Fiscal Federalism in Nigeria: Implication to the Economy of States

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***Abstract*:-The paper discusses fiscal federalism in Nigeria, and the implication to the economy of states. Federalism, fiscal federalism and inter-governmental relations were defined in the conceptual framework, while basic theories of fiscal federalism were reviewed. The empirical issues/opinions of experts on fiscal federalism concluded the literature review. The paper reviewed the evolution of fiscal federalism in Nigeria; Sir S. Philipson headed the first fiscal commission preparatory to the 1954 federal constitution. Other commissions/instruments of fiscal federalism include, the Hicks-Philipson, Louis Chick, Jeremy Raisman and R.C. Tress, the Bin, Decree 15 of 1967, the Dina Commission, the Aboyade committee, Pius Okigbo, T.Y. Danjuma Commission and the Constitution of the Federal Republic of Nigeria, 1999. The paper discovered that the Nigerian fiscal imbalance was to a large extent masterminded by the military governments. That the states in Nigeria are structurally constrained to perform their constitutional responsibilities because of appropriation of greater quantity of the national resources to the purview of the government at the centre. Taxes and Royalties that were hitherto paid to states have been directed to the federal purse. The Exclusive and Concurrent lists, in favour of the government at the centre negate the economic prosperity of states in Nigeria. It is important that the Exclusive and the Concurrent lists as contained in the 1999 Constitution be reviewed. States must be made to own and exploit resources in its territory to carryout their statutory responsibilities. The federal government should refund states that have repaired federal roads, and projects. While in the near future the federal government should hand-off certain responsibilities, such as Roads, Education, Agriculture, Sanitation, etc. The distributable funds for these projects should go to the states treasury. The restructure of the Nigerian federal system will strengthen the economy of states, and pave way for more equitable society and welfare of citizens.**

***Keywords:* Fiscal Federalism, Federalism, Revenue Allocation, Inter-governmental Relations**

I. INTRODUCTION

Federalism is a political concept in which power to govern is shared between National and Sub-national governments, creating what is often referred to as federation. In a federal arrangement, each tier of government is co-ordinate and independent in its limited sphere of authority and should also have appropriate taxing powers to exploit its independent sources of revenue. Federalism therefore entails a series of legal and administrative relationship created among different tiers and units of government having varying degrees of real and jurisdictional autonomy (Anyanwu, 1997).

Fiscal federalism is a by-product of federalism. According to Wheare (1963), the basic elements of fiscal federalism include; division of powers among the tiers of government, and co-ordinate supremacy of the different levels of government with regards to their respective jurisdictions. Igbuzor and Bamdele (2002) submitted that fiscal federalism is the division of resources among the tiers of government in a federal system. Nigeria operates a federal system where there is constitutional division of powers, functions and resources among the three levels of government. Consequently, Ekpo (1999) described fiscal federalism as essentially about the allocation of government resources and spending/expenditure to the various tiers of government.

Agiobenebo (1999) encapsulate the concept of fiscal federalism as:

> *The political decentralisation of socio-economic responsibilities and functions giving rise to a number of interesting relational and fiscal issues. Decentralised system of government give rise to a set of fiscal exigencies referred to as fiscal federalism.*

These fiscal exigencies the author refers to as governmental responsibilities and functions, and the allocation of resources among the tiers of government.

The critical role of an efficient fiscal guidelines, laws and policies to drive the process of development was emphasized by Ekpo and Ndebbio (1996). They reiterated that:

> Fiscal operations at the local government level become significant if macroeconomic stability is necessary in the wider economy. If fiscal imbalance appears rampant at the local level, it could pose problems for macroeconomic management of the economy.

Three major principles guide the intergovernmental fiscal relations in a federation. First is the fiscal relation which consists of the functions expected to be performed by each level of government in the fiscal allocation, the jurisdictional cooperation, this refers to areas of shared responsibility by the National, State and local governments and lastly, the principle of jurisdictional community.

In Nigeria, these principles are enshrined in the 1999 Constitution as Amended, in the Exclusive, Concurrent and Residual lists. This classification assigns duties such as railway, electricity, defence to federal government, while education, transport, agriculture are placed under the concurrent list. Responsibility for functions whose benefits accrue to a limited geographical area such as, markets, primary education, motor parks, cemeteries, etc are exclusively the responsibility of the local government.

The question however is, whether the various revenue allocation formulas, financial guidelines have arrogated to the tiers of government corresponding revenue based on ability to carryout their statutory assignment? The answer is no, different formula that have been adopted for revenue allocation have consistently increased the financial base of the federal government against the states. The consequence is that the state governments are not able to meet-up with their statutory duties, except it goes cap-in-hand begging from the federal government. This has gradually eroded the fiscal autonomy of the federating units. From income tax to value added tax, rent from petroleum and solid minerals, the states in Nigeria have been short-change by the federal government in revenue allocation from the National resources.

Further discussions will be limited to four sections. Section two is the literature review, section three are regimes of fiscal federalism in Nigeria. Section four is the implication of fiscal imbalance to the economy of states, and the conclusion in the last section.

II. LITERATURE REVIEW

Conceptual Framework

Federalism

Federalism refers to a system where each tier of government is co-ordinate and independent in its delimited sphere of authority and also have appropriate taxing powers to exploit its independent resources (Vincent, 2001). Some writers believed that each level of government should have adequate resources to perform its function without appealing to the other level of government for financial assistance. Wheare (1963) emphatically argued that:

> If state authorities, for example, find that the services allotted them are too expensive for them to perform, and if they call upon the federal authority for grants and subsidies to assist them, they are no longer coordinate with the federal government but subordinate to it. Financial subordination makes an end of federalism in fact, no matter how carefully/the legal forms may be preserved. It follows therefore that both state and federal authorities in a federation must be given the power in the constitution each to have access to and control its own sufficient financial resources. Each must have the power to borrow for the financing of its own services by itself.

The rights of both the federal and the state governments in a federal structure are enshrined in the constitution. Modern federations have sub-levels of government each distinguished by the scope of the geographical areas over which their respective jurisdictions extend. The jurisdiction of the federal (central) government covers the entire country in some subject-matters. Other (state/province and local/municipal) government's jurisdictions cover sub-sections of the country. Local governments exercise responsibility over non over-lapping areas within a state. Federalism is a standard concept of government based on multilevel area/jurisdiction to cater for racial, religious, linguistic and other differences (Oates, 2009). Ideally a system of multi-level government should be structured from the point of view of ensuring an efficient supply of public services.

Fiscal Federalism

Fiscal federalism is a by-product of federalism. Federalism is a political concept in which power to govern is shared between national, and subnational governments creating what is often called .a federation (Akindele and Olaopa, 2012). It is a political theory that is divergent in concept, varied in ecology and dynamic in practice. The concept of federalism implies that each tier of government is coordinate and independent in its delimited sphere of authority and should also have appropriate taxing powers to exploit its independent sources of revenue. Fiscal federalism demands that each level of government should have adequate resources to perform its functions without appealing to the other level of government for financial assistance. According to Wheare (1963),

> Both state and federal authorities in a federation must be given the power in the constitution each to have access to and to control, its own sufficient financial resources. Each must have a power to tax and to borrow for the financing of its own services by itself.

For any federation to be sustained there must be fiscal decentralization and financial autonomy. Fiscal decentralization means delegating decision-making to lower levels of government instead of concentrating it at the centre. Each level of government, therefore, should be free to take decisions and allocate resources according to its own priorities in its own area of jurisdiction. In addition, the federating units should be able to act independently on matters within their own jurisdiction.

Fiscal federalism connote set of guiding principles or concept that helps in designing financial relations between the national and subnational levels of government, while fiscal

decentralisation is the process of applying such principles. The fiscal relationships among the components of the federation explained the functions expected to be performed by each level of government in the fiscal allocation, interjurisdictional cooperation, that is the shared responsibility by the national, state and local governments, and the multijurisdictional community (Tella, 2009). In this case, each jurisdiction (state, region or zone) will provide services whose benefits will accrue to people within its boundaries, and so, should use only such sources of finance as will internalize the costs.

Inter-Governmental Relations

Dike and Iwuamadi (2005) describe Inter-governmental Fiscal Relations as:

> The measures for statutory revenue allocation between the Federal Government and the associated' tiers, the strategies of revenue mobilization, approval, controls and cc-ordination of financial policies, assistance in aids and investigations in manner of disbursement or administration of funds appropriated to the layers of government

The 1999 Constitution of the Federal Republic of Nigeria confine the fiscal relationship between the three tiers of government in the Exclusive, Concurrent and Residual Legislative lists.

The economic rationale for inter-governmental transfers arises from well known deficiencies of most modern fiscal systems such as: Fiscal imbalances of various kinds, that is, vertical and horizontal imbalances, benefit spill out/spill over, local services as central merit goods or minimum standards.

Theoretical Framework

Based on welfare economics, Musgrave and Musgrave (1989) assert that governments exist to correct the failures of the free market in the efficient allocation of resources, equitable distribution of income, and economic stability and growth. That government has three major functions to perform - allocation, distribution and stabilization. These roles are performed with the presumption that they would improve or maximize social welfare.

The institutional framework, on the other hand, is essentially about the structure of government. The structure can be conceptualized in a two-dimensional sense, namely, the arrangements between and within levels of government. Such arrangements are defined to include not only the decision- making units, but also the decision-making processes, practices and interrelationships.

Federalism is essentially about government structure in the multilevel sense, rather than within a particular level of government, in the performance of government functions. There are different forms of federalism. The prominent ones are fiscal, political and administrative. Fiscal federalism is essentially about the allocation pf government spending and resources to the various tiers of government (Oates 1972, Janzi 1995). In contrast, political federalism deals with the division of powers between tiers of government, where the tiers are each, within a sphere, coordinate and independent. It follows, therefore, that there would be constitutional or some other legal provisions to protect the autonomy of the different tiers of government. Administrative federalism, on the other hand, involves delegation of functions to lower-level governments, usually according to the guidelines or controls imposed by the higher-level government and, therefore, without the autonomy which is characteristic of decentralization.

Of the different forms of federalism, the one of relevance in this paper is fiscal federalism. This type explains division of fiscal responsibilities between the different tiers of government, the optimum size and number of subnational governments, and tax and revenue sharing arrangements.

Federalism denotes a partial decentralization of government. It is a case of more than one level of government. The question then is: why is it desirable to have more than one level of government as is the case in Australia, Nigeria and the USA? The argument is relatively straightforward. Some economic functions are best performed by the central government and others by subnational governments. There are also a number of practical advantages that accrue from decentralization. A substantial part of the argument is based on the theory of public goods and public choice theories of the political process.

The government has three major economic functions to perform, namely, allocation, distribution and stabilization. Allocation function is predicated on the assumption that there is a well-defined set of publicly provided goods. The publicly provided goods are of three major types depending on the degree to which the free market system fails in their provision. These are private goods, impure public goods and pure public goods. Private goods are those whose consumption is both enjoyed individually and made contingent upon payment, e.g., electricity, water and milk. Impure public goods are those whose consumption is both collective and made contingent upon payment, e.g., highways with toll imposed. Finally, pure public goods are those whose consumption is collective but not contingent upon payment, e.g., fresh air.

The free market system tends to break down completely in the case of pure public goods, partially in the case of impure public goods, and probably partially in the case of private goods (Musgrave and Musgrave 1989). The argument for federalism based on the allocation function is usually illustrated with pure public goods as such goods constitute the limiting case of market failure.

We have national public goods whose spatial incidence covers the entire nation, e.g., defence, international

affairs, space exploration and the benefits of research and development. Second, there are local public goods whose spatial incidence is limited to particular geographic areas, e.g., regional transportation systems, street lighting and local fire engines.

Its been argued that the central government would be in a better position to perform the distribution and stabilization functions as well as provide national public goods (Musgrave and Musgrave 1989). All of these functions will be inefficiently performed at the local government level for two interrelated reasons - difficulty in appropriating the full social benefits of the programmes undertaken at that level, and the tendency towards the free rider, problem. The local government tends to take into consideration only its own marginal costs and benefits when deciding on its level of provision, and ignore the benefits conferred on other local governments. Consequently, the locality, insofar as it confers benefits on other localities, will tend to operate at a level which is lower than the nationally desired level. This problem is unlikely to arise if the decision is taken by the central government, as all the associated costs and benefits would be intema1ized and national marginal costs and benefits taken into consideration. But the local governments understand the basic needs of their people, ways of reaching the poor as well as the culture, linguistic and tribal differences among the population. Considering all these variables, the component governments are considered in a better position to perform the distribution and stabilisation functions and this inform the evolution of federal system of government.

Empirical Issues

Wheare (1963), one of the earliest authorities on federalism, defines the concept as ‘the method of dividing powers so that the central and regional governments are each, within a sphere, co-ordinate and independent. Different forms of federalism exist. Distinction is based on the scope of the geographical areas over which different levels of government have jurisdiction. In most federation, the central government has a jurisdiction which covers defence, currency and central banking, citizenship, etc. Regional/state/provincial governments exercise powers over non-overlapping subsections of the country in such matters as law and order, social services, commerce and local governments, among other things. Local governments have authorities over non-overlapping areas within a state or province such as control of pets, tenement rating, primary education dispensaries, orphanages, markets, motor parks and so on.

It makes economic sense to assign the provision of pure public goods, such as defence, to a single unit of government with jurisdiction over the entire country. This is because the service does not taper off with area covered and additional persons can be supplied at no extra cost. Per capita cost of such goods is reduced to the barest minimum when it is supplied by the central government. In other words, the central government provision of pure public goods enables a country to reap fully the benefits of economies of scale.

In the provision of semi-public goods, there is a justification for the involvement of state and local governments. Semi-public goods are supplied to only a limited area at any given time at minimal cost. A high quality of services can be supplied to additional households and over a wider area up to a given limit without extra cost. Beyond this limited area, the benefits taper off suddenly to zero. In such a case the semi public goods must be provided by a number of state governments.

Where a certain level of government is responsible for the provision of pure public goods, which have the characteristics of joint supply and non-exclusion, and another level of government is responsible for semi-public goods, some degree of decentralization is required. There are other services such as primary education, registration of births and deaths and marriages that are local public goods requiring a relatively very large number of local governments to provide. Further fiscal decentralization is required; this is the case of Nigeria political federation.

The extent to which fiscal powers should be assigned to state or local governments is a function of the possible advantages to be realized in terms of the citizens’ preference which may be quite important in a diverse and heterogeneous country. In this case, the objective of having a decentralized fiscal system is to satisfy the differing preferences of different states and localities. Where preferences are homogeneous in a country, the state governments may simply be asked to administer the decisions of the central government.

Issues in fiscal federalism arise, mainly from the federal set-up of the country and the zero-sum of sharing a given amount of resources. The problems boil down to what formula to use in sharing resources to ensure an optimization of the various interests, while maintaining a high rate of economic growth. Two of the most important yardsticks by which revenue allocation are evaluated are equity and efficiency. By equity, we mean the normative concept of fairness while efficiency refers to the extent to which revenue allocation distorts efficient economic decision-making. Because equity is a normative concept, the answer to the question of what is a fair revenue allocation formula is bound to be answered differently by different people.

Fiscal federalism may be viewed as a set of fiscal activities, relations and interactions, rights and demands by and among the various governments in a federation. The constitution defines the rights to revenue among governmental units. Revenue allocation then requires defining the functions and sources of revenue of each level of government. Usually, the roles, responsibilities and rights of each government are constitutionally determined and the fiscal arrangements follow automatically. It has been difficult, however, to match responsibilities with resources at every level of government. Continuous adjustments are being made to the revenue

allocation formula in order to meet the changing economic and political circumstances. Revenue allocation is a mechanism used to address the fiscal imbalances which emerge in the process of economic development.

It should be noted also that efficiency is the basis for the tax jurisdiction and assignment of responsibilities. Where the distribution of functions does not rest on and, in fact, does not guarantee an adequate and independent revenue base, then the canon of fiscal federalism is bastardized and is in jeopardy. Ideally, therefore, tax jurisdiction should guarantee the fiscal autonomy of each level of government (Phillips 1975). However, efficiency requires that the taxing powers be vested in that level of government most likely to administer the taxes at the least cost. For this reason, taxing powers on sources which cut across states and which are major sources of revenue are vested in the central government, while those sources that cut across local government boundaries within a state are vested in the state government.

There are few generally acceptable variables, factors and weights for distributing revenues among the states. There is a disagreement between those who favour equalization principles, which promote balanced development of the federation, and those who favour derivation principle, which is not only one of the pillars of fiscal federalism but a source of lopsided development. Fiscal relations in a federal system require resolving these conflicting issues. Federal system demands more than economic efficiency in the allocation of resources. The primary goal of federalism is to sustain political stability and contentment of the component units of the federation. Against the argument that federalism inhibit economies of scale in public administration, he emphasizes that it should be noted that economies of scale are not infinite but subject to the law of diminishing returns. It could, in fact, be said that federalism is a political device of spreading the risk involved in governance, especially in large and heterogenous countries, (i.e., in multiethnic, multicultural, multilingual and multireligious countries with each group wanting to preserve its identity). Since a high degree of political autonomy is essential for the preservation of group identity, federalism is justified beyond what pure economic considerations may support.

Ugwu (2002) argues that economic growth would be accelerated by the devolution, rather than the concentration, of governmental powers. For the system to work well, there must be adequate institutions that would coordinate the various socio-economic policies of the different levels of government. The component units must also be willing to cooperate in the task of harmonizing government policies. Therefore, the goal of federalism is to reduce, prevent and manage ethnic conflicts by granting the respective state and local governments maximum financial autonomy.

Fiscal federalism, under which provision of public goods is decentralized to subnational governments, allows public-good levels to be tailored to suit the preferences of a non homogenous population. This is achieved via sorting of individuals into demand-homogeneous jurisdictions, each of which provides a different amount of public good. The drawbacks of federalism include the sacrifice of scale economies due to smaller jurisdictive sizes, losses from interjurisdictional tax competition when government revenue comes from taxation of a mobile tax base, and failure to properly account for public-good spil1oves across jurisdictions (Barro, 2006).

III. FISCAL FEDERALISM IN NIGERIA

The evolution of fiscal federalism in Nigeria is been tortuous, taking several constitutions, commissions, Acts and Decrees from 1948 to 1999 Constitution of Federal Republic of Nigeria. The journey to strike a fiscal balance in Nigeria federation is reviewed as follows:

The Phillipson Commission 1948/49

The Richard's Constitution was the first constitution to provide fiscal responsibilities to the regional governments. Funds have to be made available for the regions to meet their expenditure requirements. The first fiscal commission was inaugurated and given mandate to comprehensively examine the issues of revenue allocation system to be adopted. Sir Sydney Phillipson was appointed in June 1946 to handle that assignment. The Commission was to determine the criteria for declaring and determining, which is regional revenue, the magnitude of grants from the centrally collected revenue and the guiding principles for allocation of such grants to the regions.

The Commission recommended that for revenue to be declared regional it must be obtained from the region and should be collected by the regional authorities. It was essential that the revenue must not have any significant national policy entanglements. These receipts include, licenses, fees of courts, mining rents, rents from government property, earnings of government departments and miscellaneous sources of revenue.

Two principles were used to deal with the issues of revenue allocation to the regions. The first was Derivation while the second was Even Progression. The principle of Derivation suggests that the receipts from some taxes should be shared among the regions in proportion to the contribution made to the total revenue by each of the regions.

The principle of Even Progression derives from the need to maintain unity in the country. It combined the element of needs and national interest. The thrust of this principle was to balance development with an underlying assumption that even-paced progress would promote stability and unity. It was the view of the Phillipson Commission that revenue allocation formula should be such that every level of regional services were maintained, while adequate allowance was made for future planning. Although these conflicting principles proposed in the allocation of revenue in practice, Derivation

was the only criterion used in allocating revenue to the regions in the 1948/49 and 1951/52 fiscal years.

The Hicks-Phillipson Commission, 1952/53

The Commission was to determine the division of fiscal powers and jurisdiction between the regional and central governments. The principle of independent revenue was evolved by the regions for the first time. In this case the regional governments now had full control over revenues which were declared regional. These included general tax, jangali, produce sales tax, license fees, and rents from government property.

Under this principle, regional governments have the powers to impose these taxes and the rights to revenue generated from them. The central government collected and retained export and import duties other than those on tobacco and spirit and 54% of import and excise taxes on tobacco. There were those areas whose powers were excisable by the Central authority, but the revenue obtained were assigned wholly or partly to the regional authorities. For example, 100% of net earnings from import duty on motor fuel was assigned to the regions, while 50% of the earnings from import taxes and excise duties on tobacco went to the regions which was distributed in the following ratio: North 30%, West 40% and the East including the Southern Cameroons 30% (Louis, 1953).

The Hicks-Phillipson Commission recommended the principles of Derivation, Needs, and National Interest. Taking into account the principle of national interest, grants were given to the regions by the central authority or government to cover the full cost of Regional Police Force. The central government bore 50% of the cost of running the Native Authority Police forces. It also funded 100% of education requirements. Under the present arrangement, the Western Region benefited most. The' principle of Derivation from import duties on motor spirit and Needs which translated into education grants gave the West monumental benefits over the North and East. With respect to the principle of Needs, which was charged to capital grant, the North was most favoured. The North received over N4m annually in the fiscal years 1952/53 and 1953/54, while the East benefited greatly from educational grants, that is, the principle of National interest.

The use of Derivation, Needs and National Interest in horizontal revenue allocation formula intensified inter-regional conflicts and frictions. This is because, while the North preferred the use of Needs, the West favoured Derivation, while the East was favourably disposed towards National Interest as major criteria for sharing or allocating revenue to the regions.

Following the Conference on the Nigerian Constitution held in London in July and August 1953, the 1951 Constitution came under review. The new arrangement envisaged the devolution of more powers and autonomy to the regions. Louis Chick was appointed to work out a new fiscal arrangement under the new Constitution.

The Louis Chick Commission 1954/55

Chick was asked to review the existing fiscal arrangement with a view to relocating functions between the central and regional governments. The Chick's Commission was to focus on the horizontal revenue sharing arrangements to ensure that' the principle of derivation is followed to the fullest. Two principles were generally identified in the Chick's Commission. They were Derivation and Fiscal Autonomy. Those revenues that were declared, regional by the Hicks-Phillipson Commission were not altered.

It recommended that 50% of the net proceeds of import duties on all other commodities other than motor spirit and tobacco should be distributed in the following ratio: North 30%; West 40%; East, including Southern Cameroons, 30%. This recommendation was based on the attempt by government to increase the revenue going to the regions. The West being the richest in the regions benefited most from the principle of Derivation.

The uneven regional progress experienced by the emphasis placed on Derivation caused inter-regional friction and political rivalry. The North and East openly canvassed that the Derivation principle should be dc-emphasized.

Jeremy Raisman and R.C. Tress Commission 1959/60

Following the tension generated by the Chick's Commission recommendations, Jeremy Raisman and R.C. Tress were appointed by the Secretary of State for the colonies to review the revenue allocation system in 1959. The Commission's report published in 1958, recommended that the central government should continue to exercise fiscal powers over customs, sales taxes, mining rents and royalties. To broaden the financial base of the regions, the Commission further recommended the retention of revenue from regional income tax, sales tax on hides and skins and taxes on property. The Regions could also obtain revenue from taxes levied by the central government. They were export duties, taxes on motor fuel and custom and excise duties on tobacco.

To dc-emphasize the principle of Derivation, the Distributable Pool Account was established and 30% of revenue collected from general customs, taxes, mining rents and royalties were paid in the following proportions: North 40%, East 3 1% and West 24%. The distribution pattern in this case largely reflected the principle of Needs and National Interest. The Raisman- Tress proposals were accepted with minor modifications. Thus the report formed the fulcrum of revenue allocation between 1959/60 and 1964/65.

Two issues stood out during the Raisman-Tress era. First, the statutory allocation to the regions increased from N62m to N84m between 1958 and 1960. The increase in the Distributable Pool Account was attributed to the growth of the petroleum industry and the huge revenue collected from

import tariffs. Second, was the rapid decline on the share allocation to the West. It fell from 40% in 1954/55 to 24% in 1959/60. The East stood in between the North and the West. The collapse of the prices of cocoa in the World market partly explained this decline.

The recommendation of the Rasman-Tress Commission surreptitiously laid the foundation for the denial of communities of the control of the benefits of minerals in their areas. Note the recommendations were made in 1956 about the same time oil was discovered in commercial quantity in the country (Oloibiri, Bayelsa State) to be precise. The Commission felt that oil development in the Eastern region would take place in large scale and that would upset the balance of national development. This has remained the thinking of the majority tribes up till this moment. The post-independence 1963 Constitution still left regions with some high level measure of fiscal autonomy, but clearly gave the centre financial advantage.

There were agitations by some regions in 1964 over the revenue sharing formula, especially on the issue of derivation. The agitations necessitated the inclusion of such principles as land mass and population in subsequent revenue sharing formula.

The Bin commission, 1964

The Bin Commission, while recognizing the demand for inclusion of population and landmass, observed that the overall environmental devastation and health hazards caused by petroleum exploration and exploitation demanded that the regions of origin should have nothing less than 50% of the revenue from oil. This recommendation was adopted and implemented until the adventure of the military into governance.

The Post Military Era

The evolution of fiscal federalism in the post military era covers from 1966 to 1999. We treat the post-military era separately because of the neglect each succeeding administration paid to the principle of derivation.

Decree 15 of 1967

The Military suspended the 1963 Republican Constitution by promulgating Decree 15 of 1967, which assumed control of national revenue. The regions were abolished. Nigeria at that point became a unitary state. Thereafter, the Federal Military Government proceeded to create 12 states to replace the regions.

Dina Commission, 1968

The new political structure (creation of states) required the determination of their functional responsibilities and fiscal powers. The Dina Commission looked into previous revenue allocation formulae and made recommendations for a federal system of government with adequate powers and resources to the states. The position did not meet the expectations of the military authorities, hence the report was rejected.

Decrees 13 of 1970 and 1971

By these Decrees, the Federal Military Government transferred major fiscal powers and resources to the central government. In order to execute the post-war target of the 3Rs (Reconciliation, Rehabilitation and Reconstruction), the General Gowon Administration assumed 100% rights over all offshore rents and royalties from oil by Decree No. 9 of 1971. By this time, oil has become the major revenue earner for the country and agricultural produce that earned Nigeria so much foreign exchange earlier was neglected.

The Abayode Committee, 1977

Professor Ojetunji Abayode was appointed to head a Technical Committee on revenue allocation in preparation for return to civilian rule in 1979. The Committee was given the responsibility to review inter-governmental tax jurisdiction and revenue allocation, having in mind the task of injecting greater efficiency in the working of fiscal federalism.

The Abayode Committee further recommended that 10% of the state receipts be added to the local government's allocation and the creation of the Joint Fiscal and Planning Commission for periodic revision of the fiscal system. The Military Government rejected the report of the Committee on grounds that it was too technical.

The Pius Okigbo Commission, 1979

The Federal Government appointed a 7 man Presidential Commission headed by Dr. Pius Okigbo on revenue allocation in 1979.

T.Y. Danjuma Fiscal Commission, 1988

The Babangida regime reviewed some aspects of the Political Bureau Report. It increased the allocation for local government to 15% and it rose to 20% under Decree 10 of 1991 and 23 of 1991.

The Danjuma Commission recommended the setting up of a permanent body member's revenue allocation, mobilization and fiscal commission to look into revenue allocation matters in future. Danjuma's recommendation may have informed the establishment of a permanent revenue allocation body, the National Revenue Mobilization, Allocation and Fiscal Commission (NRMAFC) in Sections 140 of the 1979 Constitution, 151 of the' 1989 and 153(1) of the 1999 Constitutions. The revenue allocation formula that is obtainable in the 1999 Constitution is that determined by the Revenue Mobilization, Allocation and Fiscal Commission (RMAFC).

The Constitution of the Federal Republic of Nigeria, 1999

The Third Schedule, Part 1, of the 1999 Constitution establishes the Revenue Mobilization, Allocation and Fiscal Commission as a permanent of body. Section 162(2) of the

1999 Constitution improves from section 149(2) of the 1979 Constitution which placed the distribution of public funds from the distributable pool solely on the National Assembly, which was saddled with a lot of responsibilities. The establishment of the Revenue Mobilization arid Fiscal Commission by the 1999 Constitution enables the body to pay full attention to the issue of revenue allocation which has been a thorny issue in the country.

The Constitution provides, in section 162 (2), the parameters for sharing revenue from the Federation Account thus:

> The President upon the receipt of advice from the Revenue Mobilization, Allocation and Fiscal Commission shall table before the National Assembly proposals for revenue allocation from the Federation Account and, in determining the formula, the National Assembly shall take into account the allocation principles, especially those of population, equality, of states, internal revenue as well as population density. Provided that the principles of derivation shall be constantly reflected in any approved formula as being not less than thirteen percent of the revenue accruing to the Federation Account directly from any national resources"
>
> Section 162 (3) also provides that:
>
> Any amount standing to the credit of the Federation Account shall be distributed among the Federal and State Governments and the Local Government Councils in each state on such terms and in such manner as may be prescribed by the National Assembly.

Subsections (5), (6), (7) and (8) of Section 162 of the 1909 Constitution make financial provision for the local government councils. Section 162 (6) provides that:

> Each State shall maintain a special account to be called "State Joint Local Government Account" into which shall be paid all allocations to the local government councils of the states from the Federation Account and from the Government of the State
>
> (7) Each State shall pay to local government in its area of jurisdiction such proportion of its total revenue on such terms and in such manner as may be prescribed by the National Assembly
>
> (8) The amount standing to the credit of local government councils of such a state shall be distributed among the local government councils of that state on such terms and in such manner as any be prescribed by the House of Assembly.

The Constitution further provides for a four-year review of the revenue allocation formula to remove distortions and imbalances in the system. Parts I and II of the Second Schedule of the Constitution contain the legislative powers of the Federal and State governments. The Exclusive Legislative List contains 68 items, whereas the Concurrent Legislative List contains 30 items. The Fourth Schedule of the 1999 Constitution contains the functions of the Local Government Councils, which in a way spelt out their legislative powers. Sections 4 (7) and 7 (1) (6) (b) of the 1999 Constitution give the State Houses of Assembly powers to make laws, including provisions for statutory allocation of public revenue to local government councils in the states. The issues dealt in the various fiscal regimes are summarised in Appendix.

IV. IMPACT OF FISCAL IMBALANCE TO THE ECONOMY OF STATES

Fiscal balance is one of the most keenly contested issues in Nigeria. A comprehensive review of the reports of the various commissions and constitutions from the 1946 Philipsons Commission to the activities of the National Revenue Mobilization, Allocation and Fiscal Commission established in 1989, the federal government controls all the major sources of revenue like import and excise duties, mining rents and royalties, petroleum sales tax, petroleum profit tax and companies income tax, among other revenues sources. Local government taxes are minimal and relatively inelastic. This limits their ability to raise independent revenue, hence their overdependence on allocations from the federation account.

Much of the revenue collected by the federal government and distributed among the different tiers of government using the vertical revenue allocation formula is from the federation account. But the federal government seems to exercise too much control over its distribution. Sales tax was an internal revenue source for the state governments before 1994 when it was renamed value added tax and put under the jurisdiction of the federal government for efficiency of collection and made payable to the federation account. Revenue collected as VAT has doubled in the decade, and is strictly under the control of the federal government.

Another item which the federal government has appropriated to itself is the revenue from petroleum price adjustments. In theory, revenue from taxes on domestic sales of crude oil should be paid into the federation account. This was not an important source of revenue until 1994 when the Petroleum (Special) Trust Fund (PTF) was created and managed by a board of trustees reporting directly to the Head of State. Revenue from substantial 1994 increase in the domestic prices of petroleum products and from new taxes on sale of crude oil went into the funding of the PTF instead of going into the federation account. In 1995, 1996 and 1997,

N35 billion, N42 billion and N38 billion accrued to the federal government alone through the petroleum price adjustment. Thus, while all the 774 local governments shared N32 billion, N36 billion and N42 billion in 1995, 1996 and 1997, PTF alone had no less oil revenue for each of those years to spend as it liked.

Similarly, the gains from the operations of the Autonomous Foreign Exchange Market (AFEM) which accrues exclusively to the federal government yielded N38, N62 and N47 billion in 1995, 1996 and 1997 respectively. This revenue which amounted to II, 15 and 10 per cent of total revenue in those respective years should have been paid into the federation account and distributed to all the tiers of government, as they all felt the negative effect of the devaluation of the naira. But this was not to be.

Also, in theory, all petroleum royalties and profit tax revenue from oil exports ought to be paid directly into the federation account. In practice, however, part of this revenue, were diverted to a federal government- controlled oil dedicated account for the execution of “priority projects”. According to the World Bank, about $12 billion may have been diverted into these accounts between 1988 and 1994 alone (World Bank Report 1996).

The stabilization account is yet another source of such extrabudgetary funds. The money kept in this account is set aside from the federation account. It was first set up by the Babangida regime in 1989 and later specified in the 1989 Constitution as a mandatory deduction from the federation account to be used whenever there is a shortfall in revenue earnings. Both the federal and state governments have access to this account but no formal procedure is given for withdrawals. So far, the local governments have had limited access to the stabilization account. However, whenever the state and local governments fail to draw their share of the accounts the federal government may borrow from the balance.

There are several other off-budget accounts that have been operated by the federal government. Some of these are the Oil Surplus Account opened at the beginning of the Gulf War in 1990. Another one is the special debt account intended for repaying part of the countries’ external debt. From the foregoing, we can see that the discretionary powers exercised by the federal government has caused public resources to be overconcentrated at the centre.

Currently, the federal government controls between 68 and 75 per cent of total public sector expenditure while the other two tiers accounted for the remaining 32-25 per cent (World Bank, 2012). All the local governments in the country had control over only 8 per cent of total public spending in 2005 and 6 per cent of same in 2010. At this same time, local government internal revenue only increased marginally from 5 to 8 per cent.

Given that about 70 per cent of Nigerians still live in the rural areas and local governments are the closest to the rural people, its share of total public sector expenditure is too small if the rural areas are to be transformed. Its responsibilities for economic planning and development, citizenship development and empowerment through primary, adult and vocational education and capacity enhancement through health care provision cannot be effectively executed, with just 6 per cent of total public sector spending. Thus, about 95 per cent -of the local governments do not have adequate funding. It is no surprise that most grassroots communities are so undeveloped that about 40 per cent of them do not have any sizeable community that can be called “developed”. This shows the absence of any concerted development effort in most of the local governments.

The despicable conditions of the local government in the state buttress the economic conditions of the states in Nigeria. Two-third of states in Nigeria cannot pay salary of workers, except it gets federal allocation, not to talk of providing social infrastructure. Good numbers of the states in Nigeria are thus poor and underdeveloped. Most of states have local resources that it can tap to increase internally generated revenue, but the current fiscal structure legally frustrate the efforts of the states. A good example is the Port Harcourt Seaport. It suppose to be a veritable source of revenue to the state, but the federal structure arrogated all sea ports to the federal government. Painfully, the federal government are not exploiting some of these resources; living the states economically idle and financially desolate.

V. CONCLUSION/RECOMMENDATION

From the review of fiscal regimes in Nigeria, it is clear that the states and local governments have been short changed in terms of revenue allocation. The states are also deprived of resources that could ordinarily have formed part of their internally generated revenue. As it is the states and local governments are not economically buoyant in Nigeria. Some states cannot pay salaries and fulfil its obligation, unless it obtains federal allocation. The situation has challenged the academic community and researchers on the need to review the current fiscal structure to allow the states to exploit resources and levy tax on areas the federal government have wrongly appropriated, and in some instance are not even exploiting.

It is only when the exclusive, current and residual lists as contained in the 1999 Constitution is practically adjusted to favour the states can the states be able to fulfil its core mandate of developing the rural areas of the state, by providing for education, sanitation, roads electricity, etc.

The current fiscal structure arrogate to the federal government, millions of kilometre of roads, stadium, monuments, which the states are maintaining on the ground that the federal government will refund the state. Today, Billions of Naira are owed states that have maintain federal

government project. These unpaid monies have impoverished the state governments.

Lastly, there is need to separate the office of the Accountant-General of the Federation from the Office of the Accountant-General of the Federal Government. In a federal system of government, the tiers of government are co-ordinate, no one tiers should be in charge of the finances of other tiers. These are some of the imperatives of the call for the restructuring of the Nigeria federation. No doubt, there are different forms of federalism, but political and financial decentralisation remains the core of a multi-layer political arrangement. Until there is proper financial decentralisation in the Nigeria federal system, the much needed development of infrastructure and manpower to drive social progress will continue to de-accelerate in a steady manner.

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APPENDIX: THE SYSTEM OF REVENUE ALLOCATION FROM 1947-1999

Year/Political System	Fiscal Commissioners	Recommendations	Accepted Principles
1947/48 Unitary system	Sir Sydney Phillipson and S.O. Adebo		a. Derivation b. Even progress
1952/53 Quasi-federal system	Prof. J.R. Hicks, Sir Sydney Phillipson and D. Skelton	Derivation, Needs, National Interest	a. Derivation b. Need c. National interest
1954/58 Federal system (3 regions, later Cameroon became a separate region)	Sir Louis Chick		a. Derivation b. Fiscal independence
1964/67 Federal system (4 regions, Cameroon inclusive & Mid-West)	Mr. H. Binns	a. Regional financial comparability b. Continuity of service c. Minimum responsibilities	a. Derivation b. Fiscal independence c. National interest East 30% North 42% Mid-West 8% West 20%
1968 Federal system	Chief O. Dina	a. Minimum national standard of basic needs b. Population c. Tax efforts d. Financial prudence e. Fiscal adequacy f. Balanced development g. Independent revenue h. Derivation i. National interest	a. Equality of States 50% b. Population 50% c. Derivation
1975/76	F.M.G.		a. Equality of states b. Population c. Derivation
1977	Prof. A.O. Aboyade	a. Equality of access to dev. Opportunities (25%) b. National minimum std. for national integration (22%) c. Absorbtive capacity (20%) d. Independent revenue and minimum tax effort (18%) e. Fiscal efficiency (15%) Federal 57% States joint A/c 30% Local government 10% Special grants A/c 30%	a. Equality of access to dev. Opportunities (25%) b. National minim std. for national integration (22%) c. Absorbtive capacity (20%) d. Independent revenue and minimum tax effort (18%) e. Fiscal efficiency (15%) Federal 60% States joint A/c 30% Local government 10% Special grants A/c 0%
1979	Dr. Pius Okigbo		Declared ultra vires by the Supreme Court
1981	Federal Government Revenue Act of 1981/82		Federal 53% States 35% Local government 10% Sharing of states' allocation minimum responsibility Equality of states Population Social development Internal revenue effort Derivation Ecology
1988/89	Gen. T.Y. Danjuma	Vertical allocation: Federal govt. 47% State govts. 30% Local govts. 15% Special funds 8% Special fund: FCT 1% Stabilization 0.5% Savings 2% Derivation 2% OMPADEC 1.5% Dev. Of non-oil 0.5% Gen. Ecology 0.5%	Vertical allocation: Federal govt. 50% State govts. 30% Local govts. 15% Special funds 5% Special fund: FCT 1% Stabilization 0.5% Savings - Derivation 1% OMPADEC 1.5% Dev. Of non-oil - Gen. Ecology 1%

		Horizontal allocation Equality of states 40% Population 30% Social dev. Factor 10% Land mass and terrain-Int. rev. effort 20%	Horizontal allocation Equality of states 40% Population 30% Social dev. Factor 10% Land mass and terrain-Int. rev. effort 20%
1999	F.M.G.		Fed. Govt. 48.5% State govts. 24% Local govts. 20% FCT 1% Gen. ecology 2% Stabilization 0.5% Derivation (MR) 1% OMPADEC 3%

Source: T.J. Agiobenebo in NES, 1999.