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Fiscal Federation and Revenue Allocation in Nigeria: An Empirical Study

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Abstract

Nigeria's politics surrounding the distribution of federal money among the federating units have never been easy. Thus, this study looked into Nigeria's politics around revenue allocation and fiscal federalism in practice. In order to get some results, it used the secondary method of data collection and documentation analysis. The federalism idea served as the study's location and direction. According to the study, the revenue allocation formula is not so much used for allocating shares of the so-called national cake to different segments of the population as it is for preserving political stability, social justice, and fiscal efficiency—all of which are necessary for ensuring growth and sustainable development within the confines of well-defined national objectives. However, the report claimed that throughout time, the Nigerian federal government has usurped most powers and centralized resources at the expense of the federating units. As a result, there have been persistent calls for the federating units to have more authority and resources. These initiatives, which have included the politics of derivation, the reconsideration of the sharing formula, and the struggle for resource control, have frequently been confrontational and violent, dividing the nation along long-standing ethno-regional lines. The report made several recommendations, including the need to diversify the economy, guarantee justice, equity, and accountability, and devolve authority and resources through constitutional frameworks in order to maintain Nigeria's cohesion, stability, and existence.

Keywords*: Fiscal Federalism, Federalism, Resource Control Revenue Allocation, and Devolution of Powers*

Introduction

In contemporary times, fiscal decentralization has gained popularity irrespective of societal levels of development and civilization. Countries are resorting to devolution as a means of enhancing the efficiency of their public sectors. In the US, the federal government has returned a sizable amount of its jurisdiction to the states for a number of important programs, such as Medicaid, poverty, housing, legal services, and job training. Since state and local governments are more proximate to the public, it is hoped that they will be more sensitive to the unique preferences of their constituents and capable of coming up with innovative solutions for delivering these services (Sharma, 2005:169).

But this does not signify that all political arrangements are "fiscally" federal; rather, it just means that any country attempting "fiscal decentralization" can adopt "fiscal federalism" as a set of recommendations. In actuality, fiscal federalism is a comprehensive normative framework for assigning duties to the different governmental levels and for choosing the appropriate fiscal instruments to carry out these obligations, according to Oates (1999: 1120).

Nigeria is a multi-state country that belongs under the federal state category. The Nigerian federal system was established with the ratification of Richard's constitution in 1946, which granted internal autonomy to the then-existing provinces of Nigeria. Additionally, the 1954 Littleton Constitution's adoption gave Nigeria's federal system more legitimacy (Nwosu, 1980).

Even in non-federal states, there has been a growing movement in recent years for greater fiscal autonomy. According to Tanzi (1996), several scholars have linked this to both rising incomes and globalization, as well as the world's growing democracy. Additional particular explanations for the growing call for decentralization include:

• More and more central governments are attempting to develop local capacities by giving their regional government's greater power as they become aware that they are unable to meet the competing demands of their diverse constituency.

• Local and regional political leaders are calling for greater autonomy and the taxing authority that comes along with their spending responsibility;

• With regard to national economic development measures, central governments are looking to local and regional governments for assistance (Ozo-Eson, 2005:1).

Conceptual Framework

i. Federalism

The Latin term "foedus," which meaning compact, covenant, or agreement, is where the idea of federalism originates. Nonetheless, there are countless attempts to define the term "federalism." First of all, Wheare (1963), who is sometimes cited as the father of federalism, described federalism as "the method of partitioning governmental authorities so that central and regional administrations are each inside a sphere, coordinate, and independent." Riker also characterizes federalism as a method of government. Federalism is the primary alternate to empire, according to him. Federalism has been defined as having, among other things, two levels of authority over the same region and the assurance of self-government for each level of government (Riker, 1964). According to Elaigwu (2005, p. 6), federalism is understood to be:

> *A halfway ground between two types of self-determination in a multinational state: on the one hand, the self-determination of constituent groups to maintain their unique identities, and on the other, the determination supplied by a national government that ensures security for everyone in the nation-state.*

Additionally, he makes the case that people's desire to create a federal union without necessarily surrendering their individuality is the source of federalism. Federalism, then, is an effort to incorporate the various political, social, cultural, and economic interests into a more comprehensive framework of unity. As a result, it makes an effort to balance the right to take independent action in some situations with the requirement for cooperation in others. Therefore, federalism is conceptually about fairness, equity, and fair play amongst the polity's constituent parts as well as its communal groupings in a plural society like Nigeria. Additionally, it deals with the spatial mobilization and usage of social resources in a way that promotes development and progress that is balanced. All things considered, the division of political and economic authority among the many parts and tiers of a federal government is federalism. It is, therefore, a system of governance that is specifically intended to address the dual challenge of upholding diversity and unity.

ii. Fiscal Federalism

According to the federal principle, every level of government should have enough funding to carry out its duties without having to request financial support from higher levels of government. Put another way, allocated tasks and financial resources should be in line. As persuasively argued by Wheare (1963): borrow to pay for its own services out of pocket.

This implies that fiscal federalism is the term used to describe the method by which responsibilities and tasks are assigned to the various governmental tiers within a federation. Anyanwu (1997) provides evidence in favor of this point of view by stating that fiscal federalism is the term used to describe the institutional framework or structure that a society has in place for deciding how to raise money, incur costs, and take on debt or borrowing. Accordingly, Ovenseri-Ogbomo (2007, p. 56) contends that fiscal federalism comprises the allocation of monetary and economic duties between or among the federating entities and the legally recognized, centrally administered government. This study argues that fiscal federalism is fundamentally an institutional framework that shares authority over revenue collection and distribution in a federal system, enabling the central government and the federating units to carry out their legal responsibilities. Since the various federating units in Nigeria demand more financing, a say in the revenue base, and changes to the allocation method, Nigerian fiscal federalism has become an argumentative issue, particularly in the Fourth Republic. There are significant implications for Nigeria's security, stability, and progress from this.

iii. Revenue Allocation

The federal and state governments, or whatever names they may go by, are constitutionally designated as the minimum number of tiers of government in all federal systems. Nonetheless, Nigeria is a federal state with three levels of government: federal, state, and municipal. More often than not, the federating units' statutory responsibilities are not complemented by the distribution of revenue sources. This leads to an imbalance between the obligation to make expenditures and the resources available to do so, which causes the different governmental levels' fiscal capacities and their expenditure responsibilities to diverge (Jega, 2007). As a result, the debate over revenue sharing or allocation emerged as a means of striking a balance between the duties and powers of various governmental levels. Usually, to do this, resources are moved from one governmental level to another. Like in many federations, Nigeria's constitution or Revenue Commission may approve a formula or set of criteria for the transfer of resources from the federal to the subordinate levels of government (Omodero, 2019).

Thus, the allocation of financial resources from one level of government to another can be referred to as revenue allocation. It can be understood in this study as the way the several federation governments divide up federally collected funds. The sharing formula has been controversial and existed before Nigeria gained its independence.

Theory of Fiscal Federalism

The initial theory of fiscal federalism derived its fundamental foundation from the two foundational works on the theory of public goods by Kenneth Arrow, Richard Musgrave, and Paul Sadweh Samuelson (1954, 1955). The basis for what is now recognized as the appropriate function of the state in the economy was established by Musgrave's 1959 book on public finance. The concept was subsequently referred to as the "Decentralization Theorem" (Ozo-Eson, 2005).

Background Issues in Nigerian Federalism

Countries typically adopt federalism to reunite legally divided units into a single nation, to reorganize a nation that was formerly unitary, or as a result of both processes together. Every federation has a unique history pertaining to its formation and the way its borders and politics have changed. According to Anderson (2008), these tales feature international treaties, colonial empires, dynastic marriages, battles and revolutions, and peaceful democratic procedures. Nigeria, being a poly state with a multitude of cleavages, including ethnic, religious, linguistic, and cultural heterogeneity, chose federalism in part as a means of handling conflict among her diverse populace. Aggressive ethno-regional politics emerged as a result of growing anxieties and mistrust amongst communities in the competitive setting during the last stages of colonization. The unitary colonial State witnessed official federalization by 1954 (Eliagwu, 2005).

It is crucial to emphasize that the shape and nature of the collective authority, or framework, and the modifications made to it since 1900, have an impact on the country's unity or lack thereof (Coleman, 1958). While the 1914 merger brought the North and the South together politically, it did not have the goal of creating a single State in order to install a native government. Thus, virtually little was done to unite the Northern and Southern Provinces between 1914 and 1946. Each set of provinces was handled independently, and the colonial officers in charge of these administrations battled assiduously to maintain their divisions. Similarly, there was no forum for the territory's residents to get together and discuss matters impacting the nation as a whole prior to the adoption of the Richards Constitution in 1946, which established a Central Legislative Council. Some scholars argue that given Nigeria's multiethnic composition, the different political developments in the North and the South must have been appropriate for colonial rule but detrimental to the creation of a State and a Nation (Eliagwu, 2005).

In 1951, the McPherson Constitution was adopted in place of the Richards Constitution, which had been opposed and rejected. The regions now have more autonomy because to this Constitution. Once more, the Eastern area was to have a unicameral legislature, but the Western and Northern regions were to have bicameral legislatures. One may argue that Nigeria was using a unitary system of government up until this point, or at most, what Elaigwu (2005, p. 25) refers to as "a quasi-federal form of government." As the areas gained more autonomy and the possibility of achieving self-government increased, new nationalist identities began to take shape around them. As a result, all of the political parties that arose to challenge the colonial rulers for power had distinctly ethno-regional foundations. The foremost ethnic groups of those areas, the Hausa/Fulani, Igbo, and Yoruba, controlled and dominated the Northern People Congress (NPC), the Northern People Congress (NPC) National Council of Nigerian Citizens (NCNC), and the Action Group (AG), which had their bases in the North, East and West, respectively. In light of this, regionalism and ethnicity have become deeply embedded in Nigerian politics, where power is obtained by manipulating shared emotions. It is enough to say that the very notion of Nigeria's decolonization provoked conflicts between groups that fought for control in an effort to: (i) defend their interests from any encroachment by other parties throughout the competition process; and (ii) usurp control of the colonial government's reins of power and manage the allocation of resources and patronage (Elaigwu, 2005).

The Constitutional Conferences of the 1950s provided ample evidence of the centrifugal forces at work in Nigeria and the leaders' general mistrust of one another. The fears that Nigeria's ethno-regional leaders held for one another subdued some nationalists' calls for a more centralized federal system of government or a more unified style of governance. So, in exchange for the assurance of self-government and the eventual abolition of colonial umpireship, the regions chose more autonomy. A balance between centrifugal and centripetal forces led to the adoption of a federal structure. It was predicated on the federating units' specific mindset, which is to seek "union but not unity." The 1954 Constitution just made the leaders of Nigeria's federal system of government lawful; they had chosen a federal system otherwise. The Constitution granted the regions considerable discretion in making decisions. Regional bureaucracies were formed, and Regional Assemblies emerged (Hembe, 2000). But the strong ethnoregionalism that prevailed between 1951 and 1959 created the mistaken sense that the areas were homogeneous. The regions were by no means homogeneous, with several vociferous and politically engaged minority groups present in each. As Nigeria approached independence, demands for distinct political entities increased due to minority communities' fears of being dominated by majority ethnic groups (Eliagwu, p. 2005).

Consequently, there have been incessant calls for the establishment of additional States within the Nigerian federation. From its founding as three regions, the nation has expanded its number of constituent units to 36 States, a Federal Capital Territory, and 774 Local Government Areas through the process of State creation. In Nigeria, there are still more calls for the creation of additional states. According to Ekekwe (1986), these calls are driven by the constitutive interests of the advantaged classes, for whom the establishment of the state has become a means of gaining access to power and multiplying opportunities for prebendalist accumulation such as rent-seeking.

The Development of Nigeria's Revenue Allocation and Generation

Since colonial times, numerous commissions and committees have worked on the problem of fiscal federalism (Sagagi, 2015). However, this topic is still very much at the forefront of the national conversation today. This is still an unresolved issue, as seen by the requests and calls for the reevaluation of the sharing formula and resource control. According to Kalu (2011), there were two Supreme Court rulings, one Act of the Legislature, six Military Decrees, nine Commissions, and one Act of the Legislature that attempted to define and alter the budgetary interrelationships among the federation's constituent parts between 1948 and 2012. In the present democratic regime, there has been an increasing trend of redefinition or interpretation of the income sharing framework, both between the States and the Federal Center (vertical sharing) and among the States themselves (horizontal sharing). He goes on to say that fiscal federalism in Nigeria was developed gradually. According to him, Nigerian fiscal federalism saw its initial growth between 1948 and 1952. This stage was distinguished by a centralized financial system in which regional governments received the surplus from the national government's budget according to the derivation principle.

Thus, the federal government's spending requirements came first. The principle of derivation for the distribution of federally collected revenue was operationalized in the second phase (1952–54), along with the introduction of autonomous revenue and tax jurisdiction for the regional administrations. The second phase's fundamental components were transferred to the third phase (1954–59). This phase's stress on the derivation principle in the distribution of federally collected money was one of its main differentiators. Considering the surge in their respective exports of cotton and cocoa, the Northern and Western Regions were happy about this. The Eastern Region was not happy with its application since palm oil, its primary export crop, was having trouble on the international market. This was the age of fiscal federalism centered on the state. Proponents of either a greater focus on derivation or resource control, particularly minorities in the oil-producing areas, continue to use it as a benchmark today.

The post-independence era of politics (1960–1966) produced the fourth (4th) stage of Nigeria's fiscal federalism development, which is still the primary pillar of fiscal federalism in the country today. During this phase, the derivation principle was used to lessen the prior emphasis on regional financial independence. It was maintained that regional stability depended on the federal government's financial stability. In light of this, the constitutions of 1960 and 1963 stipulated a 50% deduction for all mining earnings. The Distributable Pool Account, which served as the model for the Federation Account of today, was established during this phase. Certain tax proceeds were deposited into this account by the federal government, and the regions were then distributed funds from it according to the subsequent criteria: (1) uninterrupted government services; (2) minimal tasks of every government; (3) necessity, as determined by population density in the region; and (4) balanced federation development (Kalu, 2011).

Growing centralization has been a defining feature of the fifth phase, which started in 1966 as the States' reliance on the federal center grew. The military's tight grip on Nigerian politics has mostly corresponded with this time. The military's centrist command structure had an impact on the fiscal relations between governments. Military rulers used a sum of historical happenings and events to further their centrist preferences. Put another way, the Civil War-era demand for national unity was used as a political tool to fortify the Center at the States' detriment. The formation of states from their constituent areas and the ongoing disintegration of those states served as vehicles for the centralization of budgetary power. Furthermore, Kalu argues that different decrees were issued that took jurisdictions and tax powers away from the States. This era is well described by the idea of a predatory center. The 1999 military-dictated Constitution incorporates elements of the centrist ideology. Therefore, democratically elected central administrations have found it too hard to resist fiscal centralization, especially in the current democratic environment. Lower levels of government have expressed their desire for a more decentralized fiscal system as a result of this. Nonetheless, the National Assembly's and the federal government's designated fiscal commissions have persisted in developing revenue distribution formulas that uphold fiscal centralism (Ezo-Eson, 2005).

In Nigeria, the politics and debate about the best way to divide resources have been ongoing and heated. A number of Commissions have been established over time to devise a fair and just mechanism for the nation's revenue distribution. Aboyade Technical Committee (1977); Okigbo Presidential Commission (1979); T.Y. Danjuma Fiscal Commission (1988); Phillipson Commission (1946); Chicks-Phillipson Commission (1951); Chicks Commission (1953); Raisman Commission (1958); Binns Commission (1964); Dina Interim Revenue Allocation Committee (1968); Aboyade Commission (1977); Okigbo Presidential Commission (1979); and Revenue Mobilization, Allocation and Fiscal Commission (1999)

Considering the lengthy history of commissions and committees created to address budgetary concerns and problems with revenue allocation that occasionally emerged, the commissions and committees were typically disbanded or abandoned after completing their designated tasks. In contrast to prior ad hoc commissions or committees, a body was required to manage revenue allocation and fiscal concerns continuously due to the growth of additional States and Local Governments, which complicated intergovernmental fiscal relations. By Decree No. 49 of 1989, the Revenue Mobilization Allocation and Fiscal Commission was replaced as the National Revenue Mobilization Allocation and Fiscal Commission (NRMAFC). Decree No. 98 of 1993, which is currently known as RMAFC Act Cap. R7 LFN 2004, later modified Decree No. 49 of 1989. However, in accordance with section 153 (1) of the 1999 Federal Republic of Nigeria (as amended) Constitution, the Commission was renamed the Revenue Mobilization Allocation and Fiscal Commission (RMAFC). It was one of the fourteen (14) Federal Executive institutions founded, according to Babalola (2015), to serve as checks and balances on Nigerian democratic processes.

The Vertical and Horizontal Formulas are the two main sets of Revenue Allocation Formulas. Funds for the federal, state, and municipal governments—the three officially recognized divisions of government—are distributed using the Vertical Formula. In contrast, the Horizontal mechanism uses a revenue sharing mechanism to provide cash to municipal and state governments, respectively. The following is the revised revenue sharing formula:

A: Vertical Formula

1	Federal	54.68 percent
2	States	24.72 percent
3	Local Government	20.60 percent
	Total	**100 percent**

Source: Ikeji (2011)

B: Horizontal Formula

i.	Equality	40percent
ii.	Population	30 percent
iii.	Land Mass and Terrain	10 percent@ 5 percent each
iv.	Social Development Factors	10 percent
	1. Education	4 percent
	2. Health	3 percent
	3. Water	3 percent
v.	Internal Revenue Generation	10 percent
	Total	**100 percent**

Source: Ikeji (2011)

The Nigerian Fiscal Federalism: Its Nature and Crises

Due to the nature of federalism, countries with federal systems of government must constantly assess their systems and develop fair and practical guidelines for revenue distribution and taxation. From Nigeria's point of view, multiple attempts were made to arrive at a cooperative formula for allocating its national economic resources among the federation's constituent states. Notwithstanding these endeavors, Nigerian federalism continues to face significant challenges due to innately difficult difficulties. The over-reliance on oil money, disagreements over the revenue sharing formula, Nigeria's fiscal relations' inclination toward centralization, and the push for resource control are a few of these pressing concerns. In Olobiri, Bayelsa State, Nigeria, oil was first found in commercial quantities by Shell-BP in May 1956. The start of oil exploration by international corporations two years later was a turning point in the political economy of the Nigerian federation. Nigeria became the seventh largest oil exporter in the world and its economy was centered on oil due to the phenomenon of oil exploration. Due to this scenario, oil became the primary fiscal federalism concern. Nigeria has received about $250 billion in oil earnings in the last nine years (Sagay, 2008).

It is ironic, nevertheless, that Nigeria's economy has suffered as a result of oil drilling despite the resource's huge return of income. It therefore makes the scenario appropriate to be called the "resource curse." As a result, the previously thriving agricultural sector as well as other profitable industries including mining, industry, and human capital development were undermined. It inevitably sapped the spirit of competition that over time in Nigeria would have fueled economic expansion in these underutilized areas. Furthermore, an excessive reliance on oil money had a detrimental effect and presented significant difficulties for the nation's fiscal federalism. As a result, over time, a leech syndrome has developed among the federation's constituent units. It inevitably led to the states being reliant on the Federation Account's handouts. The majority of states are economically dependent on the federal government because to their leech-like characteristics, which has reduced the federating units' degree of autonomy. This resulted in the Federal Government and the component units having a master-servant relationship.

The process of distributing national resources and revenues among the federation's tiers of government is known as revenue allocation. The longevity of a federalist system of government depends on the nature of intergovernmental budgetary relations in such countries. Revenue distribution is usually a divisive topic in federal states across the globe. One of the most frequent causes of intergovernmental disputes, according to Olalokun (1979, 109), "in most, if not all, federal countries, centers on the problem of securing adequate financial resources on the part of the lower levels of government to discharge essential political and constitutional responsibilities." Due to the political nature of revenue sharing, there have been several agitations, disputes, and outright rejections among the constituent states of the Nigerian federation since its foundation. Contradictory conditions that were frequently disallowed by the most Nigerian states abound in the income sharing process. For example, the income sharing principle was characterized by illogicality previous to the 1977 Aboyade Technical Committee on revenue allocation formula. Furthermore, it is challenging to quantify the idea of even development in a useful way.

The federation's current conditions lead to a variety of interpretations of the idea of national interest, which resists any one interpretation. It is critical to emphasize that the debate and squabbling over revenue allocation will continue to be a chronic issue in Nigeria's fiscal federalism as long as states' survival and economic growth are dependent on the federal government. Nigeria's fiscal federalism is also challenged by the Federal Government's hegemonic and centralizing inclinations.

The abrupt transition of Nigeria from an agrarian to an oil-driven economy fueled central government power over the states and furthered centralism. A sequence of military edicts and fiats by several military regimes solidified the central government's hegemonic authority. Therefore, laws like the Petroleum Tax Decree 13 of 1970 and the 1975 Amendment Decree, which granted the Federal Government jurisdiction over mining rents and royalties from both onshore and offshore exploration, further undercut the concept of derivation (Sagay, 2008).

Conclusion

The study examined the development of theoretical explanations of fiscal federalism, examined the nature and state of fiscal relations in Nigeria, and came to the conclusion that these relationships are extremely unbalanced, preferring the federal government to the numerous state and municipal administrations. The Federal Government always receives a larger share under the sharing system, with less of an impact on the general population.

Thus far, the unbalanced financial structure has led to mistrust, indifference, and ongoing confrontation, both overt and hidden. Based on the analysis, it can be concluded that Nigeria's centralist fiscal relations system, problematic over-reliance on oil revenue, disputes over the principle of sharing, and unbalanced federal-state relations are stubborn obstacles that threaten both the country's continued existence as a federal state and its ability to have harmonious fiscal relations. Urgent corrective action is required to address Nigeria's unsolvable fiscal federalism issues, which stem from the country's highly despised and incoherent system.

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