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Fiscal Federation and Revenue Allocation in Nigeria: An Empirical Study

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Abstract: *The politics of determining the sharing of the federal revenue among the federating units in Nigeria has always been contentious. This study therefore investigated the practice of fiscal federalism and the politics of revenue allocation in Nigeria. It adopted the secondary method of data collection and relied on documentary analysis to arrive at some conclusions. The study was located and guided by the theory of federalism. It was obvious in the study that, revenue allocation formula is not a mere instrument for determining what segment of the polity gets what percentage of the so-called national cake, rather it is more of a tool used for ensuring fiscal efficiency, social justice and political stability, which guarantees growth and sustainable development within the context of well-defined national objectives. The study submitted that, in Nigeria, however, the federal government, over the years, has centralized resources and appropriated most powers at the detriment of the federating units. There has therefore, been unrelenting agitations for devolution of powers and resources to the federating units. These activities, including the agitation for resource control, review of the sharing formula and the politics of derivation have often times been confrontational, violent and have polarized the country along the age long ethno-regional lines. Among other recommendations, the study established the need to devolve powers and resources through constitutional frameworks, diversify the economy, ensure justice, equity and accountability in the quest for cohesion, stability and continued existence of Nigeria.*

Keywords: Federalism, Fiscal Federalism, Revenue Allocation, Resource Control 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).

However, this does not imply that all political structures are "fiscally" federal; rather, it merely indicates that "fiscal federalism" is a set of guidelines that can be used by any nation trying "fiscal decentralization." Actually, according to Oates (1999: 1120), fiscal federalism is a general normative framework for allocating responsibilities to the various governmental levels and for selecting the proper fiscal tools to carry out these responsibilities.

Nigeria is a multi-state nation that is properly categorized as a federal state. The passage of Richard's constitution in 1946, which gave the then-existing regions of Nigeria domestic autonomy, marked the beginning of the Nigerian federal system. Additionally, the 1954 Littleton Constitution's adoption gave Nigeria's federal system more legitimacy (Nwosu, 1980).

In recent years, there has been a growing drive toward increased fiscal decentralization even in non-federal states. According to Tanzi (1996), several scholars have linked this to both rising incomes and globalization, as well as the world's growing democracy. The need for decentralization is also growing for the following specific reasons:

• Central governments are looking to local and regional governments for support with national economic development strategies as they are finding it increasingly difficult to meet the competing needs of their various constituencies. As a result, they are trying to build local capacities by assigning responsibilities downward to their regional governments.

• Political leaders at the regional and local levels are calling for increased independence and the taxing authority that accompanies with accountability for spending (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 off, federalism is defined as ―the method of partitioning governmental authorities so that central and regional administrations are each inside a sphere, coordinate, and independent‖ by Wheare (1963), often considered to be the father of federalism. Riker also characterizes federalism as a method of government. Federalism is the primary alternative 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 autonomy for each level of government (Riker, 1964). According to Elaigwu (2005, p. 6), federalism is understood to be:

> *a compromise solution in a multinational State between two types of self-determination – the determination provided by a national government which guarantees security for all in the nation – State on one hand, and the selfdetermination of component groups to retain their individual identities on the other.*

Furthermore, he argues that the desire of people to create a federal union without necessarily losing their identity is the source of federalism, which is an attempt to reflect the various political, social, cultural, and economic interests within the larger framework of unity. As such, it seeks to satisfy the need for cooperation in some areas and the right to independent action in others. Therefore, in a plural society such as Nigeria, federalism is theoretically about equality, justice, and fair play among the polity's constituent units as well as communal groups. It is also concerned with the spatial mobilization and utilization of societal resources in a way that promotes balanced growth and development. All things considered, federalism can be defined as the division of political and economic authority among the many parts and tiers of a federal government. It is a type of government that is purposefully made to address the dual issue of upholding diversity and togetherness.

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.

According to this, the system by which duties and obligations are distributed among the several tiers of a federation's government is known as fiscal federalism. In support of this perspective, Anyanwu (1997) argues that fiscal federalism is an institutional framework or structure that exists in a society for deciding how much money to spend, raise money, and borrow or take on debt. Parallel to this, Ovenseri-Ogbomo (2007, p. 56) argues that ―fiscal federalism involves the sharing of financial and economic responsibility between or among the federating units and the legally formed centrally managed government. According to this study, fiscal federalism essentially refers to an institutional framework that divides authority over revenue collection and distribution in a federal system so that the federal government and its component entities can fulfill their legal obligations. Because the different federating units in Nigeria are fighting for different allocation formulas, additional resources, or a say in the tax base, fiscal federalism in the country has become a divisive topic, particularly in the Fourth Republic. The stability, security, and development of Nigeria are significantly impacted by 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 matched 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 lower levels of government (Omodero, 2019). Thus, the transfer 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 basic foundations for the initial theory of Fiscal Federalism were laid by Kenneth Arrow, Richard Musgrave and Paul Sadweh Samuelson's two important papers (1954, 1955) on the theory of public goods. Musgrave's book (1959) on public finance provided the framework for what became accepted as the proper role of the state in the economy. The theory was later to be known as "Decentralisation Theorem" (Ozo-Eson, 2005:1).

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 environment during the terminal colonial period. The unitary colonial State witnessed official federalization by 1954 (Eliagwu, 2005).

It is crucial to emphasize that the shape and nature of the common government, or superstructure, 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. According to some academics, considering Nigeria's multiethnic makeup, the distinct political development of the North and the South must have been appropriate for colonial administration but unhelpful for the establishment 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. Because of this, all of the political parties that arose to challenge the colonial rulers for power had distinctly ethno-regional foundations. The primary ethnic groups of those regions, such as the Igbo, Hausa/Fulani, and Yoruba, controlled and dominated the National Council of Nigerian Citizens (NCNC), the Northern People Congress (NPC), and the Action Group (AG), which had their bases in the East, North, and West, respectively. Given this context, regionalism and ethnicity have been ingrained in Nigerian politics, with the manipulation of similar feelings to gain power.

It is sufficient to say that the very idea of Nigeria's decolonization sparked conflicts between groups that fought for control in an attempt to:

(i) defend their interests against potential invasion by other groups in the competitive process; and
(ii) usurp control of the colonial government's reins of power and manage the distribution of allottable resources and patronage (Elaigwu, 2005).

The sense of distrust of Nigerian leaders for one another and the existence of centrifugal forces in the country were amply demonstrated in the Constitutional Conferences of the 1950s. The mutual fear of one another by the ethno-regional leaders in Nigeria diluted the demands of some nationalists for a more unitary form of government or a federal system with a very strong centre. In light of the prospect of self-government and the eventual abolition of colonial umpireship, the regions chose to embrace increased 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 persistent calls for the formation of more States within the Nigerian federation. From its original three areas, the nation has expanded over time to include 36 States, one Federal Capital Territory, and 774 Local Government Areas as constituent parts of the Nigerian Federation through the process of State construction. In Nigeria, there are still more calls for the creation of additional states. According to Ekekwe (1986), these demands are driven by the constitutive interests of the privileged 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.

EVOLUTION OF REVENUE GENERATION AND ALLOCATION IN NIGERIA

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 demands for resource control and the reconsideration of the sharing formula. 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. Redefining or interpreting the framework for revenue sharing—both between the States and the Federal Center (vertical sharing) and among the States themselves (horizontal sharing)—has become more and more popular under the current democratic regime. 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 emphasis 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 phase 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. The federal government deposited specific tax proceeds into this account, from which the regions received distributions based on the following standards: (1) uninterrupted government services; (2) minimum responsibilities of each government; (3) need, as determined by the region's population size; and (4) balanced development of the federation (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 number 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).

The politics and controversy on the appropriate formula for sharing resources in Nigeria has been recurrent and contentious. Over the years, various Commissions have been set up to work out acceptable and equitable revenue allocation formula for the country. The Commissions include:

- The Phillipson Commission of 1946
- The Chicks -Phillipson Commission of 1951
- The Chicks Commission of 1953
- The Raisman Commission of 1958
- The Binns Commission of 1964
- The Dina Interim Revenue Allocation Committee of 1968
- The Aboyade Technical Committee of 1977

- The Okigbo Presidential Commission of 1979
- The T.Y Danjuma Fiscal Commission of 1988
- 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. Decree No. 49 of 1989 created the National Revenue Mobilization Allocation and Fiscal Commission (NRMAFC), which replaced the Revenue Mobilization Allocation and Fiscal Commission. Later, Decree No. 98 of 1993 (currently RMAFC Act Cap. R7 LFN 2004) modified Decree No. 49 of 1989. But in the 1999 Federal Republic of Nigeria (as amended) Constitution, the Commission was renamed Revenue Mobilization Allocation and Fiscal Commission (RMAFC) under section 153 (1). It was one of the fourteen (14) Federal Executive bodies created to provide checks and balances in Nigerian democratic practices (Babalola, 2015).

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%
2. States	24.72%
3. Local government	20.60%
TOTAL	100%

Source: Ikeji (2011, pp. 121-136).

B: Horizontal Formula

i. Equality	40%
ii. Population	30%
iii. Land Mass and Terrain	10% (@ 5% each)
iv. Social Development Factors	10%
i. Education	4%
ii. Health	3%
iii. Water	3%
v. Internal Revenue Generation	10%
TOTAL	100%

Source: Ikeji (2011, pp. 121-136).

THE NATURE AND CRISIS OF FISCAL FEDERALISM IN NIGERIA

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 around 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. Conflicting criteria that were frequently rejected by the majority of 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 rely on the federal government for economic development and survival. 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, the principle of derivation was further undermined by decrees like the Petroleum Tax Decree 13 of 1970 and the 1975 Amendment Decree, which gave the Federal Government control over mining rents and royalties from both onshore and offshore exploration (Sagay, 2008).

CONCLUSION AND SUGGESTIONS

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, favoring the federal government over the many state and local governments. In the sharing system, the Federal Government always obtains a higher amount with less of an influence on the general public. 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-dependence 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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