Fiscal Federalism and Challenges of National Development in Nigeria

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Abstract

In emerging and developmental state of Nigeria, the construct of federalism has continued to attract gamut of attentions due to its configuration and cosmetic nature. The Nigerian state since amalgamation of the 1914 and subsequent constitutional development that ushered in federalism, revenue allocations and transfers of resource control had become contending issues and debates that had propelled lingering questions on Nigerian federal practices. The witness is the persistent struggle for redrafting of revenue allocation parameters and quest for restructuring. The most worrisome is the power of government at the centre determining what constitutes revenue allocations and how it would be shared among the federating units. However, it is against this backdrop that the study appreciates the intergovernmental fiscal relations, institutions and measures aimed at controlling excesses and imbalances amongst the tiers of government in Nigeria. Methodologically, the study utilized documentary method and data were generated through the secondary sources and analyzed in content. The framework of analysis for the study was anchored on the power theory. The findings of the study had adequately revealed that components and federating units are engulfed with myriads of developmental challenges due to the nature and character of the fiscal and federal deficits. Therefore, the paper recommends the need for defined statutory role of each and culture of self reliant among the tiers of government.

Keywords: *Federalism, Fiscal arrangement, National Development, Nigeria, Revenue allocation*

Introduction

The history of post colonial Nigerian state is surrounded around state funding, revenue generation and allocation, in other words, fiscal federalism. Fiscal decentralization has become fashionable regardless of levels of development and civilization of societies. Nations are turning to devolution to improve the performance of their public sectors. Thus, ever increasing number of people desiring to get more involved in government, and the inability of the central government to deliver quality services have intensified the clamor for greater decentralization (Aigbokhan, 1999; Oates, 1972; Tanzi, 1995; Chete, 1998).

Fiscal federalism is essentially about the allocation of government resources and spending to the various tiers of government. Decentralized systems of governments give rise to a set of fiscal exigencies referred to as fiscal federalism also known as fiscal decentralization (Ewetan, 2012). It refers to the scope and structure of the tiers of governmental responsibilities and functions, and the allocation of resources among the tiers of government to cope with respective functions. The importance of revenue generation, allocation as well as its distribution towards maintaining both the existing and new socio-politico-economic structure in any economy be it centrally planned, market or mixed economies cannot be overemphasized.

Nigeria after fifty eight years of independence has been battling with the problems of development in spite of huge human material and natural resources at her disposal. Development could be seen as a critical factor and a desirable phenomenon in the substance and growth of any nation (Lawal and Oluwatoyin, 2011). However, development could be learnt from the lesson of the Asian Tigers and some other developing nations, is not a free gift. It is a product of careful design effective resource mobilization and collaborative action with the people and their leadership. Thus, it entails sacrifice and dedication coupled with careful observation and openness to change efforts (Akume, 2012).

Following the truism, Nigeria fiscal federalism has affected Nigeria fiscal development negatively. Indeed, there has been an endless search for a suitable and acceptable formula for fiscal federalism, based on the consent of the people that could facilitate development and growth. The stunted development could be explained on the basis of unhealthy fiscal decentralization that either antagonizes the tiers of government or make room for sustainable national development.

In short, there are complex dialectical processes to national development, however, the functions of government, and management and distribution of resources amongst them could not be underestimated. Thus, appropriate fiscal decentralization, conditions and processes will be observed. This study sets out to further expose and analyze the link between fiscal federalism and sustainable national development in Nigeria.

Conceptual Clarifications

Fiscal Federalism

Understanding federalism as a larger concept will help facilitate the understanding of the concept of fiscal federalism. This is because federalism is the operational context within which fiscal federalism is situated. Hence, it is an integral aspect of federalism. Federalism refers to a political system where there are at least two levels of government. In such cases, there is juxtaposition of two levels of power of a central government otherwise called the federal government and other states labeled variously as states, regions, republics, cantons or unions (Ajayi, 1997: 150).

Federalism is a system in which the power to govern is shared between national state governments, creating what is often called a federation (Akindele and Olaopa, 2002). Furthermore, Sagay (2008:11) conceptualized federalism as "an arrangement whereby powers within a multi-national country are shared between a federal government and component units in such a way that each unit, including the central authority exits as a government separately and independently from others, operating directly on persons and prosperities with its territorial area and with a will of its own apparatus for the conduct of affairs and with an authority in some matters exclusive of others".

Fiscal federalism is a general normative framework for the assignment of functions to the different levels of government and appropriate fiscal instruments for carrying out these functions (Arowolo, 2011). It is a set of guiding principles or concept that helps in designing financial relations between the national and sub national levels of government, while fiscal decentralization is the process of applying such principles (Sharma, 2003). Furthermore, to Ozo-Eson (2005), fiscal federalism concerns the division of public sector functions and finances among different tiers of government. In other words, it is the study of how competencies (expenditure) and fiscal instruments (revenue) are allocated among different (vertical) layers of the administration importantly, is the observation of the movement of revenue proceeds or payments from the central government to its lower levels of governments.

Fiscal federalism is characterized by fiscal relations between central and lower levels of government. The fiscal relationship between and among the constituent of the federation is explained in terms of three main theories namely, the theory of fiscal relations which concerns the functions expected to be performed by each level of government in the fiscal allocation; the theory of inter jurisdictional cooperation which refers to areas of shared responsibility by the national, state and local governments' and the theory of multijurisdictional community (Tella, 1999).

Hence, for the purpose of this study we define fiscal federalism as a set of guiding principles or concepts that, involves the transmission and cooperation's among the tiers of government in form of fiscal relations, inter jurisdictional cooperation and multijurisdictional relations.

Development

Development can be defined as an encompassing process involving the steady and systematic change in the cultural, economic and political spheres of society in a way that increases production, empower the people and their communities, protects the environment, strengthens institutions, grows quality of life and promotes good governance. This implies that is possible to speak of social, cultural, spiritual, institutions economic and political development. Gran (1983), defines development as a social and practical process which aims at the liberation of human potential so that people acquire the maximum socially feasible and practical control over all the available resources needed for the realization of basic human needs and security. Kortes (1990:57), "development could be defined from a people centered perspective as a process by which the members of a society increase their personal and institutional capacities to mobilize and manage resources to produce sustainable and justly distributed improvements in their quality of life consistent with their own aspirations".

Accordingly, Burkey (1993:35), sees development as "a process by which an individual develops self-respect, and becomes more self-confident, self- reliant, cooperative and tolerant to others through becoming aware of his/her shortcomings as well as his/her potential for positive changes". Furthermore, Todaro and Smith's (2006:17), opines that economic and social perspective, "development is a process meant for equitable social and economic transformation of the society through institutionalized social structures, and people's positive attitudes for an accelerated and increased growth and poverty eradication". Thus, development here is preserved as a multidimensional process involving the totality of man in his political, economic, psychological, social relations, among others.

Literature Review

It is a tactful and concise review of extant works or study materials that have direct and indirect bearing to the topic of investigation. As a significant and critical activity, the review of literature focuses on identifying contributions already made on the subject of investigation (Abada, Okafor & Omeh, 2018). However, the review of extant literature will be done based on the following themes:

Fiscal Arrangement and Federal Practices in Nigeria

Revenue allocations and transfers of resource control had become contending issues and debates that had propelled lingering questions on Nigerian federal practices. The most worrisome to national development is the power of government at the centre determining what constitutes revenue allocations and how it would be shared among the federating units. Sequel to this, Eme (2013) argues that the issue of fiscal federalism in Nigeria seems to have derailed national development due to fiscal imbalance, over-dependence on the centre, agitation for resource control, among others. In his view, Babalola (2015), posits that fiscal imbalances occur because constituent units hardly have enough resources to match their expenditure. But, irrespective of how they occur, imbalances must be corrected in order for the federation to continue to exist, and this may take the form of intergovernmental transfers which have the capacity to enable or limit governments in the discharge of their responsibilities.

However, Danjuma (1994), posits that fiscal federalism necessitates revenue sharing arrangement to enable the component units carry out their various functions. The fiscal arrangement within the federation should, therefore, adequately cater for the federating units to enable them discharge their constitutional responsibilities. In Nigeria, it involves the assignment of functional responsibilities and taxing powers among the federal, state and local governments. The functions are classified into three. The first is the exclusive list on which only the federal governments can act. The concurrent list contains responsibilities shared by both federal and state government to act while the third, the residual list is reserved for the state government only. Though revenue sharing in Nigeria, has witnessed a plethora of reviews, as evidenced by various committees and commissions instituted in this regard, yet no reliable formula has been evolved in meeting the country's yearnings and aspirations (Teidi, 2003:39).

However, Elaigwu (2007) noted that in terms of resource distribution, the principle of derivation occupied a significant place in the distribution formula. This followed recommendations of the Louis Chick Commission of 1953 which was set up to 'assess the effect, on the public expenditure of Nigeria as whole, of the reallocation of functions between the centre and the regions'. Derivation principle provides for revenue allocation in proportion to the contribution to the federal purse by each state. It was also strongly felt that the principle of derivation which gave 50% of revenues to the old regional governments controlled by the dominant ethnic groups was abandoned in order to enable these same groups to control the oil wealth produced from the oil minority states. Adoption of this principle of derivation as the basis for revenue allocated to the regions increased financial disparity among the regions. In view of this, Teriba (1966) posits that;

"Following Sir Louis Chick's recommendations, the Western Region received the largest share of the proceeds of import, export and excise duties as well as the total allocation from about 39 per cent under the 1952-54 regime to more than 41 per cent between 1954 and 1959. The Eastern region declined from 29 per cent to 24 per cent during the period. Though the North maintained the same share but has suffered a considerable loss of revenue through errors of 'defective derivation percentages. Consequent upon the dissatisfaction with the system was agitation for another fiscal Commission "

Though, introduction of Distributive Pool Account (DPA) de-emphasized derivation principle. According to Egwaikhide (2016), the application of derivation promoted regional hostility and disunity because it supported uneven development. The current revenue allocation formula poses a lot of problems as it grants minimal fiscal autonomy to the state and local governments in terms of revenue assignments and the major taxes such as company income tax, value added tax, customs and excise duties, tax on petroleum products and education tax are assigned to the federal government.

Table 1: Nigeria's federal, state and Local Tax jurisdiction and Agreement

Tax	Legal Jurisdiction	Collection	Retention
Import duties	Federal	Federal	
Exercise duties	Federal	Federal	
Export Duties	Federal	Federal	
Mining rent and royalty	Federal	Federal	
Petroleum profit tax	Federal	Federal	
Capital gains tax	Federal	State	State
Personal Income tax (other than listed in 8)	Federal	State	State
Personal Income tax; Armed and Police Forces, external affair officers, non-residents, residents of Federal Capital Territory	Federal	Federal	Federal
Value added tax (Sales tax before	Federal	Federal/ State	Federal/ State
Company tax	Federal	Federal	Federal
Stamp duties	Federal	State	State
Gift tax	Federal	State	State
Property tax and ratings	State	State/Local	State/Local
License and fees	Local	Local	Local
Motor park dues	Local	Local	Local
Motor vehicle	State	Local	Local
Capital transfer tax (CTT)	Federal	State	
Pools betting and other betting taxes	Federal	State	
Engagement tax	Federal	State	
Land registration and security fees	Federal	State	
Market and trading license and fees	Federal	Local	

Source: Anyanwu (1995)

The two components of Revenue Allocation Formula in Nigeria used for the disbursement of the Federation Account Vertical and Horizontal Formulae are Vertical Allocation Formula (VAF) and Horizontal Allocation Formula (HAF)

Vertical Allocation Formula (VAF): This formula shows the percentage allocated to the three tiers of government i.e. federal, states and local governments. This formula is applied vertically to the total volume of disbursable revenue in the Federation Account at a particular point in time. The VAF allows every tier of government to know what is due to it; the Federal Government on one hand and the 36 States and 774 Local Governments on the other (Bashir, 2008:3).

The subject of these sharing schemes is the federally collected revenues. This is because the revenues generated within the jurisdictional areas of the units states and local governments are not subject to the national sharing formula. In the annals of federal countries‟ revenue sharing arrangements, the sources of the federally collected revenue that form the subject of the sharing formula have remained largely unchanged. These sources which are not amenable to other units include import duties, mining rents, excise units, export duties and royalties (Ovwasa, 1995). The implication of this is that, since these sources of revenue are not amenable to the jurisdiction of the other units of government, the problem of revenue allocation has focused on not who should raise the taxes, but on how to share the proceeds that is, the actual revenue collected by the federal government. The imbalance between functions and resources base, calls for higher level government to transfer revenue to the lower level.

Horizontal Allocation Formula (HAF): The formula is applicable to States and Local governments only. It provides the basis for sharing of the volume of revenue already allocated en bloc to the 36 States and 774 Local Governments. Through the application of the principles of horizontal allocation formula, the allocation due to each State or Local Government is determined. Thus, it can conveniently be concluded that the vertical allocation formula is for inter-tier sharing between the three tiers of government while the horizontal allocation formula is for intra tier sharing amongst the 36 States and the 774 Local Governments in Nigeria (Bashir, 2008:3). It arises out of the variations in revenue generation capacities of the component units. Where the revenue raising capacities are low, heavier tax burden is imposed relative to higher revenue raising capacities area. This transfer is called "equalization transfer". This transfer is necessary because higher taxation will scare away businesses and the economy of the unit will become more depressed. To avoid this, the higher the federal level of government has to transfer to the lower unit(s), the better, to enable it make up for the differences between its internally generated revenue and those required for maintaining the minimum standard of services.

Public Finance and Economic Development

According to Olowononi (2016), it is argued that the principles and practice of public finance which concentrates functions and power in the hands of the federal government will accelerate economic development. Of course the rational is that classical federalism favours centralization and integrates fiscal powers. However, a major explanation for Nigeria's poor economic performance in particular may be found in the state's flawed domestic political economy, which encourages over dependency on oil. Nigeria's post-colonial economy inherited an economy that was reliant on agricultural products for its foreign exchange earnings, but the discovery of oil changed that, and by 1973 the Nigerian economy had been transformed into an oil rentier economy, as the state became heavily dependent on oil rents for its sustenance. Nigeria's neglect of the agricultural sector has been well documented and needs no extensive discussion here (Bangura, 1986).

Nigeria's economic record since the oil boom of the 1970s has been characterized by a lack of growth and increasing poverty. The Nigerian state now operates oil centered economy in which all other sectors, and by extension, governments at all levels, consequently depend on the oil sector. Over the last four decades, the sources of public revenue in Nigeria are proceeds from the sale of crude oil, taxes, levies, fines, tolls, penalties and charges. Oil revenues are the main source of public revenue, accounting for about 80% to 85% of the total (AfDB, UNECA, and OECD 2010). In the period 2001-09, oil revenues averaged 27% of GDP while tax revenues averaged 6.4%. Oil revenues have been volatile, ranging from 35.6% in 2001 to 19.6% in 2009 when oil prices dropped as a result of the global recession. This problem is further compounded by the country's federal system, which is loaded with a myriad of centrifugal forces, including ethnic diversity and economic disparity among the federating units. Nigeria is one of the oil rich countries in the world, yet the country's oil wealth has not provided the needed stimulus for economic development. It also affects the political balance because, whichever level of government has the major financial resources, finds in its hand the means of political control, and determine which governments or structures are able to use these instruments to control the economy. Therefore the contemporary controversy of restructuring does not merely exist because of the arrangements in themselves but because of the development implication of Nigerian fiscal federalism

Theoretical Framework of Analysis

The systems and practices of intergovernmental arrangements, nature and configuration of relationships among the tier levels of government in Nigeria is a replicate of power wielding. Therefore, situating the relationship that exists between the government at the centre and various component units calls for the appreciation of unequal power equation. Hence, the understanding of this piece of study is guided with the domestication of power theory as propounded by Han Morgenthau in 1967.

Accordingly, Morgenthau (1967: 29) sees power as man's control over the minds and actions of other men. Meanwhile, in Nigeria federal practices, the government at the centre controls and at the same appropriates enormous power over resources at the expense of the federated units.

Fundamentally, the interactions and interconnectedness of various tiers of government, the exercise of power for appropriation of values and resources always set in. Therefore, the spillover effect of over centralization of power by central government is the powerlessness of the component units toward promoting development of their jurisdiction. The imbalance in the fiscal arrangement had stood tall to conscripts other tiers of government from performing. Despite the stipends that accrue to the federating units are not enough to offset the administrative and logistical operations.

The entrenchment of the institutions of federal accounts at the centre and state-local government joint account across states in Nigeria proves the nature of undiluted power configuration and excesses exercised. The effects abound as other tiers other than the government at the centre cannot claim to be performing with bare hand and resources. Likewise, the untimely disbursement of federal allocations amount to shivering by federating units that seek alternative of going for loans. The amounts which would have used to provide adequate development will then be offered as a sacrificial servicing of loans. The state government on their part through the instrumentation of joint account with local government councils in their areas of operation had continued unceaselessly appropriating unnecessary power over accruable and other funds made available to third tier government. The implication is the continued general poverty and lack of development of man and the Nigeria nation state. There is no infrastructure and other indicators of both human and physical development made by state government, rather they rely on allocations that may not come at when due.

Methodology

The practice of Nigeria's version of federalism and the attendant implications on the development of the polity at large has called for the needs to decentralize power and weigh the operations of intergovernmental relations as it affects other tier levels of government. The study of this kind tolled the procedural steps underlining the strengths and weakness of other levels of government in discharging their fundamental responsibilities to bring forth development in the country. Therefore, worried by the conscripted nature of federal practices, the study gears toward filling the gap in the extant literature. Methodologically, the study adopted documentary method, while data were adequately sourced through the secondary sources of data collection. The analysis of data was done through content frame. The secondary sources appropriated include journal articles, monographs, text books, internet, newspaper etc.

Findings

The quest and entrenchment of modern democracy in many developing economies had heightened the path of participation of the citizens in matters important to the system. The government in the long run, reflecting the mandate given, is charged with providing basic necessities of life at any level of its operation. Such practice is not an exception in Nigeria as it claims to provide dividends and infrastructure for development. However, despite the claims and counter-claims by Nigeria federal practices has attracted gamut of agitations to restructure the structure of federalism peculiar to the system. Also identified as finding is that the components and federating units are totally engulfed with myriads of developmental challenges due largely to the nature of federal and fiscal deficit of the system

Result

Arising from investigation of the study is the result of the findings. Accordingly, the study exposed that unless the system of federal relations is being amended to reflect true and formidable fiscal and intergovernmental arrangement, other tiers of government other than the government at the center will continue to exist at the mercy of the central government. Also, the lump sided nature and accruable to the government at the center conscripts the federating states and local government from performing, thereby making them face difficulties in providing laudable developmental projects and dividend to the people in their respective jurisdiction.

Conclusion and Recommendations

It is undisputable and very clear that in many emerging African democracies, the system of fixing the state to respond to the demands of the citizenry has become problematique following the nature and character of post colonial African states. The Nigeria state is not totally exonerated as agitations from different quarters ensue to restructure the federal practice. It is on this note that paper appreciated the cosmetic nature and configuration of Nigerian federalism as implicated on the fiscal imbalance between and amongst the three tiers of government; central, component units and local government. The theory utilized centered on the power theory which emphasizes that central government due to its nature as the government at the center lords over other tiers at the expense of the other levels of government. Importantly, the implication of unequal power and fiscal responsibilities has dwindled other levels of government other than the government at the center from providing basic infrastructure for the wellbeing of the people and nation- state at large.

However, arising through the investigation and findings of the study, the paper recommends the following;

There is the need through enforceable legal frame, statutory role of the three tier system as invoked in Nigerian federal system. It is important noting that the mixing up of the levels of government in terms of unclear demarcation of lines of action had forced the central government to appropriate the advantages. The constitution like every other documents need to review in order to reflect the restructuring question.

It is high time tiers of government shall have sense of responsibilities. The federating units and the local government should exhibit the culture of self reliant. This is important for making them devise more and reliable sources for its sustenance. The component units together with local government is expected by now not hope for stipend coming from the center, that which may not come forth as when due. Also, unexplored avenues should be appropriated to make yields to government, thereby entrenching the spirit of self- reliant.

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