

RIVERS STATE GOVERNMENT

ARREARS CLEARANCE FRAMEWORK

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ACCRONYMS:

OAGF	Office of the Accountant General of the Federation
APA	Annual Performance Assessment
DLI	Disbursement Linked Indicator
DLR	Disbursement Linked Result
DMO	Debt Management Office
FRA	Fiscal Responsibility Act
FRL	Fiscal Responsibility Law
IGR	Internally Generated Revenue
ISPO	Irrevocable Standing Payment Order
IVA	Independent Verification Agent
MDAs	Ministries, Departments and Agencies
PforR	Program for Result
SFTAS	States Fiscal Transparency Accountability and Sustainability Program
FGN	Federal Government of Nigeria
WB	The World Bank

SECTION 1.

1.0 INTRODUCTION

It is becoming increasingly challenging for government to meet its financial obligations as at when due, particularly in the face of dwindling revenue. The often mismatch of government revenue and expenditure in government budgeting has constrained government to incur debts which often time result in expenditure arrears, ostensibly due to Government inability to pay as at when due. Expenditure arrears most time are result of poor financial management practices, unrealistic budgeting, gaps in reporting, inefficient cash management and inadequate legal framework.

The accumulation of domestic expenditure arrears by government can have serious negative effect on the domestic economy; a large flow of arrears may disguise the true size of government deficit, significantly reduce the impact of fiscal policy on aggregate demand and potentially undermine macro-economic stability. It is therefore imperative that government at all levels design and implement a practicable Expenditure Arrears Clearance Framework (ACF) to effectively manage their domestic expenditure arrears.

In line with her quest to effectively management her domestic expenditure arrears, the Rivers State Government has prepared this Domestic Arrears Clearance Framework as a working document for the management of its domestic expenditure arrears.

1.1 COVERAGE AND SCOPE OF THE FRAMEWORK:

This document covers the policy guidelines and procedures for managing and settling the domestic expenditure arrears of the Rivers State Government. The State's arrears are financial obligations that have been incurred by the Rivers State Government for which payment have not been made by the

due date. These payments may have been overdue based on the following:

- Specific contractual commitment such as payment for construction of roads
- Particular local obligation such as of salaries
- Continuing service arrangement such as payment for electricity supply.
- Paucity of fund.

The framework is guided by the World Bank and the Federal Debt Management Office's (DMO) template for the establishment of Domestic Arrears Clearance Committee (DAC), as well as established best practices in the settlement of State's Domestic Expenditure Arrears. The main categories of Rivers State's expenditure arrears are as follows:

- Contractors' Arrears;
- Pension and Gratuity Arrears;
- Salary Arrears and
- Judgment Debt.

Expenditure arrears also describe as payables under liabilities and commitments which have remained unpaid beyond a specified due date of payment and where no due date is specified, have remained unpaid after a specified number of days after the date on the invoice or contract, in accordance with a law, regulation, government policy or local practice. Commitments are explicit or implicit agreement to make payments to another party in exchange for supply of goods and services or of fulfilling other conditions. Commitments can also be of a continuing nature that requires a series of payments. They may or may not involve a contract, but they are often based on a legal obligation.

1.2 PURPOSE OF THE FRAMEWORK DOCUMENT

This framework document is aimed at providing practical guidance in the identification, recording and management of domestic expenditure arrears in Rivers State. This will assist the State to establish system and processes to facilitate reduction of her stock of domestic expenditure arrears.

1.3 USERS OF THE FRAMEWORK DOCUMENT

This framework is primarily meant for the government of Rivers State. Besides, the staff of Ministries, Departments and Agencies (MDAs) such as Ministry of Finance, Office of the Accountant-General, Ministry of Budget and Economic Planning, Office of the State Auditor-General, Bureau of Public Procurement, Ministry of Works, State Pension Board and other line MDAs, etc., who may be involved in debt management and settlement of arrears at one time or the other will find it useful. The framework should be used in conjunction with other extant public finance laws and regulations, the accounting system and procedures manuals of the State.

1.4 DESCRIPTION OF RIVERS STATE'S POLICY ON ARREARS:

The Rivers State policy on Domestic Expenditure Arrears management is aimed at controlling the accumulation of expenditure arrears, ensuring their completeness, accuracy, and validity and the prompt settlement thereof. The Rivers State Government shall adopt the following measures to clear her existing arrears and prevent accumulation of new ones:

- The State shall empower her legal and regulatory framework on financial issues by strengthening legal and regulatory framework
- The State shall ensure that its budget shall be a realistic plan for expenditures and revenues to enhance its credibility and the borrowing limit shall include a margin to handle the situation of revenue shortfalls;

- The State shall deploy a robust integrated financial management information system to enhance its financial management and reporting practices and strengthen control measures to curb revenue leakages and other corrupt practices.
- The State Government shall strengthen her commitment controls to effectively limit commitments to approved budget allocations and to availability of actual cash;
- The State shall adopt a modern/active cash management system and an integrated cash and debt management arrangement, to facilitate availability of fund to meet government financial obligations as at when due.
- Establishment of Treasury Single Account (TSA) and concentration of government cash balances to ensure effective aggregate control over government cash balances and avoid unnecessary borrowing.
- Payment shall be centralized to the State Treasury to prevent arrears as a result of administrative hurdles;

SECTION 2.

2.0 PLANNED ACTIONS FOR SETTLEMENT OF RIVERS STATE DOMESTIC EXPENDITURE ARREARS

The Arrears Clearance Framework is designed to address the causes for the accumulation of arrears and prompt settlement of outstanding stock. The framework will communicate to stakeholders, the government plan, timetable and criteria for the liquidation of arrears, thereby minimising any possibility for and perception of favouritism and corruption in payments

Rivers State Multi-Year Plan is the financial plan of the State for clearance of her stock of arrears based on the total fund available to the State in the fiscal year. The State Government shall clear her arrears using funds from any of the following sources:

- The State's Internally Generated Revenue (IGR);
- Federal transfers;
- Grant from the Federal Government;
- Borrowing;
- Bonds;

2.1 PRINCIPLES GUIDING THE ARREARS CLEARANCE STRATEGY

The following key factors will guide the Domestic Expenditure Arrears strategy.

- **Comprehensiveness:** The Arrears clearance should apply to all outstanding payments incurred by the government.
- **Transparency:** Transparency is key in every facet of the Domestic Expenditure Arrears Clearance process.
- **Credibility:** The process should be seen as credible. To demonstrate commitment to addressing the root causes of the problem, the strategy should include measures to avoid the accumulation of new arrears, and MDAs that fail to implement these measures should be penalized appropriately.
- **Realistic**
- **Verification:** Arrears should be verified to ensure that only valid claims are cleared. This activity shall be undertaken by the State Auditor-General's Office, or internal audit function in the Ministry of Finance. This process will include the following steps:
 - **Step-1. Collection of Unpaid Invoices:** The initial responsibility for producing the necessary documentation will rest with the Chief Financial Officer (Director of Finance and Accounts) of the respective MDAs.

The responsibility for the proof of validity of claims without proper documentation will rest with the claimant. Only original documents will be accepted, not photocopies, to avoid fraudulent claims.

- Step-2. Verification of Claims: Arrears will be subject to tests to verify their existence, value, and age of the debt.
- Step-3. Categorization of Claims: Based on the review of validity, each claim will be categorized as valid, contestable, or rejected.
 - ✓ Valid claims are those for which adequate documentation exists to recognize a government liability.
 - ✓ Contestable claims are those for which incomplete documentation has been provided.
 - ✓ Rejected claims are those for which legitimate documentation has not been presented.
- Step-4. Appeals from Claimants: Holders of contestable claims shall be invited to provide further documentation to support their claims or have their claims referred for adjudication. Such claims may arise through collusion with government officials or poor record keeping. The burden of proof on the validity of such claims will rest with the claimants, and the government may decide to settle them in the future on a case by case basis, based on the recommendations of the independent arbitrator. Claim holders will have the right to appeal the independent arbitrator's decisions through the judicial system.
- Step-5. Rejection of Invalid Claims: The government will formally notify rejected claimants and state the basis for the rejection. It is essential that government retain full records of decisions made to defend future legal actions by claimants that may arise.

Arrears will be verified using the following guidelines:

- The legal validity of the payable shall be verified by checking that the transaction was duly authorized by a responsible officer in accordance with authorized public finance and procurement laws, rules, regulations and consistency with budgetary authorizations. Where this is not the case, appropriate sanctions will be applied to officials, and a legal assessment will be made as to whether the claim is valid.
- Evidence that the goods were delivered and services were duly received and accepted by a responsible officer shall be verified.
 - ✓ In case of doubt or for material transactions, delivery will be reconfirmed by requesting information from the supplier.
 - ✓ For goods and services, the financial records of the supplier can be asked to show that amount was registered as a receivable in their accounts.
 - ✓ In cases of salary arrears, payroll records shall be checked to ensure beneficiaries were employed at that time.
 - ✓ In more complex transactions, particularly those related to major construction or other investment projects, evidence of certificate of valuation or a completion certificate produced by relevant experts shall be required.
- Invoices and supporting documentation will be checked to verify the value of the amount payable. Invoices should contain the following information at a minimum:
 - ✓ The amount,
 - ✓ The supplier,
 - ✓ The reference to the contract or
 - ✓ Purchase order or agreement signed by the responsible officials, and
 - ✓ The documents confirming receipt of goods or services,

such as the inventory records of the purchasing entity. In case of doubt, a cross-check with suppliers' financial statements shall be made.

Entitlement arrears shall be computed by the line Ministry or Agency and provided to the Ministry of Finance.

▪ **Classification:**

Once collected and verified, the data of the arrears shall be analyzed and classified for the purposes of arrears clearance. A database of valid outstanding payments shall be established and maintained centrally by the Ministry of Finance.

This can be a resource-intensive and time-consuming exercise, requiring dedicated staff resources. A practical approach will be to focus in the first instance on large claims, gradually expanding the coverage of the database.

- **Contractual terms:** The database shall capture any relevant contractors' information including, for example, whether the outstanding balance results in interest and/or penalties for non-payment.

- **Payment status:** The database shall capture the total amount due on the invoice, amounts already paid, amount outstanding, and any rescheduling, discounting, or factoring of the unpaid obligation.

- **Risk of non-payment:** The database shall include a risk assessment of further payment delays. For example, if civil servants are not paid, this could be a potential for industrial action; if a contractor for a major infrastructure project is not paid, the project may not be completed, or completion may be delayed for many years. Other risk factors will include litigation and potential socio-economic impacts.

When the database has been established, the Ministry of Finance or its Agency shall keep it up-to-date showing the discharge of arrears and any subsequent additions to the stock. All stocks of accounts payable will be classified as liabilities, further classified as either domestic or foreign, and included in

the government's measurement of gross debts. Payments in arrears shall be included as a memorandum item to the government's Balance Sheet.

2.2 Key Actions for each step of the Arrears Clearance Strategy:

A comprehensive, transparent and credible arrears clearance strategy should typically follow the following steps:

- Stocktaking
 - Verification
 - Classification
 - Prioritization
 - Liquidation
- **Stock-taking:** A stock taking of arrears will enable the State government to understand the extent, composition and the age of the State government's unpaid bills and prioritize their clearance.
The State government would come up with a time table which should be communicated for the stocktaking exercise, and a clear definition of the information requirements should be provided to all relevant stakeholders.
- **Verification:** The data should be verified to ensure that they are genuine claims.
- **Classification:** Once collected and verified, the data of the arrears should be analyzed and classified for the purpose of arrears clearance. A data base of valid outstanding payments should be established centrally by the Ministry of Finance.
- **Prioritization of Arrears for Clearance**
Once the database of valid claims on government is established, a set of criteria for prioritizing their liquidation should be determined. The prioritization should be based on transparent criteria depending on the nature of the arrears. The following factors should be put into consideration prioritization of arrears for clearance:

- Socia-economic impact: arrears to economically sensitive or vulnerable sectors, such as salaries of low income workers, pension and social benefits should be prioritized.
- Age of Debts: Older obligations should have priority over newer obligations.
- Cost: Arrears that accrue interest and penalty charges should have priority.
- Risk: Arrears that may result in legal action, disruption of essential services or cost escalation of future supplies to government should be prioritized.
- Currency: Payment of foreign currency denominated debts should be prioritized.
- Creditors: The government should prioritize the clearance of intra-governmental debts, as this can be done administratively through the annual budget at minimal net cost.
- Value: Government should grade the debts according to their amount. Whereas large amount is placed in the lower rung of the ladder, smaller amounts may be accumulated as early as possible.

- Liquidation

The payment or liquidation of obligations shall begin after establishing and publishing the criteria for prioritizing arrears for clearance.

- The Arrears Clearance Committee: The Arrears Clearance Committee will oversee arrears liquidation to ensure the consistent application of the principles of the framework. The committee shall ensure that payments are made in accordance with the agreed prioritization criteria.

This committee will comprise representatives from relevant departments, receive reports from spending units, and prepare periodic (for example, quarterly) reports to the Ministry of Finance on the performance of

entities on payment of arrears. The reports should highlight any non-reporting spending units and recommend remedial actions.

- Provision in the Medium-Term Expenditure Framework (MTEF): The annual budget and medium-term budget framework shall make explicit provision for the clearance of arrears. The Multi-Year Plan is the financial plan of the State for clearance of her stock of arrears based on the total fund available to the State in the fiscal year.

Measures including the centralized management and control of the budget line for arrears repayment shall be put in place to avoid the recycling of arrears (paying old arrears while accumulating new ones). Any payment from this centralized budget will be backed by a list of verified eligible creditors, in line with the priorities of the repayment strategy.

Entities shall be required to provide this information to the Ministry of Finance for budget preparation, medium-term expenditure framework, performance monitoring, and budget release purposes, as well as verification against the database at the time of payment.

A separate control on the remaining stock of arrears shall be kept by the Ministry of Finance to ensure that sufficient provision is made in each subsequent annual budget until all arrears are paid.

- Centralization of Payments: Responsibility for payments of arrears shall be centralized. This is to ensure that payments are made according to the agreed framework and schedule. Reports of payments made against the budget line for arrears in addition to regular fiscal reports will help to demonstrate the government's commitment to the arrears clearance strategy and build confidence among suppliers in their subsequent dealings with government.

- o Funding payment of arrears: The State Government shall clear her arrears using funds from any of the following sources:
 - i. Statutory Allocation
 - ii. Internally Generated Revenue (IGR)
 - iii. Grants from the Federal Government, and
 - iv. Loans

If sufficient liquidity is not immediately available, governments shall negotiate a schedule of payments with creditors according to a pre-defined calendar and an agreed interest rate.

SECTION 3.

3.1 Establishing a Consolidated Internal Domestic Expenditure Arrears Database.

The Committee, through its Secretariat is to establish and maintain a comprehensive database of all the State's domestic arrears. The database should have the capacity and functionality to record all the categories of the arrears claims and balances into the following categories

- a. Valid;
- b. Contestable; and
- c. Rejected

3.2 Features and Functionalities of the Consolidated Internal Domestic Expenditure Arrears Database.

1. The aggregate and individual amounts of contractors' arrears, categorized as valid, contestable and rejected.

For Contractors' arrears, at a minimum, the internal domestic arrears database must include:

- a. The name of the Contractor;
 - b. The amount due at the end-of-year;
 - c. The nature of goods and services procured that generated the claim;
 - d. Billing data (as applicable).
2. The aggregate amount of pension and gratuity arrears, categorized as valid, contestable and rejected.
 3. The aggregate amount of salary arrears and other staff claims, categorized as valid, contestable and rejected. The aggregate amount of each of the other types of arrears, categorized as valid, contestable and rejected.

3.3 Recommended Process for Establishing the Database.

The following process is recommended to be followed for establishing a database:

1. Designate a unit at the Domestic Arrears Committee secretariat and specific staff for collecting arrears data maintaining the information and updating the database.
2. The data can be held on excel spreadsheets or in a specialized database software. Note, that the proposed database is software/software agnostic and can be created using spreadsheets as its most basic.
3. There should be a clear definition of arrears, data requirements and a monthly cut-off data for inclusion of new arrears. These will require circulars/instructions/guidelines and templates for the institutions and entities that are to provide the arrears data

3.4 Establishment of Domestic Arrears Database

1. Cash or accrual accounting systems will need accurate reporting of accounts payable and be able to identify those in arrears. Cash accounting systems may need to be supplemented with a separate reporting mechanism for monitoring expenditure commitments, invoices received and verified, accounts payable, invoices paid, and arrears.
2. The arrears data should be certified by the Head of Finance of the respective MDAs or institutions who are the primary record holders as a true and complete account of all arrears and include all necessary documents/information for validation and verification.
3. There should be sanctions for non-reporting or late reporting of arrears

To allow for appropriate categorization, the following data shall be captured for each outstanding claim:

- Age of Debts: The database will capture the original due date on each invoice, and arrears shall be classified according to how long they have been overdue such as:
 - ✓ One to three months,
 - ✓ Three to six months,
 - ✓ Six to 12 months, and
 - ✓ More than 12 months.

Older arrears should be classified by the financial year in which they were incurred. If the due date is not recorded in the invoice, the invoice date can be used as a proxy for the due date.

- Debtor: The database shall capture the government entity incurring the liability, classified by institutional group (The State government, Local government, MDAs, extra-budgetary fund, or State-Owned enterprise).
- Creditor: The database will capture the creditor's name classified by type:
 - Employees,

- Private individuals,
 - Private businesses,
 - Financial institutions,
 - The State government,
 - Local government,
 - Extra-budgetary funds, or
 - State-Owned enterprise.
- Economic category: The database shall classify arrears into economic categories, such as compensation of employees, acquisition of goods and services, transfers, acquisition of nonfinancial assets, and acquisition of financial assets.
 - Currency: The database shall capture the currency in which the obligation was originally denominated so that cash Managers can ensure that sufficient foreign exchange is available to meet external arrears.
 - The age of the payable shall be checked by reference to the invoice and other supporting documentation. A confirmation from the supplier will be obtained in contentious cases.
 - The Ministry of Finance, taking full account of the legal framework with respect to disclosure of taxpayer records, will undertake checks with the revenue authority to ensure that suppliers are registered taxpayers and determine whether they are delinquent in tax payments.

3.5 Establishing a Publicly Accessible Arrears Database

In order to achieve this, the State is to publish online, elements of the internal domestic arrears database on the State's official website. This will constitute the online publicly accessible arrears database.

Furthermore, the website shall provide State contractors who are owed above twenty million naira (N20 million) the opportunity to

confirm that their debts are included within the database. The publicly accessible arrears database published online shall include the following information about domestic expenditure arrears categorized as valid in the internal domestic arrears database:

- a. The amount of total domestic expenditure arrears;
- b. The aggregate amount of contractors' arrears;
- c. The aggregate amount of pension and gratuity arrears;
- d. The aggregate amount of salary arrears and other staff claims; and
- e. A list of individual contractors with recognized arrears of twenty million naira (N20 million) or more in the database. For each of these contractors, the name of the contractor, the nature of the goods and services procured, and the billing date shall be provided. The amount of the contractor's claim and other billing data may be provided.

to request a restricted disclosure of the information not reported on the online database namely; the amount of the contractor's claim and other billing data by filling a confidential form online and attaching supporting evidence of the claim.

- If the State's Ministry of Finance confirms the validity of this claim, the restricted disclosure will be provided to the creditor.
- If the creditor believes the amount recorded in the database is incorrect, they can request the State's Ministry of Finance to review and provide supporting evidence.
- If the State's Ministry of Finance confirms the validity of this further claim, the correction will be made to the internal and online version of the database.
- If the State's Ministry of Finance confirms the validity of this claim, it shall be added to the internal domestic arrears

database and included as relevant in the online publicly accessible arrears database.

SECTION 4: ORGANISATION AND INSTITUTIONAL ARRANGEMENT

4.1 INSTITUTIONAL ARRANGEMENT FOR IMPLEMENTATION OF THE FRAMEWORK.

Rivers State is a participant in the Federal Government of Nigeria (FGN) and World Bank multi-year (2018-2022) States Fiscal Transparency Accountability and Sustainability (SFTAS) Program to support Nigerian States to strengthen fiscal performance and sustainability. One of the disbursement-linked indicators under the Program (DLI #8) requires States to establish a database of verified domestic arrears, establish an arrears clearance framework (ACF) setting out the procedures to clear the stock of arrears, and implement the ACF.

Consequently, the Rivers State Government has put in place a Domestic Arrear Clearance Committee as institutional arrangement charged with the overall arrears clearance process, including recording, verification, classification, reporting, prioritization and clearance of government domestic expenditure arrears in the State and to oversee the work of the State towards achieving the SFTAS DLI #8. It is understood that any state that reduces its stock of arrears at the end of the year by at least five percent (5%), compared to the previous year, will be eligible for an annual performance-based grant.

The Arrears Clearance Committee shall oversee arrears liquidation to ensure the consistent application of the principles of the framework. The Committee would ensure that payments are made in accordance with the agreed prioritization criteria. The Committee would receive reports from spending units and prepare periodic reports to the Ministry of Finance and Governor's Office on the performance of MDAs on payment of arrears. The report should highlight any non reporting spending units and recommend remedial actions.

4.2 OBJECTIVE AND RESPONSIBILITIES OF THE COMMITTEE

The Committee will support the Ministry of Finance and Office of the Accountant-General in its responsibility for accurate recording, verification and reporting of domestic arrears balances across all types of arrears. The specific duties of the Committee shall include, but not limited to the following:

- Introduction of specific guidelines setting out the roles and responsibility of individuals and institutions for the recording, verification of domestic arrears on agreed recording templates,
- The creation, maintenance and regular (monthly) update of an accurate internal domestic expenditure arrears database and the publicly accessible online version of the database,
- Oversight of the overall recording, verification and reporting process for domestic expenditure arrears to ensure that they meet the requirements for SFTAS DLI-#8 as described in the SFTAS verification protocols,
- Ensure adequate classification of the arrears for prioritization purposes,
- Develop the State's Arrears Clearance Framework (ACF), including policies on prioritization and clearance of arrears
- Provide accurate monthly, quarterly and annually reports that present the true position for verified domestic arrears and the progress made in implementing the State's ACF
- Provide data/documentation to support the verification of SFTAS DLI #8, including the State Arrears Recording, Verification and Clearance Report.

4.3 SPECIFIC ACTIVITIES

The specific activities for the committee include but are not limited to the following:

- Adoption and implementation of records management guidelines for domestic arrears.
- Adoption and implementation of verification guidelines for all types of domestic arrears.
- Establishment of a consolidated internal domestic arrears database.
- Establishment of a publicly-assessable online version of the database.

- Reporting of valid and verified domestic arrears to end-users.
- Development of the ACF.
- Produce the State Arrears Recording, Verification and Clearance Report.

4.4 SUPERVISION AND REPORTING ARRANGEMENTS

The Committee will report directly to the State Governor through the Honourable Commissioner for Finance, keeping the appointed SFTAS focal persons informed.

4.5 MEMBERSHIP OF THE COMMITTEE

The membership of the Committee will include the following officials of the Rivers State Government;

i.	Commissioner of Finance	<i>Chairman</i>
ii.	State Accountant-General	<i>Alternative Chair</i>
iii.	Auditor General (State)	<i>Member</i>
iv.	Permanent Secretary Ministry of Budget	<i>Member</i>
v.	Director-General-(BoPP)	<i>Member</i>
vi.	Director General (Pension Board)	<i>Member</i>
vii.	Director-DMO (Min of Finance)	<i>Member</i>
viii.	The State SFTAS Focal Officer (PforR)	<i>Member</i>

4.6 COMMITTEE SECRETARIAT

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

4.7 POWERS AND AUTHORITIES OF THE COMMITTEE

The Committee shall have delegated authority to request any and every information it requires in order to carry out its functions from the MDAs. The Committee will be able to incur expenditures, including the engagement of professional assistance in the course of executing its role. All expenditures must be incurred through the procurement systems of the selected institution.

4.8 TENURE OF THE COMMITTEE:

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

Signed



Isaac Kamalu, Esq.
(Hon Commissioner of Finance)



Sir Abere R Dagogo
(Accountant General)

