were however only 9 percent less than in 2013 largely due to the lag in crude oil sale collections. It is however expected that if prices continue to decline sharply, federation account revenues would be reduced much further. Projections are that there will be a rebound in prices, but they will still settle at a relatively

lower average in the medium-term. The ECA which had been the buffer against these vagaries in oil price movements was significantly depleted in 2013. The government started to re-build the buffer in 2014 as oil output began to recover; however, further accretion has been hampered due to recent price developments and withdrawals continue to be made to settle petrol subsidy arrears. As of end-January, 2015, the ECA balance had been reduced to about US$2.5 billion, from US$4.1 billion in August 2014. Based on this, Nigeria's macroeconomic outlook and Edo state's fiscal outlook at this time are viewed as uncertain. Further, the continued stalling of the Petroleum Industry Bill (PIB) poses a risk to sustainable growth in oil output. In addition, Edo's fiscal program also runs the risk of being affected by policies outside the jurisdiction of the state government. This was the case in 2011 when the Federal Government through the amended Personal Income Tax Act reduced tax liabilities of low and medium income earners. Most recently, the amendment of the Pensions Act, increasing employer contribution from 7 1/2% to 10%, increased the pension liability of all employers of labor. Edo state is however implementing a credible program to expand its internal revenue base, by adding other taxes, and to optimize revenue from those new sources[29]; and this is a mitigating factor against these risks. Edo hopes to grow its internal revenue more sustainably from 2015. This is, indeed, one of the areas of focus under this operation.

87. **Fiduciary Risk**: The Edo state financial management fiduciary risk assessment conducted in 2010 revealed weaknesses in the state PFM system that pose a risk to efficient use of public funds; which could include DPO funds. However, the first Edo state DPO, along with support under the SEEFOR project have helped the state move much further than where it was in terms of PFM as of 2010. As described in earlier sections of this document, among other measures, Edo has embraced the use of a modern, computerized budget and treasury management system across its budget process; ensuring that its expenditure management systems, including the implementation of a commitment control system, are progressively robust and all budget expenditures are transacted through this (Oracle-based) financial management system, with the required in-built controls. While implementation of many of these reforms is still on-going, Edo state is moving towards better PFM practices. The design of the second pillar of this operation was made to further help this goal and mitigate this risk.

88. **Other (Country Security) Risk:** Reforms in Edo state or any other part of Nigeria could be negatively affected by a further deterioration in the security situation of the country. The instability associated with terrorism activities could engender a general slow-down of reform efforts as attention is focused on security issues and economic activity is curbed. As of date however, terrorist activity in the country has been limited to the northern parts and the Nigerian military has recently recorded some successes in the fight against the terrorists. Risks to the security of lives and property in the wake of possible post-election violence were initially considered to be high due to outbreaks of violence following previous elections. However, presidential and national assembly elections on March 28 and 29, 2015 were a lot more peaceful in comparison to the 2011 elections partly due to improvements in the conduct of the elections by the Independent National Electoral Commission (INEC).

[29] This was described in Section 4.2 of this document.

**Annex 1: Edo State Fiscal Improvement and Service Delivery Development Policy Operation: Policy and Results Matrix**

| Prior Actions and Triggers | | Results |
|---|---|---|
| **Prior Actions under ESFISDO** | **Triggers for Follow-On Operation** | **(Result indicators with baseline and targets)** |
| ***Pillar 1: Ensuring Fiscal Sustainability*** | | |
| Prior action #1: Deployment of Unique Tax Identification Number (U-TIN) registration kits at EIRS and all tax offices across Edo state | Trigger #1: Deployment of an Electronic Database Management System (EDBMS) by Edo Internal Revenue Service for the management of taxpayer data and activity | A1: Number of taxpayers captured in Edo state's electronic taxpayer (U-TIN) database<br>Baseline (2014): 38,000<br>Target (2016):120,000 |
| Prior action #2: Completion of payroll verification audit of education and health sector staff | Trigger # 2: Completion of payroll verification audit of all other MDAs (i.e. excluding Education and Health sectors) staff | A2: Audited civil service payroll with accurate staff numbers<br>Baseline (2014): No<br>Target (2016): Yes |
| ***Pillar 2: Improving Budget Institutions and Practices*** | | |
| Prior action #3: Issuance of circular by Edo state Head of Service to establish a procurement cadre in the public service in preparation for professionalization of the procurement function in MDAs | Trigger #3: Certification of at least 30% of the procurement staff in Edo state public service | B1: Percentage of procurement staff in Edo state public service[30] certified<br>Baseline (2014): 0%<br>Target (2016): 30% |
| Prior action #4: Complete systems configuration and Operational Acceptance Testing (OAT) of the SIFMIS Hyperion Budget module | Trigger # 4: Preparation of the state's budget for FY 2016 directly on the Hyperion Budget Module of SIFMIS | B2: Operational integrated electronic platform for budget preparation, execution, and reporting<br>Baseline (2014): No<br>Target (2016): Yes |
| Prior action #5: Introduce the Procure-to-Pay (P2P) module of SIFMIS for processing of all MDA expenditure transactions | Trigger # 5: Complete roll-out of Oracle SIFMIS to at least 75% of MDAs for **real-time** transaction processing (P2P) and reporting | B3: Expenditure arrears in relation to total expenditure<br>Baseline (end-2013): 25.6%<br>Target (end-2016): No more than 10% |
| Prior action #6: Approval by the state executive council of the 2015 budgets of six key MDAs[31] that are based on the sector strategic priorities articulated in the State Strategic Plan (SSP) | Trigger #6: Approval by the state executive council of the 2016 budgets of the six key MDAs that are based on costed Medium Term Sector Strategies (MTSS)[32] | B4: Number of MDAs for which Medium Term Sector Strategies (MTSSs) are prepared and reflected in the annual budget in consistency with fiscal stability goals<br>Baseline (2014): 0 |

[30]Commencing with staff of the Ministries of Basic Education; Secondary, Technical & Tertiary Education; Works; Transport; Environment & Public Utilities; and Health.

[31] These MDAs are those that usually constitute the largest share of the state's budget –Basic Education; Secondary, Technical & Tertiary Education; Works; Transport; Environment & Public Utilities; and Health.

[32] The MTSS process is to facilitate and smoothen Edo's transition to a rolling Medium Term Expenditure Framework (MTEF) as part of its annual budget process. Currently, the annual budget draws directly from the State Strategic Plan.

| **Prior Actions and Triggers** | | **Results** |
|---|---|---|
| **Prior Actions under ESFISDO** | **Triggers for Follow-On Operation** | **(Result indicators with baseline and targets)** |
| | | Target (2016): 6 |
| Prior action #7: Submission of FY 2013 annual audited financial statements of the Edo State Government to State House of Assembly within 9 months of end-FY and publication of same on the state's website or open-data web portal | Trigger #7: Submission of FY 2014 annual audited financial statements of the Edo State Government to State House of Assembly within 7 months of end-FY and publication of same on the state's website or open-data web portal | B5: Number of months between end of fiscal year and the publication of the state's audited financial statements<br>Baseline (2014): 9<br>Target (2016): 7 |
| ***Pillar 3: Improving Access to Land for Investment*** | | |
| Prior action #8: Complete an Assessment of the impact of reducing land transaction charges on the volume of formalized land transactions and state internal revenue | Trigger # 8: Implement recommendations of land transaction fee regime Assessment | C1: Land Transfer Fees[33] as a percentage of land value in Edo state<br>Baseline (2014): 26.4%<br>Target (2016): 20.4% |
| ***Pillar 4: Improving the Quality of Education*** | | |
| Prior action #9: Provision in Ministry of Education's 2015 approved budget of funding for TVET colleges based on their approved school improvement plans | Trigger # 9: Partnership agreements[34] executed between a minimum of 3 TVET colleges and private sector actors[35] | D1: Number of partnership agreements executed between TVET colleges and private sector actors<br>Baseline (2014): 0<br>Target (2016): 3<br><br>D2: Percentage of eligible female students in TVET colleges benefitting from TVET-Private sector partnership arrangements<br>Baseline (2014): 0%<br>Target (2016): 50% |
| Prior action #10: Issuance by State Universal Basic Education Board (SUBEB) of guidelines and template for monitoring and reporting on teacher and pupil attendance by school-based management committees | Trigger # 10: Issuance of SUBEB 2015 annual review report that incorporates disaggregated data and information on teacher and pupil attendance rates at basic education level | D3: Percentage of SBMCs monitoring and reporting on teacher and pupil attendance (disaggregated by gender) at basic education level<br>Baseline (2014): 0%<br>Target (2016): 60% |

[33] Otherwise called "Governor's Consent Fees"
[34] This includes collaborations, cooperation and other twinning arrangements for expertise; for apprenticeships, internships and entrepreneurship development programs for TVET students; or full-time job placements for TVET graduates.
[35] This includes small-scale entrepreneurs and large scale industrial and commercial firms in the private sector as well as professional associations.

## Annex 2: Letter of Development Policy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**OFFICE OF THE GOVERNOR**
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Ref: No. OG. 51/Vol.20/6 March 26, 2015

Dr. Jim Y. Kim
President
The World Bank
1818 H Street, NW
Washington, D.C. 20433

Dear Dr. Kim,

**Edo State Government: Letter of Development Policy**

1. On behalf of the Edo State Government, I write to request for the Edo State Fiscal Improvement and Service Delivery Credit of US$75 million equivalent from the International Development Association (IDA) to be provided through the Edo State Fiscal Improvement and Service Delivery Development Policy Operation (ESFIDO) in support of our economic transformation program whose framework has been outlined in our Edo State Strategic Plan 2010-2020. The funds provided will help to fill a financing gap that exists in the budget for implementing our development program. At the same time, the operation will also support Edo state to adopt and/or strengthen policy and institutional reforms in support of our development agenda.

2. The proposed Operation will support the deepening of policy and institutional changes in the following areas: (i) Fiscal sustainability; (ii) Budget institutions and practices; (iii) Access to land for investment and (iv) Quality of education. As part of efforts to improve fiscal sustainability, the state is continuing to adopt measures to improve its internally-generated revenue as well as further sanitize its payroll to prevent expenditure leakages. As part of measures to improve its budget institutions and practices, the state would further strengthen its public procurement institutional structure by instituting a procurement professional cadre in the state public service. The state has also adopted a more robust budget classification system and chart of accounts in order to strengthen its Public Financial Management (PFM)

information management system.It is configuring the Hyperion Budget module of its Oracle budget management system in line with a new national Chart of Accounts/budget classification system. Furthermore, the state isalso fine tuning and upgrading its deployment of the Procure-to-Pay (P2P) module of the system.Building on earlier progress made in aligning its annual budgets with its strategic policy priorities, the state has aligned its 2015 budget with the sectoral priorities outlined in its State Strategic Plan. The state would build on this process by preparing its 2016 budget based on more formal, costed MTSSs covering the period 2016-2018 and which would also be published on the state's open data portal. In addition, the state is strengthening external oversight by further improving the timeliness of preparing and submitting its audited financial statements to the state parliament. In order to improve access to investment land, the state seeks to reduce land transaction charges with a view to increasing the volume of formalized transactions. In terms of improving the quality of education, Edo will strengthen public-private partnerships in TVET education and improve accountability through greater involvement of the established School-based Management Committees.More details on the proposed reforms to be supported under the ESFISDO are set out in Part C of this letter.

**A. Reporting on the First Edo State DPO**

3. The first Edo State Growth and Employment Support Development Policy Operation was approved by the Board of the Bank in March 2012. However, due to delays at the national parliament in approving the national borrowing plan for 2012, it became effective in June 2013 and we received the funds in September 2013. The proceeds were a useful boost to our own budget resources but most importantly, the policy dialogue under this operation played a strong catalytic role in helping to steer our government on the path of policy reform while pursuing our development objectives in the areas of infrastructure development, information and communication technology and human capital development. The complementarity between DPO-1 and other Bank operations in the state were especially useful. Edo state received technical and financial assistance from the State Employment and Effectiveness for Results (SEEFOR) project as well as technical assistance from the Niger Delta Social Accountability (NDSA) project and these have strengthened the capability of the state to implement public financial management, education sector, overall governance and social accountability reforms.

4. The reforms being supported under ESFISDO for the most part represent a deepening of reforms that were supported under the first DPO. Under this engagement, as part of public financial management reforms to improve overall economic governance, we commenced a process of strengthening our public procurement practices through increased competition and transparency. We introduced a system of making public, information on contract awards above specified thresholds for transparency and social accountability purposes. We also enacted a modern public procurement law that defines the principles and procedures to be applied in the public procurement of goods, works and services. Further, we established a Public Procurement Regulatory Agency responsible for regulating the implementation of the public procurement law as well as inaugurated a state Procurement Council responsible for public procurement policy directions, in addition to this, we recently approved the

establishment of a professional procurement cadre in the state civil service system. This means that we have developed a system where civil servants can choose to become professional procurement officers in the state. All public contracts above threshold are now competitively awarded. Edo also began building a modern, computerized budget and treasury management system across its budget process. In this regard, the state is progressively ensuring that our expenditure management systems, including the implementation of a commitment control system, are progressively robust and all budget expenditures are transacted through this (Oracle-based) financial management system, with the required in-built controls. The timeliness of preparation of the State government's annual accounts as well as the external auditing of these accounts has also progressively improved from 15 months now to nine months. As part of investment climate reforms, we undertook a comprehensive workflow review of the processes and time taken to obtain land titles with the aim of streamlining these processes. We then streamlined the processes on this basis and it is now possible to process land certificates of occupancy at the Ministry of Lands & Survey within 30 days, compared with over 60 days previously. As part of reforms to improve the quality of education in the state, and in particular, technical and vocational education (TVE) to meet the state's requirements for high quality middle level manpower, Edo established school-based management committees for TVE institutions to improve governance of these institutions and consequently the quality of training received at this institutions. In order to build a strong platform for social accountability, the state unveiled an open data portal in 2013 which is to some extent, interactive and allows the state open up its activities to public scrutiny. The annual budgets, audited financial statements and public contract awards are published on this portal. This initiative has become a reference point for other states in Nigeria.

5. We have been very conscious of our obligation to the people of Edo state to deliver high value public services under a strong governance environment and the policy and institutional reform program supported by the DPO has been very useful in this regard.

**B. Edo State's Development Agenda - Progress under Edo State Strategic Plan 2010-2020**

The current Government of Edo State under my leadership was re-elected for a second term of four years on July 14, 2012 and was inaugurated on the November 12 of the same year. Since inauguration, we have continued to maintain the momentum of executing development programs spanning physical to human development. We have maintained a deliberate policy of investing in infrastructure development across the eighteen local governments of the state.

Before the end of the last term of four years (2008-2012), working very closely with the Economic and Strategy Team (EST) and all the Ministries, Departments and Agencies (MDAs) in the state, we developed a state-owned strategic plan of 10 years known as the State Strategy Plan (SSP) which is aimed at guiding development planning and policy initiatives for the people of the state. The SSP built on our earlier strategy - the Edo Vision 2020 – and is anchored on three main pillars, namely: (i) *People* (building the human capacity of Edo citizens with emphasis on Water, Health and Education), (ii) *Infrastructure* (with an emphasis on Power,

Housing, Transport, Tourism, Roads and Drainage), and (iii) *Production* (emphasis on Agriculture, Industry and Commerce). The Edo SSP seeks to position the Edo economy on a sustainable growth trajectory and prioritizes plans to significantly increase internally generated revenue (IGR) in order to reduce dependence on largely oil revenue-based federal allocations as well as ensure fiscal sustainability.

***People (Water, Health & Education)***

As a government we believe that the educational sector is the only sustainable investment that can guarantee the future of the state, hence in our first four years we concentrated in rebuilding the existing infrastructure and building new ones where they do not hitherto exist. A Total School Transformation Program through which about 435 classrooms across all the state LGAs have been renovated and equipped. However in our second term beginning from 2012 we came to the realization that communities must be involved in the management of the schools in the state. This led to the establishment of School Based Management Committees (SBMCs) across most of the schools to assist with quality monitoring and reporting.

We also went a step further by organizing and building the capacity of the technical colleges to develop school improvement plans (SIP) upon which their priorities are costed and directly funded and managed by the SBMCs and School Project Implementation Committees (SPICs). We have begun to monitor teacher attendance in schools in the state and recently concluded a process to competitively recruit and deploy new teachers to schools.

In health, a significant amount of hospital reconstruction has been undertaken including the Central Hospital in Benin which has been upgraded to a full scale tertiary hospital. Staff quarters have been built at all General Hospitals (we have one general hospital in each LGA outside of the three LGAs that make up Benin City). We have constructed/renovated more than 30 Primary Health care centres across the three senatorial districts, we have renovated infrastructure at the schools of – Nursing, Midwifery and Health Technology. We have also invested in equipment for all 33 state government-owned hospitals and have addressed staff morale and training requirements.

In terms of water supply, my administration has invested heavily in rural water infrastructure and so far, we have deployed boreholes in more than 35 communities across the three senatorial districts. Following this, we commenced a program in 2013 aimed at building the capacity of benefitting rural communities to create vehicles that will handle fund raising (via daily/weekly collections from community residents), financing of monthly running costs and day-to-day management of the boreholes from the funds raised. We have so far implemented this initiative at benefitting communities in three pilot LGAs.

We are currently preparing to invest in studies to determine how best to approach urban and semi-urban water management. This is in the light of the growth of urban and semi urban areas and their water requirements relative to the installed capacity of existing state owned water utilities; significant investments made by households and commercial entities in boreholes and the impact (of boreholes) on the aquifer.

***Infrastructure (Power, Housing, Transport, Tourism, Roads & Drainage)***

In my first term in office (specifically between 2009 and 2012), my administration contracted more than 450km of roads (with associated drainage and furnishings) across the State. To date, we have completed and commissioned more than 80% of this and have (during my second term) contracted additional road works targeted at:

- Metropolitan arterial road development – to decongest main metropolitan highways by flowing traffic unto arteries that interconnect multiple city highways. In Benin City for example, we have completed repair works on 1st East Circular Road and have awarded contracts for the upgrade/expansion of the 2nd East Circular Road and upgrade of the West Circular Road
- Rural roads development – to enhance access to schools, hospitals/primary health centres, farms and markets. Examples of completed works in this area are the construction/rehabilitation of Igbanke internal roads, Irrua-Usugbenu-Ugbegun road, Damgbala-Ojah-Uneme-Osu-Igarra road, etc.

On drainages, we have concluded phase 1 and made significant progress on phase 2 of the Benin-city storm water control project. It will be recalled that the 1st phase provides drainage infrastructure to collect storm water from the Ugbowo-Okhoro-New Benin axis and empties into Ikpoba River, while the 2nd phase is designed to collect storm water from the Ugbowo-Uwelu-Siluko axis and empties into Ekenhuan River. The completion of phase 1 has enabled us design and construct drainages (along highways and arterial roads in that axis) with gradients that channel into the storm water drainage. The same is expected upon completion of phase 2.

In 2014, we launched a new urban transport system in Benin Metropolis. This system is designed to integrate the existing Bus Mass Transit Service "Comrade Bus" to a new mini-cab service. Each service operates within dedicated zones and routes. The mini-cab service is a PPP initiative targeted at operators of the proscribed commercial motorcycle "okada" transport service. The "Comrade Bus" service was introduced during my 1st term in office, to address transportation challenges in the state and linking of towns/villages to interstate roads.

Our medium term objective on housing is to facilitate access to land for development of affordable housing on PPP basis. To this end, we have decided on the provision of affordable housing in the three senatorial districts via PPP and (by Q2 2015) we will contract a suitable consultant to conduct a state wide survey of housing deficit at the low and medium income levels and advise Edo State on effective strategies to close identified housing gaps. Our blueprint for affordable housing will be ready for implementation by Q4 2015 and will serve as basis for procurement of housing developers via PPP.

On electricity, we have (through our Rural Electrification Agency) made significant investments in rural electrification infrastructure including transformers, feeder pillars, high tension cables, etc. in all, more than 80 communities spread across 15 local government areas have experienced first time or improved electricity supply resulting from our rural electricity infrastructure investments. At State level, we are looking to provide land (and associated right of way) to enable significant growth in power production by 2020 (Edo State aims to produce 1 of every 5 megawatts of electricity produced in Nigeria by 2020). So far, we have completed (federal government owned) gas fired 450mw power plant in the outskirts of Benin City and a PPP based $2^{nd}$ (gas fired) 450-750mw power plant under construction in the same vicinity; two PPP based gas fired power plants are in the offing. My government is currently looking to encourage power production from renewable sources as well and as a first step we are looking to conduct a feasibility study at the state owned Ikpoba River dam to determine its potential for hydro-power pari-pasu water supply to the metropolis. We will further invest in feasibility studies (and site/location analysis) for solar based power generation in Edo Central and Edo North.

***Production (Agriculture, Industry & Commerce)***

In view of the importance of agriculture to accelerating economic growth and galvanizing the people for food production, crime reduction and engendering a violence free society, we have been actively involved in engaging serious minded, reputable and financially capable investors in the development of mechanized agriculture in the state. In 2014 we gave out up to 50,000 acres of land for rice production (in Edo north) under a Public Private Partnership arrangement. The uniqueness of this approach is that the communities have also been given opportunity to participate in the production process and also benefit from the availability of technology and knowledge transfer. Under this same window, the private company will collaborate with the state College of Agriculture to establish a Rice Institute at the College of Agriculture Technology that will teach courses on the development of new initiatives for rice production and milling. We are currently reviewing applications for over 250,000ha of land from prospecting investors interested in commercial agriculture for Palm, Cassava, Rubber and Rice. Our Agribusiness investment initiatives are tied to the state government's outgrower scheme, commercial agribusiness investors in Edo State are obliged to participate/support the scheme (this is enshrined in the land concession agreement).

We have also taken steps to attract our youth to agribusiness via the Edo Youth Agribusiness Initiative "Comrade Farmers". This is a capacity building programme for unemployed youths who are being encouraged to embrace agriculture as a business and source of income. They are trained on modern techniques in Cropping, Grass cutter farming, Snail farming, Goat rearing, Cattle rearing and Piggery management. Over 1,300 young Edo residents have been trained including 180 Edo citizens that returned from Libya as a result of the Libyan crisis.

Our policy thrust for industrialization is to utilize abundant electricity to promote and encourage large, medium and small scale industrial development for job creation. Through partnership with the private sector, the State Government will acquire adequate land in strategic locations (around ongoing IPP projects) for the development of industrial layouts/parks to take advantage of emerging power generation. The first industrial estate in Ologbo (near Benin) in partnership with a private firm has kicked off, the state government is currently assisting with obtaining an Export Processing Zone (EPZ) license for the project.

At the start of the $2^{nd}$ quarter in 2014, I set up a committee of the state executive council to work with the ministry of commerce and the EST to develop a framework for intervention in the micro-small-and-medium-enterprise (MSME) sector of Edo State. The Committee submitted its report in good time and its recommendations have become the basis for our application to the CBN to participate in the MSME Development Financing Scheme.

### C. The State's Policy and Institutional Reform Program

My government over the past six years has demonstrated that with focused leadership, team spirit and a right planning approach, we can be more efficient in managing resources; no matter how little; to cater for the greater interest of the larger population and improve the quality of life of the citizenry. We have come to a pleasant conclusion that real and impactful development is possible in Africa and indeed in Nigeria. We however realize that pursuing a large infrastructure and human development agenda without necessary policy and institutional reforms poses challenges for long term sustainability. We have therefore committed ourselves to reforming the way government services are administered in our state. We are interested in leaving behind a legacy that can be sustained by succeeding governments; hence we are strengthening our policy and institutional environment to enable this. We very much welcome the support of the new DPO to assist us in this regard. In this letter, I will limit myself to three main aspects of this policy and institutional reform agenda: (i) Improving the management of our public resources to ensure maximum value for scarce resources; (ii) Improving the investment climate to trigger an inflow of private investment into the state; and (iii) Improving the quality of education to empower our youths to take up emerging employment opportunities from an expanded private sector.

#### (i) Improving the Management of Public Resources

All tiers of government in Nigeria are disproportionately dependent on oil revenues from the center. Given the volatility risks associated with oil revenues, as has been evident once again since mid-2014, it is especially important for Edo state to properly manage the resources it gets; while at the same time, build more sustainable sources of revenue. As part of efforts to improve the management of our resources, Edo is prioritizing the following: (a) mobilization of internally-generated revenue (IGR); (b) efforts to plug expenditure leakages especially payroll expenditure; (c) establishment of a strong PFM institutional platform; (d) improvement in practices in strategic planning and budget preparation; (e) improved budget execution and monitoring; and (f) improved practices in internal and external auditing.

- *Mobilization of Internally-Generated Revenue (IGR)*

In order to mobilize and grow its IGR, Edo is prioritizing collections from other sources besides direct income taxes. IGR in proportion of total Edo state revenue is less than 25 per cent. Collections from direct income taxes in the formal sector comprise the bulk (about 60 per cent) of our IGR but can be affected by factor beyond our control because legislation for this tax type is under federal jurisdiction. The 2011 amendment to the Personal Income Tax Act which granted huge tax reliefs to majority of taxpayers resulted in a significant real decline in tax revenue accruable to the Edo state in 2012 We have now introduced a Land Use Charge Law in 2012 (incorporating the Ground Rent, Tenement Rate and the Property Tax) to consolidate all land related charges under one single charge for ease of administration and collection.

Administration of this tax handle, however, commenced only in 2014 but promises to deliver considerable tax returns as the state adopts measures to expand its land use tax base. Second, we enacted the Hotels and Events Centers Occupancy and Restaurant Consumption Law in 2011 and thereby introduced a consumption tax targeted at the hospitality industry which ensures that a minimum tax of 5 percent on goods and services consumed at these facilities accrues to the state government. Full implementation of this law commenced in 2013. Furthermore, we are in the process of reviewing the Entertainment tax law and have recently issued new regulations for conduct of Lottery, Pools Betting, Casino and Gaming activities in the state, with a view to optimizing tax revenue collection from these activities. Regulations for online lottery, casino and gaming activities are about to be finalized. A significant amount of IGR is expected to accrue from this source given the vibrant market that exists as a result of the large youth population in the state.

We are also improving our capability to mobilize internal revenue.After our government came into office in 2008, we were able to increase our IGR significantly by over 250 percent between 2008 and 2011 as we implemented measures to eliminate inefficiencies in revenue collection and plug many sources of leakage. Tax audits were conducted and a sizeable amount of the increased collections were tax arrears accruing from back tax assessments. However, we recognize that there is a huge potential to improve IGR further. Also, we estimate that the number of tax payers captured in the tax net is much below potential. In this regard, our Internal Revenue Service is finalizing plans to undertake a state-wide electronic taxpayer enumeration survey. In parallel, we have deployed electronic taxpayer registration kits at the Internal Revenue Service headquarters in Benin City and at all our tax offices across the 18 local government areas of the state; and will subsequently establish an Electronic Data Base Management System (EDBMS) of identified taxpayers. This is geared towards maximum tax net capture, especially for the informal sector as well as better enforcement. The EDBMS will constitute a reliable, transparent and efficient system to enable the state better track, monitor and manage taxpayer activity as each taxpayer will be identifiable by a unique taxpayer number with their biometric data captured.

We also recognize the importance of institutional capacity development in tax administration. In this regard, we enacted a new revenue administration law in 2012. The law establishes the EIRS as an autonomous revenue service anchored on strict professionalism, transparency, integrity and results. Also, the EIRS is also strengthening tax administration capacity through a major organizational structure and business process re-engineering for improved service delivery and full automation of processes. It is undertaking service-wide training/capacity needs assessment to guide capacity development for EIRS staff. Also, we are leveraging ICT for better taxpayer service delivery. We have deployed Point of Sale (POS) terminals at all the collecting banks linked to the IGR accounts and are on the verge of launching a new and dedicated website that supports online tax payment as well as other taxpayer services like TIN registration

- *Eliminating Payroll Expenditure Leakages*

In order to plug payroll expenditure leakages, our government, in 2011, gathered relevant biometric data pertaining to public servants and transferred the data to an oracle-based human resource system to enable monthly payroll calculation.This reduced cases of ghost workers appearing on the payroll. Building on this achievement, our government intends to periodically conduct verification audits of the payroll to establish their continued authenticity and integrity and avoid leakages through this route that has traditionally constituted a huge source of expenditure leakage. In early 2015, we hired a consultant to conduct an independent verification audit of our employee and pensioner database beginning with the largest ministries – Education and Health. A preliminary report of this first phase has been submitted by the consultant and we would take action as necessary.

- *Establishment of a strong PFM institutional platform*

As part of measures to establish a strong public financial management (PFM) institutional platform, we are strengthening our PFM legal and regulatory framework; our human and organizational capacity for PFM; as well as our PFM information system. We are entrenching our improved PFM policies and practices in relevant laws in order to protect them from being easily reversed.Given the importance of the public procurement process in ensuring that public expenditure delivers good value for money, Edo prioritized the enactment of a modern public procurement law in its institutional reform program.This was a prior action under the first DPO. The law defines the principles and procedures to be applied in the public procurement of goods, works and services. It also defines in the regulations, respective roles of different institutions and officers in public procurement. We have established a Public Procurement Regulatory Agency in March 2014 responsible for regulating the implementation of the public procurement law and also inaugurated a state Procurement Council responsible for policy directions.We are currently preparing an organic Public Finance law along with related Financial Regulations and Instructions that would, among other things. help redefine the roles and responsibilities of both line ministries and central management agencies. the accountability of vote holders, rules on debt and the creation of special funds, accounting, internal control and financial reporting requirements, the treasury functions of the Accountant-General, powers of the legislature and rights and obligations of functionaries and citizens in the financial matters of the state. Furthermore, we are revising the Edo Audit Act of 1982 and related regulations.

We are strengthening the human and organizational capacity for PFM thorough a strengthened capacity building framework across central finance institutions and key MDAs. In terms of the PFM information system, the Oracle system for budget preparation, execution, accounting and reporting is being scaled up with enhanced modules for improved financial management; and key financial management bottlenecks impacting the effectiveness and efficiency of service delivery have been expunged from the procedures without weakening internal controls. Furthermore, the state intends to establish a PFM reform coordination unit to be hosted in the Ministry of Finance, to be staffed by qualified personnel for improved PFM reform coordination. The Unit will coordinate all PFM related reform actions across the government; serve as the secretariat for the PFM Steering Committee and the Technical Committee; and monitor the State's PFM performance as custodian of the self-/independent assessment exercises on PEFA or other PFM performance assessments. The PFM reform unit will provide regular reports to the Steering Committee on progress in the implementation of the state's PFM reform action plan. as well as support the modernization of the State Auditor-General's Office and the PAC Secretariat, among other tasks. To operationalize the procurement units that were recently created in the respective MDAs, the state civil service office will institutionalize a new procurement professional cadre. It is the plan to progressively build the professional capacity of this new cadre based on a Procurement certification program.

- *Improvement in Practices in Strategic Planning and Budget Preparation*

Our government recognizes the crucial role of strategic planning and budget preparation in improving public expenditure. Thus, we are building on earlier progress made in aligning our annual budgets with our strategic policy priorities.Building on our 2009 Vision 2020 document which outlined our medium term development priorities, we have developed a State Strategic Plan (SSP) as the framework for the strategic planning process. The SSP consists of the government's priorities translated into sector objectives initiatives, which are incorporated into the annual budget preparation process. We are in the process of strengthening this framework by introducing a multi-year perspective to our budgeting through the development of costed Medium Term Sector Strategies (MTSSs) with more detailed strategies and initiatives for achieving medium term sector goals and objectives within a specified medium term frame. Currently, the state is benefitting from the expertise of a PFM consulting firm presently resident in the state and supporting the relevant officials to be able to prepare MTSSs. The first of the MTSSs will cover the timeframe of 2015-2017 and would be completed in April 2015. However, this will be too late to inform the 2015 budget of the state; but it would aid the learning process of the state officials ahead of 2016 budget preparation. The preparation of the 2015 budget of all MDAs has however drawn from the sector strategies as contained in the SSP. This is a prior action for this operation and is evidenced by templates prepared by the Ministry of Budget and Economic Planning which map the projects in the approved 2015 sectoral budgets to the key sector strategies prioritized in the SSP. The state would build on this process by preparing its 2016 budget based on more formal, costed MTSSs covering the period 2016-2018 and which would also be published on the state's open data portal. The use of MTSSs for preparation of the budgets of five key MDAs is a trigger for the subsequent operation

- *Improved budget execution and monitoring*

Our government continues to pursue improvements in practices relating to budget execution and monitoring in a bid to improve the efficiency of public expenditure and service delivery. To this end, continued enhancements to procurement, cash management and budget implementation monitoring practices and mechanisms are being implemented. The public procurement reforms being implemented by Edo are geared towards the achievement of transparency, accountability, competitiveness, and value for money in the public procurement processes of the state. As earlier mentioned, we enacted a modern public procurement law in 2012 to define the principles and procedures to be applied in the public procurement of goods, works and services. Further, we established a public procurement regulatory agency in 2014 to regulate the public procurement practices of the state in line with the law. Procurement Regulations, Manuals and Standard Bidding Documents are being developed by the regulatory agency to be deployed to the MDAs for use. Our government will continue to make public, information on contract awards above specified thresholds for transparency and social accountability purposes. Furthermore, the procurement agency would conduct annual procurement audits of a representative sample of contracts awarded and submit these reports to the state legislature. The government, in its quest to maintain a reliable cash planning system, has developed a database enterprise application tool that tracks all contracts, including multi-year contracts, from the point of award (commitments), to progress payments (progress certificates), and final payment (liquidation) as well as contract closure. This database application system of monitoring capital projects is one way in which the state government keeps a tab on capital budget implementation. This system maintains detailed

and comprehensive information on projects and contracts but currently covers only three major ministries: Works, Health and Environment. Ministry of Education would be the next to be covered. Already, the state has introduced an Electronic Funds Transfer (EFT) system for the payment of all supplier bills. This is critical to reducing payment delays as well as the potential for fraud under a progressive system towards a 'cash-less' economy. The State electronically transfers payments to suppliers' bank accounts, on a general basis, rather than issuing them paper cheques.

- *Improved practices in internal and external auditing*

Over the last few years, our government has significantly improved the timeliness of preparing the state's audited financial statements. As a prior action for the first DPO, Edo state cleared a two-year audit backlog. Currently, audits are now completed within 2 months of receipt of draft accounts from the State Accountant-General, and audit reports are subsequently laid before the State House of Assembly (SHoA) for review by the Public Accounts Committee (PAC). The audited financial statements for the year 2013 were submitted to the SHoA within nine months of the year-end – a clear case of timeliness and improved financial transparency; and the historical series of audited financial statements are also published on the state's open data portal. The state aims to further improve on the timeliness of submission and publication of the audit reports. Audit quality is improving although full compliance with INTOSAI standards will take some time. The state has now procured consultancy services to support the revision of the Edo Audit Act of 1982 and related regulations as well as to support the modernization of the State Auditor-General's Office and the PAC Secretariat, among other tasks. Once delivered, the external audit function of the State as well as the legislative oversight Secretariat (PAC) would have been strengthened to better deliver on their mandates

### (ii) Improving the investment climate

The economy of our state has hitherto been largely public sector-driven; as government has in the past invested directly in virtually all areas of economic activity, including state government-owned breweries, transport services and retail companies. The rationale was that the state did not have enough indigenous entrepreneurs to invest in these and other areas of the economy. But direct government ownership of such companies stifled the enterprising spirit of potential indigenous entrepreneurs. The private sector though now expanding is still relatively weak. The traditional subsistence sector and small-scale commercial and service activities in the informal sector dominate the industrial landscape. The educated unemployed do not find these two sectors attractive. Our government therefore views it as very important to improve the enabling environment to increase the contribution of the private sector, especially large corporates, to economic growth and to employment generation, either in partnership with the public sector (public-private partnerships) or in parallel. One of our main focus areas for policy and institutional reform in improving theinvestment climate is the area of access to land for investment purposes.

In 2011, we began taking steps to improve the process for obtaining titles to land; i.e. Certificates of Occupancy (C of O's).It usually took a long time for property owners to obtain C of O's inEdo State. As a result, many economic agents did not have title to their property. Economic agents were therefore limited in their ability to make long term investments. It was also a disincentive for potential new investors. The Ministry of Lands & Survey thus conducted a comprehensive workflow review of the processes and time taken to obtain C of O's in 2011. Based on this, we developed and have been implementing streamlined procedures for obtaining C of O's. We published these new procedures on the state government's website. It is now possible for the Ministry of Lands & Survey to process applications for C of O's within 30 working days using these streamlined procedures; down from up to 100 days or more previously. Also in 2011, we commenced the process of developing a new Land Information System (LIS) that is based on geo-referenced digital maps in order to improve the reliability of land information and consequently, the land registration process.We sought to modernize this system through the development of a GIS-based LIS. As a prior action for the earlier DPO, we executed an agreement with a concessionaire for devising and running the Edo GIS. We also established a website for the Edo GIS and published the first set of land maps produced under the EGIS as a means of fostering transparency and improving public access to relevant information on land. This was also a prior action under the prior DPO. However, by late 2013, the concession agreement for the Edo GIS had suffered a setback and collapsed. We however have not allowed that to weaken our resolve to improve the land information system for Edo state. We therefore contracted an ICT firm in 2014 to install the GIS software to be piloted, in the urban areas first, on limited basis (Benin City only); thereafter the system will be rolled out to more local governments across the state.We have also taken the bold step to rationalize the procedures for transferring land titles in the state through the delegation of the governor's consent to the state attorney-general.

Furthermore, in order to mitigate the constraints imposed by assessed high land transaction charges in the state, our government, in 2015, is taking steps aimed at reducing land transaction charges. We will continue to leverage on the best available technology tools to ensure that interested residents in the state have quick processing times for their application for land title documents. We will also leverage on our partnership with you to build our capacity in this regard. We hope to generate a chunk of our local revenues from land related taxes and unlock the potentials in this very critical sector of the soft economy.

### (iii) Improving the Quality of Education

Our government seeks to strengthen the capacity of the young people in the state to be able to take on employment opportunities as they are created by a more active private sector.Improving the quality of education from the primary to the tertiary level; especially science education and including vocational and technical education is therefore one of our government's strategies to tackle unemployment in the state. Ourgovernment sees technical and vocational education and training (TVET) as critical to youth empowerment and employability. Thus, we have been working to revamp the system of public TVET in the state. Hitherto, most of the state-run TVET colleges were run down in terms of physical infrastructure and were not very well governed. Earlier on, we had established School-Based Management Committees (SBMCs) in Technical and Vocational Education Institutions, with broad representation, including from civil society, to carry out some of the responsibilities decentralized to the institution level. The established

School Based Management Committees now formulate annual TVET school improvement plans (SIPs) since 2014 for each of the TVET schools; and we allocate funding in the budgets of the Ministry of Secondary, Technical and Tertiary Education for the implementation of the school improvement plans. Further, we aim to enhance the quality of content delivered at TVET colleges by establishing collaboration mechanisms with the private sector – small-scale entrepreneurs, large-scale industrial and commercial firms, as well as relevant professional associations. These collaboration mechanisms will include transfer of expertise from industry to the colleges, apprenticeships, internships and entrepreneurship development programs for TVET students or full-time job placements for TVET graduates. Already, the state is in discussions with Dangote Group to collaborate with the state College of Agriculture to establish a Rice Institute at the College of Agriculture Technology that will teach courses on the development of new initiatives for rice production and milling.

**We are also taking the issue of teacher absenteeism very seriously in Edo state.** We have implemented numerous measures aimed at improving the commitment of teachers to their jobs. A series of unscheduled school inspections sometimes led by myself, has resulted in the dismissal of some teachers, school inspectors and local government education officers. There is however still a crucial need to ensure effectiveness of these efforts. We want to position primary and secondary school-based management committees to complement the efforts on Ministry of Education inspectors to monitor teacher attendance at schools. This will be coordinated by the State Universal Basic Education Board (SUBEB).

## D. Conclusion

Let me express the appreciation of the Edo state government for the strong support given to us by the World Bank, and for the DPO program in particular. We understand that the willingness of the Bank to extend budget support to Edo state is a reflection of the Bank's confidence in the state's ability to implement its development program to deliver real benefit and outcomes for the citizens of the state. We are honored by this confidence and we pledge to continue to diligently implement the reforms outlined above in support of an enabling environment for the Government to implement its poverty reduction goals as set out in our development strategy.

Yours Faithfully

Adams Aliyu Oshiomhole, *mni,* CON
Governor

## Annex 3: IMF 2014 Article IV Consultation Mission Statement

### Statement of IMF Executive Board at the Conclusion of the IMF Article IV Consultation with Nigeria

Press Release No. 15/91
March 4, 2015

On February 27, 2015, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[36] with Nigeria.

Nigeria has a large and diverse economy that has achieved a decade of strong growth, averaging 6.8 percent a year, and now accounts for 35 percent of Sub-Saharan Africa’s gross domestic product (GDP). Inflation has remained in single digits for two years, and the banking sector, which has a strong capital base, is expanding credit. The trade surplus has been declining since the second quarter of 2013 on lower oil exports and continued strong growth of imports, and gross international reserves have been falling. Meanwhile, the general government fiscal deficit and public debt have been kept low. However, Nigeria still lags its peers in critical infrastructure and has high rates of poverty and income inequality. While the economy is diverse, with services accounting for over 50 percent of GDP in 2013, and oil only 13 percent, the oil sector remains a critical source for revenue and foreign exchange. With limited fiscal and external buffers (US$2 billion in the excess crude account and US$34.25 billion in gross international reserves, respectively at the end of 2014), the sharp decline of oil prices in the second half of 2014 underscores the challenging but compelling need to address remaining development challenges.

The authorities have responded to a sharp decline in oil prices. On February 18, 2015, the Central Bank of Nigeria closed the Dutch Auction System (rDAS) window, unifying the rDAS rate with interbank foreign exchange market rate. On February 25, 2015, the Senate approved the third revision to the 2015 budget, tightening the fiscal envelope by lowering the budget benchmark oil price to US$52/barrel.

In 2015, oil exports are projected to decline by 6 percent of GDP from the 2014 level, and oil revenue by 2 percent. A sharp contraction of public investment and domestic demand is projected to reduce growth to 4.75 percent in 2015 from 6.3 percent in 2014. Inflation is projected to rise to 11.5 percent by the end of 2015 from 8 percent at end 2014, reflecting the pass through from exchange rate depreciation. The outlook is subject to downside risks, both external (changes in oil market developments and investor sentiment) and domestic (uncertainty over the election outcome and the security situation).

[36] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

**Executive Board Assessment**[37]

Executive Directors commended the authorities for progress in promoting Nigeria’s economic diversification and for their macroeconomic response to collapsing export prices. Directors noted, however, that vulnerabilities remain high in view of the uncertainties about oil price, security, and the political situation, and concurred that additional policy adjustments and broader structural reforms will be necessary in the period ahead to reconstitute buffers, mitigate risks, and meet pressing development needs.

Directors agreed that tightening fiscal policy and allowing the exchange rate to depreciate while using some of the reserve buffer were appropriate responses to the recent fall in oil prices. Nonetheless, Directors stressed that achieving the authorities’ fiscal targets will require a careful prioritization of public spending and a cautious implementation of capital projects. They also highlighted the importance of improved budgeting at the level of state and local governments to help better manage their fiscal adjustment.

Directors agreed that mobilizing additional non-oil revenues is critical to open up fiscal space and improve public service delivery over the medium term. They welcomed ongoing initiatives to strengthen tax administration, and encouraged the authorities to also rein in exemptions, keep tax rates under review, persevere with subsidy reform, and improve the management of oil revenue. Furthermore, Directors saw merit in reviewing the current revenue sharing arrangements to help address regional disparities over the longer term and ensure that social and development needs are addressed.

Directors welcomed the recent unification of the foreign exchange rates, noting that greater exchange rate flexibility could help cushion external shocks. As the largest single supplier of foreign exchange, it will be important for the central bank to intermediate this supply in a transparent, efficient, and fair manner.

Directors noted that financial soundness indicators remain above prudential norms, but the concentration of credit risks and foreign currency exposures call for continued close oversight. They welcomed progress in strengthening supervision and regulation, including of cross border activities, and encouraged additional initiatives to foster financial market development, including of hedging instruments, and improve financial inclusion.

Directors emphasized that Nigeria’s longer term prospects rest on lowering oil dependency and strengthening private sector’s participation in economic activity. Lasting and more inclusive growth calls for improving the business environment, promoting youth and female employment, and advancing human capital development.

Directors noted that Nigeria’s economic data are broadly adequate for surveillance. Nonetheless, they encouraged the authorities to further improve statistics, in particular as regards the balance of payments.

[37] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

**Nigeria: Selected Economic and Financial Indicators, 2012–2015**

| | | | |
|---|---|---|---|
| Nominal GDP (2013, billion U.S. dollars) | 521.8 | Quota (million SDR) | 1,753.2 |
| GNI per capita, Atlas method (2013, US$) | 2,710 | Population (2012, million) | 168.8 |
| Poverty headcount ratio (adult equivalent, | 46.0 | GINI index (2010) | 48.8 |
| Life expectancy at birth (2011, years) | 52 | | |

| | 2012 | 2013 | 2014 Prel. | 2015 Prel. |
|---|---|---|---|---|
| **National income and prices** | (Annual percentage change, unless otherwise specified) | | | |
| Real GDP (at 2010 Basic Prices) | 4.3 | 5.4 | 6.3 | 4.8 |
| Oil and Gas GDP | -4.9 | -13.1 | -1.3 | -1.6 |
| Non-oil GDP | 5.9 | 8.3 | 7.3 | 5.5 |
| Production of crude oil (million barrels per day) | 2.3 | 2.2 | 2.2 | 2.3 |
| Consumer price index (end of period) | 12.0 | 7.9 | 7.9 | 11.5 |
| **Consolidated government operations**[a] | (Percent of GDP) | | | |
| Total revenues and grants | 14.3 | 11.0 | 9.9 | 7.7 |
| **Of which:** oil and gas revenue | 10.4 | 7.1 | 5.8 | 3.4 |
| Total expenditure and net lending | 14.7 | 13.4 | 12.3 | 10.6 |
| Overall balance | -0.3 | -2.4 | -2.5 | -2.8 |
| Non-oil primary balance (percent of non-oil | -11.6 | -9.7 | -8.1 | -5.5 |
| Excess Crude Account / SWF (billions of US$) | 11.0 | 3.8 | 3.6 | 1.5 |
| **Money and credit** | (Contribution to broad money growth, unless otherwise specified) | | | |
| Broad money (percentage change; end of | 29.1 | 0.9 | 7.3 | 10.8 |
| Net foreign assets | 15.9 | -3.4 | -7.4 | -0.1 |
| Net domestic assets | 2.3 | 4.3 | 14.6 | 10.9 |
| Treasury bill rate (percent; end of period) | 13.3 | 11.5 | 13.0 | ... |
| **External sector** | (Annual percentage change, unless otherwise specified) | | | |
| Exports of goods and services | 1.8 | -0.9 | -5.1 | -37.4 |
| Imports of goods and services | -10.6 | -4.9 | 9.7 | -16.6 |
| Current account balance (percent of GDP)[2] | 4.4 | 3.9 | 2.2 | 0.2 |
| Terms of trade | 1.0 | 0.4 | -2.6 | -25.6 |
| Price of Nigerian oil (US$ per barrel) | 110.0 | 109.0 | 100.6 | 52.8 |
| Nominal effective exchange rate (end of period) | 81.4 | 83.1 | ... | ... |
| Real effective exchange rate (end of period) | 135.6 | 150.1 | … | … |
| Gross international reserves (US$ billions) | 43.8 | 42.8 | 34.3 | 28.4 |
| (Equivalent months of next year's imports) | 7.1 | 6.3 | 6.1 | 4.7 |

Sources: Nigerian authorities; World Bank; and IMF staff estimates and projections.

[a/] Consists of federal, state, and local governments.