# The Search for a Symphony: A Discourse on the Issue of Derivation, Revenue Allocation, and Fiscal Federalism in Nigeria

*La búsqueda de una sinfonía: Un discurso sobre la cuestión de la derivación, la asignación de ingresos y el federalismo fiscal en Nigeria*

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## ABSTRACT

This paper joins the debate on the fiscal policy of the Nigerian government in terms of the revenue allocation formula of the federating units which has been a recurring theme in the country's political existence. A review of revenue allocation formulas shows that the tools used as a measure to allocate and distribute revenue had been more of political gerrymandering, with each regime choosing which formula suits them without minding how the federating units react. An introspective analysis of the various Decrees enacted by the military regimes and the Acts between 1979 and 1983 shows that the southern part of the federation had been denied the right in maximizing the full potential of the resources in their territory. With all these, it portends that revenue allocation and distribution from 1968 to 1989 were not in line with true fiscal federalism as should be practiced. It is therefore recommended that the government and stakeholders at all levels should parley and do the needful by reviewing the current sharing formula with a view to correct the anomaly that has bedeviled revenue allocation and distribution over the years. Simply put, there should be decentralization in the generation, distribution, and allocation of revenue where states should manage their resources as it will reflect true fiscal federalism as practiced in civilized clime. The constitution remains silent on the cardinal issue of derivation and that is why today the question of who gets what, when, and how in terms of revenue allocation and sharing remains politicized and a recurrent issue in Nigeria till today.

**Keywords:** Fiscal Federalism; Derivation; Resource Control; Nigeria; Autonomy; Decentralization.

## RESUMEN

Este artículo se suma al debate sobre la política fiscal del gobierno nigeriano en cuanto a la fórmula de asignación de ingresos de las unidades federadas, que ha sido un tema recurrente en la existencia política del país. Un examen de las fórmulas de asignación de ingresos muestra que los instrumentos utilizados como medida para asignar y distribuir los ingresos han sido más bien una maniobra política, en la que cada régimen elige la fórmula que le conviene sin importarle la reacción de las unidades federadas. Un análisis introspectivo de los diversos Decretos promulgados por los regímenes militares y las Leyes entre 1979 y 1983 muestra que a la parte sur de la federación se le ha negado el derecho a maximizar todo el potencial de los recursos de su territorio. Con todo ello, se deduce que la asignación y distribución de los ingresos entre 1968 y 1989 no se ajustó al verdadero federalismo fiscal que debería practicarse. Por lo tanto, se recomienda que el gobierno y las partes interesadas a todos los niveles se reúnan y hagan lo necesario revisando la fórmula actual de reparto con el fin de corregir la anomalía que ha afectado a la asignación y distribución de los ingresos a lo largo de los años. Sencillamente, debería haber una descentralización en la generación, distribución y asignación de los ingresos, en la que los estados deberían gestionar sus recursos, ya que reflejaría un verdadero federalismo fiscal tal y como se practica en un clima civilizado. La Constitución guarda silencio sobre la cuestión fundamental de la derivación y por eso hoy la cuestión de quién recibe qué, cuándo y cómo en términos de asignación y reparto de ingresos sigue politizada y es un tema recurrente en Nigeria hasta hoy.

**Palabras claves:** Federalismo fiscal; Derivación; Control de recursos; Nigeria; Autonomía; Descentralización.

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## 1. Introduction

Fiscal federalism is a usage in federal practice that refers to the fiscal (monetary) relationship between the different tiers of government (Nwankwo, 2012). This relationship revolves around expenditure and revenue matters and connotes revenue and expenditure decentralization (Nwankwo, 2012). Fiscal federalism is thus expected to be the product of some form of voluntary association involving certain division of responsibilities, functions, powers, and authority, consequently, it encapsulates the allocation of resources (vertical and horizontal) among the tiers and component units of a federal state, and institutions for the discharge of their constitutionally assigned responsibilities and functions (Nwankwo, 2012).

Adedokun (2002) gave a clear picture of the issue of fiscal federalism and revenue allocation in Nigeria. From his postulations, it was observed that the politics of revenue allocation in Nigeria has its foundation in the amalgamation of the Protectorate of Southern and Northern Nigeria in 1914 by the British colonial government. The administrative setup which followed divided the country into three regions: East, West, and North. This gave rise to the need to devise a formula for the collection and distribution of revenue. However, it was not until 1946 that the first imperial commission on revenue allocation and collection was set up. Three other commissions were set up before independence. Following the achievement of independence, several commissions for which more will be said later were set up. However, the outcome of these commissions made Adedokun (2002) opine that revenue collection and sharing is highly a political matter rather than a direct economic matter that needs to be resolved for the sake of the survival of the country.

By 1968 the federal government under the military had taken over all resources in Nigeria with the abolition of the regional structure and replaced it with the “twelve-state structure”. Here, the federal government arrogated ownership of revenue generation and distribution to itself. This was where the aberration of true fiscal federalism started. This became a problem for the new states because all the resources found within their domain were now exclusively under the control of the government at the center. States were now compelled to rely on the federal government for their survival. The various formula generated by successive regimes from that era till 1989 did not address the true nature of how revenue can be distributed in a federal state. There has been lopsidedness on the conditions for sharing the national cakes where some states are better off than the others; even the federal government carting away the larger share of the revenues that accrue to the federation.

Some unacceptable practice was infused as conditions for distributing revenue to the states, like landmass, population size, needs, etc. was a clear violation of the original practice before the military ended the First Republic. This practice did encourage some states to be unproductive and contribute little or nothing to the national wealth. The states that produce the resources, which are the mainstay of the economy, have little or nothing to show up to date. Armed with this observation this paper identifies and discusses the lapses that are inherent in fiscal federalism in Nigeria.

## 2. Fiscal Federalism in Nigeria: A Conceptualization

This section systematically and critically assesses the views and opinions of scholars on fiscal federalism and revenue allocation/distribution in Nigeria. Edame (2001) posited that fiscal federalism has been defined as a method of dividing powers such that Federal and State governments are each, within a sphere, co-ordinate and independent. The federal government is supreme within its sphere and that sphere is defined and limited, and so are the states in a well-ordered and democratic country.

Edame (2005) stated that at independence in 1960, Nigeria was a federation of three powerful regions. Each was provided with a tax base composed largely of revenue easily identifiable as originating from the region. A pooling account was also established for sharing revenues considered to be of national significance such as mining, rents, royalties, customs duties, import and export excise duties, and company taxes. The principles of derivation played an important role in the sharing of pooled resources at this time because the country was concerned with setting the right incentives for tapping local resources and encouraging fiscal responsibility in the regions. This system was abrogated when the four regional structures were abolished by the military, under Gowon, in 1967 and replaced with twelve state structures. It was from this point that problems started creeping up into the fiscal workings of the Nigerian federation. To buttress and consolidate this view, Ihonvbere (2000) made it clear that the first misguided, but a direct attack on federalism in Nigeria was by the military in January 1966 when Gen. Aguyi Ironsi overthrew the democratic government and promulgated Decrees 33 and 34 of May 1966 abolishing the federal system and replacing it with a military form of government (Ihonvbere, 2000, p. 89).

The sudden and unexpected termination of democratic rule by the military initiated a process that steadily eroded the powers of the regions (later states) with the transfer of several items hitherto in the residual and concurrent lists to the exclusive list. However, the first major development that made the dominant political elite at this time rethink its role in the control of the oil industry was the Nigerian Civil war. While the control over oil cannot be said to be at the heart of the Civil war, the contest over the right to revenue payments between the federal government and the government of secessionist Biafra brought to the fore the need for closer control of the industry by the dominant ruling elite. Fiscal federalism was removed when given the atmosphere of the civil war; the ruling elite saw the concentration of power at the centre as a strategy for strengthening the political class and building some platforms for cohesion. In 1967, the military introduce a twelve-state structure to replace the existing four regions and through a series of decrees issued in 1969, set about the process of centralizing fiscal powers, with exclusive powers to legislate on solid mineral, oil, and gas. These decrees completely undermined and subvert the federal bases of association especially the Petroleum Act of 1969 and the Land Use Act of 1970. In 1970, the Federal Military government allocated the bulk of federally collected revenue to the central government, (Ihonvbere, 2000). It also jettisoned the principles of derivation (for each) and a lump sum transferred to cover the fixed cost of running a government in the state allocation. It also introduced a dichotomy between onshore and offshore mining and assigned offshore rent .and royalties themselves. The channeling of all distributable revenues through pool accounts in 1975 expanded the scope of revenue collectible by the federal and shared by the various governments.

In any federal system, there must be an arrangement on how the revenue of the state will be shared among the parts. In supporting this view, Watt (1970) argues that:

> Federal finance is an extremely important and controversial subject because first, it affects the allocation of administrative responsibility. After all, the financial resources available will place limits on the scope of administration which, the level of government can sustain. Second, it affects the political balance because whichever level of government has the major financial resources, funds in its hands the means of political control; third, it is significant also because the assignment of fiscal and expenditure power will determine which governments can use these instruments to control the economy. (Watt, 1970, p. 36)

The observation of Ronald Watts on fiscal federalism and revenue allocation is instructive, particularly for Nigeria. As recognized by him, federal finance is a controversial subject. It also affects the allocation of administrative responsibilities. The percentage of revenue allocated to a tier of government will affect or influence its performance. The assumption of Roland Watts that the fiscal power and revenue allocation will determine the tier of government that controls the political economy is relevant to the situation here.

The nature of fiscal federalism and revenue allocation places the federal government in a vantage position and controls the economy. The economic role of the public sector in a federal policy is the joint responsibility of all tiers of government. But in the case of Nigeria, the joint responsibility of these tiers of government in carrying out the functions of socio-political, administrative, and economic management introduces complications in the nation's fiscal system (CBN, 2000). Fiscal laws in Nigeria tend to give more power to the federal tier of government than the other sub-federal units combined. This creates an increased dependence of the sub-federal units on the federal government particularly for their finances. State and Local Governments are neither given any strong fiscal incentive nor encouraged to generate revenue internally. Given this, they are weak financially, whereas the weak financial base of the States cannot strengthen or guarantee true federalism. As a result, there is discontentment, conflict, and agitation by the two other tiers against the federal government for reliance. It is argued that for any federation to be sustained there must be fiscal decentralization and financial autonomy. However, in the case of Nigeria, there is centralization. Several factors account for this, including the growing importance of crude oil, the Civil war, military incursion into politics the centralization exercise. But the factor that is of immediate concern here is the importance of crude oil and the proliferation of states which, since 1967 has reduced the size and capacity of the states and made them inherently weak and excessively dependent on statutory allocation. It is germane to note that because of the large number of sharing units and lack of independent sources of revenue, the dependence of these units on the federal government has not only virtually impinged on their autonomy but has hindered their capacity to carry out independent development. Moreover, a reduction in landmass is by implication, a drastic reduction in the economic power and activities of the states. In a nutshell, the incessant creation of states, the importance of crude oil and prolonged military rule with its command structure affect Nigerian fiscal federalism. Consideration of revenue sharing will reveal these dilemmas.

Dare (2000) in his postulations was not far from what other scholars have posited. He argues that fiscal federalism deals with the sharing of functions and resources among the constituent units of government in the federation. The basic principle function of sharing hinges on the spatial characteristic of the public service and requires that services whose benefits are localized will be provided by the unit of government that exercises jurisdiction over the benefiting residents, while services whose benefits are shared by the entire citizenry are best provided by the National Government. The implication of this is that the states, under true federalism, should manage whatever resources that lie within their territory while the National Government should deal with the exclusive issues that have to do with defence and foreign policy and other international matters as the need arises. By implication, the funds needed by the federal or National Government in this regard come from the quota contributed by the federating unit given under true fiscal federation.

Ekpo (2001) categorically confirms fiscal federalism as public finance of a state with more than one fiscal tier, notably federal, state, and local government. He further postulates that "much of the literature of fiscal federalism especially those on Nigeria, has been concerned with explaining the pattern of intergovernmental relation or the context of the political economy of possible consequences of such relationship". Going by what Ekpo (2001) said, it becomes imperative to state here that fiscal federalism is not properly practised as it can threaten the peaceful co-existence of the federating units. This has caused much tension since the coming of democracy in 1999 where states in the Niger Delta region have witnessed unrest due to the activities of militants and numerous court cases by these Niger Delta states and the Federal Government over resources and how it is shared. Adebayo (2003, p. 47), writing on the topic under review stated that between 1946 and 1960 when almost every constitutional review was preceded or accompanied by a corresponding revenue allocation exercise, there were eight constitutional reviews as well as eight commissions on revenue allocation, Philipson (1946), Hicks Philipson (1951), Chicks (1953), Raisman (1958), Binns (1964), Dina (1968), Aboyade (1977) and Okigbo (1980); a process which has made Niger to be credited with devising the most sophisticated formula for revenue sharing in any federation.

On assuming office, most regimes in Nigeria, since independence, makes the review of revenue allocation formulae a priority. The one initiated in August 1999 by the National Revenue Mobilization Allocation and Fiscal Commission (NRMAFC) to review the existing allocation formulae including that enshrined in the 1999 constitution, only falls into an established pattern. NARMAFC itself was established in 1989 to review revenue allocation formulae continuously among other things. This shows that at no time had the federating units in Nigeria been contented with the prevailing sharing formula.

Ozo-Eson (2005) argues that fiscal federation concerns the division of public sector functions and finances among different tiers of government. In undertaking this division, economists emphasize the need to focus on the necessity for improving the performance of the public sector and the provision of their services by ensuring a proper alignment of responsibilities and fiscal instruments. While economic analysis, as encapsulated in the theory of fiscal federalism, seeks to guide the division by focusing on efficiency and welfare-maximizing in determining optimal jurisdiction authority, it needs to be recognized that the construction of optimal jurisdiction authority in practice goes beyond purely economic considerations. Political considerations, as well as historical events and exigencies, have in practice, played major roles in shaping the inter-governmental fiscal relations in the most federation.

Judging from what Ozo-Eso said, the issue of putting in place a good fiscal mechanism that will put to rest the much-heated debate as to the best sharing formulae when it comes to the national cake in Nigeria. Since day one the issues of fiscal federalism and revenue allocation have been highly political. Each administration comes up with whatever political arrangement suits them while the main issues of true fiscal federalism are swept under the carpet. clinically put this out when they said that:

> In the context of Nigeria, however, given the historical commitment to the federation as the basis for co-existence and unity, fiscal federalism has long been an important and central feature of inter-governmental relations. Even though the constitution of a stable and acceptable intergovernmental fiscal arrangement has been the subject of various commissions, committees, and other efforts since the amalgamation of Southern and Northern Nigeria in 1914, the issue remains on the front burner today, still evoking a great deal of passion and virulent contestation. The recent stake-mate over this matter in the political Reform conference and subsequent walk-out by the delegate from the south-south attest to this. (Ozo-Eson, 2005, p. 18)

Eje & Orokpo (2014) posit that the term described fiscal federalism is rooted in a political arrangement called federalism as already attested to in previous works. It is the financial relationships between and among existing tiers of government specifically, it is the system of transfers or grants by which the federal government shares its revenue, which is generally referred to as revenue allocation. For more clarity, Eje & Orokpo (2014) went further to state that the fiscal relationship between and among the constituents of the federation can be explained in terms of three theories, namely the theory of fiscal location which concerns the functions expected to be performed by each level of government in the fiscal allocation; the theory inter-jurisdictional cooperation which refers to areas of shared responsibility by the national, state and local government, and the theory of multi-jurisdictional committee (Ozo-Eson, 2005).

Nwankwo (2012) portrays fiscal federation as a usage in federal practice that refers to the fiscal (monetary) relationship between the different tiers of government. This relation revolves around expenditure and revenue matters, and fiscal decentralization. Fiscal federalism is thus expected to be the product of some form of voluntary associations involving certain divisions of responsibilities, functions, powers, and authority. Consequently, fiscal federalism refers to the allocation of resources (vertical and horizontal) among the tiers and component units of a federal state and institutions for the discharge of their constitutionally assigned responsibilities and functions.

This viewpoint is inconsonant with the postulations of other scholars. Fiscal federalism, as it were, is anchored on how the federating components share their responsibilities in line with the resources available in the land. Originally the burden of generating these resources and translating them to revenue lies with the states where these resources are located, but the political environment in Nigeria has reshaped the way things are operated when it comes to revenue generations and resource control.

Antai (2004, p. 76) maintained that the revenue allocation aspect of fiscal federalism is done through the sharing of tax jurisdiction and/or redistribution of federally collected revenue. The general issue to resolve in this respect is revenue sharing among the three tiers of government, in line with their relative function, and between units in the same tier. Ideally, each tier should have adequate resources to enable it to carry out its function. It is, however, difficult to achieve this through the assignment of the taxing power. Two factors, namely, administrative efficiency and fiscal independence, largely influence the assignment of tax powers in a federation. This efficiency criterion demands that a given tax be assigned to the level of government that will administer it efficiently at maximum cost. Fiscal independence on the order hand requires that each level of government should, as far as possible, raise adequate resources from revenue sources assigned to it to meet its needs and responsibilities. Taking a position from Antai's postulation fiscal independence is strongly advocated to be adopted in Nigeria. This will make the component units to be more hardworking and rapid development will be witnessed as it was observed when the four regional structures were in place before the civil war.

Amunwo (2008) averred that in a federal system of government, fiscal federalism in the allocation of taxing power to federally collectible revenue and federal expenditure to the different levels of government in a federation t enable them to discharge their constitutionally assigned function and responsibilities to their citizens. Fiscal federalism deals with the sharing of functions and resources among the constituent units of government in the federation. The basic principle of function of sharing hinges on the spatial characteristics of public services and requires that services whose benefits are localized will be provided by the unit of government that exercise jurisdiction over the benefits residents, while services whose benefits shared by the entire citizenry are best provided by the Nation Government. It, therefore, means that each unit of government should therefore use only the sources of the financial obligation that will enable it to internalize the cost of the services it provides. Essentially, with the centralized provision of service with national benefits, wastage caused by multiple provisions is avoided. In a federation, there is usually a mismatch between the function assigned to a tier or unit of government and its revenue. This stems from the practice of using different yardsticks for assigning functions and allocation of revenue.

## 3. Revenue Allocation/Derivation in Nigeria

Olowononi (2000) broadly defines revenue allocation to include allocation of tax powers and the revenue sharing arrangement not only among the three levels of government but among the State government as well. Under the government's distribution function, it redistributes income and resources to promote national unity and equity. Revenue allocation can be described as a method of sharing the centrally generated revenue among different tiers of government and how the amount allocated to a particular tier is shared among its components for economic development. Ekpo (1993) stated that revenue allocation in Nigeria is a process in which political consideration has been the main determinant, and has been dominated by derivation, population, and equality principles. Between 1950 and 1960 when three powerful regions sought to derive maximum benefits from their natural resources-groundnut cotton in the North, Cocoa in the West, and Oil Palm in the East, the derivation principles were loudly and most passionately advocated, with each region using succession as a redressive mechanism should derivation be discarded. From 1970 to date, with oil assuming the status of the main earner in the economy and with a centralizing military leadership in foisting fiscal centralism in Nigeria, the Deviationists and Anti-derivations have become vociferous in their advocacy (Ekpo. 1993, p. 23).

The creation of states has come to render the principles of equality of population attractive with the 1963 census figure being considered less controversial and representing a more reliable benchmark data than its 1991 counterpart. The Aboyade Panel on revenue allocation 1977 threw all these pre-existing principles overboard and rather proposed "equality of access to development, national minimum standards, absorptive capacity, independent revenue, and fiscal efficiency" – a formula that Shagari's government rejected for being "wearisomely loaded, cumbersome, unconventional and incomprehensible" (Ekpo, 2005). Right from the onset, the principles of derivations as a criterion for horizontal revenue allocation in Nigeria were first recommended by Philipson Fiscal Commission in 1942. Thereafter, it featured prominently in all other fiscal commissions set up by the government. According to the principle of derivation, each region should receive from the central government in proportion to its contribution to the centrally collected revenue. In the views of Phillipson, the recommendation of these principles was informed by the need to promote fiscal discipline in the region.

This principle was attacked because it negates the equity principle due to several factors. Central to the criticism was the lack of accurate statistics on the regional distribution of imported items. The point has been made that the application of derivation promotes regional hostility and disunity because it supports uneven development. It was expressed that derivation principles intend to favour wealthy regions at the expense of the poor ones, and it is not only anti-redistribution, but it also negates the macro-objectives of rapid growth and development. With the emergence of oil, the antagonists of derivation increased with rapidity. The core of their argument is that it favours the oil-producing state. That the unbalanced development could be counterproductive to some groups who are very influential and powerful in suppressing politically powerless minority groups. Finally, it may lead to a shift in political power which would not be. Although the importance of derivation has tapered off for more than a decade, interstate, regional antagonism, discontent, and tension have deepened rather than abated.

## 4. The Problem of Fiscal Federalism in Nigeria

Following the unification of the Protectorates of Southern and Northern Nigeria in 1914 and the establishment of three major administrative regions (East, West, and North), the issue of revenue allocation became very important in both institutional arrangements and political activities of Nigeria. The Report of the Political Bureau notes that revenue allocation "has been one of the contentious and controversial issues in the nation's political life. So contentious has the matter been that none of the formulae evolved at various times by a commission or by Decree under different regimes since 1964 has gained general acceptability. Indeed, the issue, like a recurring decimal, has painfully remained the first problem that nearly thirteen attempts have been made at devising an acceptable revenue allocation formula each of which is more remembered for the controversies it generated than issues settle".

The first Commission on revenue allocation surfaced in 1946. The second Commission reported its findings in 1951, while the third submitted its Report in 1953. The last Commission on revenue allocation during colonial rule was established in 1958. Interestingly, its criteria and recommendations largely formed the basis for revenue allocation till 1967. From 1960 to July 1992, fourteen major revenue allocations Commissions, interim arrangements, Decrees etc., have been recorded as shown in Table 1 below.

**Table 1. Revenue Allocation: Formulae and Computations 1968 – 1989**

| S/N | COMMISSION | CONCEPTUAL FORMULAE | COMPUTED ALLOCATIONS |
|---|---|---|---|
| 1 | Dina. 1968 (Not implemented) | National Integration | 90% of rents and royalties to DPA<br>10% to the State Governments. Insignificant oil rents and revenues given to the Producing States |
| 2 | Decree No. 13 of 1970 | i) Increased Federal share<br>ii) Derivation | 60% of the export duty instead of the former 100% allocation now given to the State Governments.<br>50% of duty on motor fuel instead of the previous 100%.<br>50% of excise duty<br>50% additional rents and royalties on mining for States by derivation also went into the coffers of the Federal I Government. |
| 3 | Decree No. 9of 1971 | Federal Exclusive | 100% of rents and royalties on off-shore oils went into the coffers of the Federal Government. |
| 4 | Other Interim Allocations (1969–1974) | Largely Derivation | 90% of duties from motor fuel went to the State of consumption. 10% to DPA.<br>**On-Shore**<br>45% of mining rents and royalties to the Producing States<br>50% to DPA<br>5% to the Federal Government<br>**Off-Shore**<br>100% rents and royalties to the Federal Government<br>**Excise-Duty**<br>50% to the Federal Government<br>50% to the DPA. |

| | | | |
|---|---|---|---|
| 5 | Decree No. 6 of 1975 | i) Equality of States<br>ii) Derivation<br>iii) Population<br>iv) Pool Account criterion | 20% on-shore derivation for the Producing States<br>80% of mining rents and royalties<br>35% of import duties minus motor spirits, diesel oil tobacco, and wine<br>100% duties on motor spirit and tobacco<br>50% excise duties<br>100% export duties on hides and skins. |
| 6 | Aboyade Technical Committee (1977) | i) Equity of States<br>ii) National Minimum standard<br>iii) Absorptive capacity<br>iv) Fiscal efficiency | Principle Recommended Weighted as<br>Accepted %<br>Equality of access to 025 0.27<br>Development Opportunities<br>National Minimum Standard of 0.22 2.28<br>National Integration<br>Absorptive Capacity independent 0.20 0.20<br>Revenue<br>Tax Export 0.18 0.12<br>Fiscal Efficiency 0.15 0.13 |
| 7 | Okigbo 1980 | i) Equality of States<br>ii) Population<br>iii) Social Development Factors<br>iv) Internal Revenue. | **Allocations among Levels**<br>Federal Government–53%<br>State Governments–30%<br>Local Governments–10%<br>Special Fund–7% |
| 8 | Revenue Allocation Act of 1981 (Nullified by the Supreme Court) | i) Equality (Minimum Responsibility)<br>ii) Population<br>iii) Social Development factors<br>iv) Internal Revenue | **Allocations among Levels**<br>Federal Government–58.5%<br>State Governments–31.5%<br>Local Governments–10.0% |
| 9 | Revenue Allocation Act of 1982 | i) Equality of States<br>ii) Derivation<br>iii) Population<br>iv) Social factor based on direct and inverse Primary School Enrolment | **Allocations among Levels**<br>Federal Government–55%<br>State Governments–35%<br>Local Governments–11%<br>Of the 35% allocated to all States. 3.5% went to the Oil-Producing Areas.<br>1,0% went for the amelioration of ecological damage<br>The remaining 30.5% distributed based on:<br>a) 40% Equality of States<br>b) 40% Population<br>c) 15% Direct and Inverse Primary School Enrolment<br>d) 5% Internally Raised Revenue Effort |
| 10 | Political Bureau (1986) | i) Equality of States<br>ii) Population Federal Government<br>iii) Direct and Inverse Primary School State Enrolment<br>iv) Internal Revenue Generating Effort | **Allocation among Levels**<br>Federal Government–48. 5%<br>State Governments–24.5%<br>Local Governments–20.0%<br>Funds for developing mineral-producing areas–3.0%<br>Special Fund–4.5%<br>*State Distributions:*<br>Equality of States–40%<br>Population–40%<br>Direct and Inverse Primary School Enrolment–15%<br>Internally Raised Revenue–5% |
| 11 | National Revenue Allocation Mobilization and Fiscal Commission (1989) | i) Developmental emphasis<br>ii) View of Local Governments<br>iii) Decrease in Federal & State Allocations<br>v) Population<br>v) Internally generated revenue<br>vi) Social Development based on Primary School Enrolment | **Allocations among Levels**<br>Federal Government–50%<br>State Governments–30%<br>Local Governments–15%<br>Special Fund 5% (1.5% for derivation, 1% for amelioration of ecological damage, 2.5% for others)<br>***State Distributions 1990***<br>Equality of States–40%<br>Population–40%<br>Direct and Inverse Primary–15%<br>(11.25%–Direct<br>School Enrolment 3.75%–Inverse<br>Internally Raised Revenue–5%<br>***Revised States Distributions 1991***<br>Equality of States–40%<br>Population–40%<br>Landmass–10%<br>Internally Raised Revenue–10% |

**Source**: Akinsanya (1989)

The revenue allocation formula in Nigeria is a phenomenon that appears to be in permanent disorder. The ad-hoc and inconsistent revenue allocation principles adopted by various Nigerian governments partly explain the frequent creation or the need for new revenue allocation commissions, the Nigerian nation, a polyglot composition of over 250 different ethnic groups was fused at independence by the presence of competitive regional and ethnic blocs of population and this rendered the issue of revenue allocation one of uncommon intensity. Between 1960 and 1968, the distributional basis of revenue was found anemic, and this necessitated the setting up of a commission to look into the issue Subsequent grievances also led to the inauguration of the two others between 1968 and 1981.

## 5. Revenue Allocation Commissions and Nigerian Fiscal Federalism

A key element of the Revenue Allocation Commissions set up by various Nigerian governments between 1968 and 1989 was the need for necessary and immediate adjustments that would make the revenue allocation principles one that is fair and just.

### 5.1 Dina Interim Revenue Allocation Committee 1968

The creation of new states in 1967 and the issue of equitable distribution of the nation's resources led to the inauguration by the federal military government of the Interim Revenue Allocation Review Committee (IRARC) headed by Chief I. O. Dinna, Permanent Secretary in the Western State. The committee, according to A. Ayida (1973) was to "look into and suggest any change in the existing system of revenue allocation as a whole as well as revenue sources". This committee was set up to correct the problems associated with the recommendations of the Binns Commission. The Committee was specifically commissioned to determine the formula for revenue allocation as far as proceeds from mining rents, royalties, duties on wine, tobacco, and the distribution of funds in the distributable poor account are concerned. This eight-member committee made up of solely Nigerians was constituted under emergency because of the prevalence of the civil war, military rule, and the creation of the state (twelve states) by the military government of the day. Many inadequacies in the Federal structure of Nigeria were identified by the commission some of which were:

(i) The imbalance between fiscal responsibilities and financial capabilities of the state

(ii) The proliferation of authorities vested with powers to raise taxes and incur expenditures from the same revenue Source.

(iii) A wide gap between principles of revenue allocation and actual practice.

(iv) The lack of absence of theoretical guidelines to the problems of revenue allocation and required by the concept of pluralism and the equitable distribution of the nation's wealth. In other that a solution is preferred to the crisis of national development, the

Dina Committee recommended that:

(a) The Federal government should accept frill responsibility for the financing of Higher Education and representation in state-owned institutions.

(b) The Federal Government should assume full responsibility for prisons, public safety and order, and scientific and industrial research.

(c) There should be uniform income tax legislation for the whole country.

(d) The allocation of royalties from onshore mining operations should be in the following order: Federal government, 15% State of Derivation. 10% State Joint Accounts. 70% Special Grant Account; 5%

(e) Royalties and rent accumulated from offshore mining ventures should be distributed financial and pricing policies of the Marketing Boards should be harmonized to guarantee uniformity.

(f) A permanent National fiscal and planning commission vested with wide and effective powers which could be exercised throughout the Federation should be established.

(g) Allocations from state Joint Accounts should be based on the principles of "Minimum National Standards". Need and Balance Development. The Dina Committee submitted its report in January 1969 but at a meeting of finance commissioners of the Federation held in April 1969. Presided over by the Federal Finance Commissioner, Chief Awolowo, the recommendations of the Dina Committee were rejected.

The rejection was predicated on grounds that the committees report produce below shows clearly that the report contains materials that were not relevant to its terms of reference. We have been guided by the principle that revenue allocation must be seen as the essence of an overall financial and economic settlement in which all the governments are motivated and geared to the development of one strong and integrated National economy within the context of a truly united Niger. Thus, we have integrated the National economy within the context of a truly united Nigeria. Thus, we have interpreted our terms of reference in a way we believe will ensure the development of an integrated economy in the country. Fiscal arrangements in Nigeria appear in the past to have been dictated too much by political as well as constitutional development–The politicians who decided to reject the specific pre-commendations of the Dina Committee found de-emphasis on political and constitutional considerations in determining a revenue allocation formula objectionable. However, despite the rejection, the main provision which is the transferring of more revenue from the states to the Federal government was implemented and adopted in the next five years. To affirm the Decrees No.6-7 of 1975 endorsed the weak position of the states and the strengthening of the Federal Government.

### 5.2 The Aboyade Technical Committee 1977

In 1977, the Aboyade Technical Committee on Revenue Allocation was inaugurated by the Obasanjo's regime as part of the plan to return the nation to democratic rule (Bassey, 2005). The Committee recommended the following National Minimum Standard for national integration 22%, absorptive capacity 20%, independence revenue effort 18, fiscal efficiency 15% etc. Also, all collected federal revenue to be paid into the federation account and showed using this ratio, federal government 60%, state 30% and local government 10%. 13% of the federal government share should go into areas in need of rehabilitation and ecological disaster. The recommendation was rejected by the government by claiming that it was too technical.

### 5.3 The Okigbo Committee 1980

This committee was set up by President Shehu Shagari and the outcome of the committee was debated in the National Assembly which came up with the following recommendation; Federal government 58.5%; state government 31.5% and local government 10%, 2% out of 31.5% for the state should go to the mineral producing state using the principle of derivation, also 30% for the development of mineral producing areas in those state. The balance of 26.5% should be shared using the following principles responsibility of states or equality of state 50 per cent, population 40%, land area 10%. The bill was passed by the National Assembly in 1982, a new revenue allocation formula that gave 55 per cent to the federal government, 35 percent to states, and 105 to the local government. Like its predecessors, the Okigbo commission was mandated to examine the existing formula for revenue allocation between the federal state, and local governments, having regard for the need to ensure that each tier of government in the federation had adequate revenue to enable it to discharge its functions as laid down in the constitution of the Federal Republic of Nigeria.

In 1979, the Shehu Shagari administration picked Pius Okigbo to head what was named the Presidential Commission on Revenue Allocation. The setting up of three commissions on revenue allocation within a short period of twelve years was a manifestation of the instability that characterized the Nigerian polity. Between 1968 and 1980, income from petroleum constituted over eighty percent of federal revenue. The importance of the federal centre, therefore, increased proportionately. Because of this major shift in revenue generation, a desperate struggle to win control of state power was ensured since this control meant for all practical purposes being all-powerful and owing everything. The issue of revenue allocation, therefore, became not a matter of pure economics, but a political factor.

### 5.3 National Revenue Mobilization, Allocation and Fiscal Commission (Decree 49, 1989)

By this regime's peculiar circumstances, the revenue allocation principles it inherited, and the format adopted or recommended for it represented a classic case of a travesty of the principle of federalism. It also represented according to Okigbo (1980), a negation of the ideals of the Structural Adjustment Programme (SAP) which the regime introduced in 1986. Thus, to address the equity issue, the Babangida Administration in line with the principles of SAP and Federalism was inaugurated in 1988, the National Revenue Mobilization. Allocation and Fiscal Commission under the Chairmanship of General T. Y. Danjuma(rtd). In December 1989, the government modified and then accepted the recommendation of the commission. The revenue allocation regime that came out of this effort utilized what has been regarded as a cumbersome, static, and arbitrary yardstick to wit:

| | | |
|---|---|---|
| Equality of states | - | 40 percent |
| Population | - | 30 percent |
| Land mass | - | 10 percent |
| Social development | - | 10 percent |
| Internal revenue generation effort | - | 10 percent |
| **Total** | - | **100 percent** |

Philip Ogibo Report, Vol. 1; 1980: 27428

The government added a new dimension of revenue allocation when it gave 2 per cent of the revenue from mineral exploitation in direct proportion to the value of mineral extracted from each state, and another 1.5 percent was allocated to the fund to be administered by the federal government for the development of mineral producing areas of the country (Ekpo, 2004). Although this formula was supposed to be an improvement on the previous formulae, a studious perusal of the formula revealed that it not only retained some of the mistakes or the earlier ones but also introduced obnoxious aspects of its own. First, the act of picking a soldier to head a revenue allocation commission at a period when the action was trying to grapple with the negative effects of command structures was in bad taste. Also, whatever claims the formula may make on equitability, reasonableness and acceptability were circumscribed by its adherence to among others, the low percentage weight it assigned to derivation, and the disproportionate weight given to population and population-related factors about “Equality of States” the introduction of landmass as an index of revenue allocation was also regarded as retrogressive and unfair (Adedeji, 1969, p. 19).

Furthermore, the military rule set in as early as 1966, leading to the creation of twelve states the following year. As observed by some scholars, the creation of more states and local governments was a deliberate ploy by the military to create dependency on the federal government. At present, there are 36 States, a federal capital territory with a near status of a state, and 774 local governments.

According to Ola Vincent (2001, p. 12), before the military rule became entrenched, the following fiscal arrangements were already in place:

- The regions were assigned the proceeds from export and excise while the federal government received the share attributable to the Lagos area.
- Marketing boards were regionalized, and the respective regions retained their operational surpluses.
- Regions were empowered to fix producer prices and also impose sales tax on the produce of the marketing boards.
- Regions were assigned the full retention of mining rems and royalties with a federal tax of 30 percent payable to the distributable pool account (DPA). This was later adjusted to 35 percent in 1957; Regions were allowed to administer and retain income tax on incomes not above 700.00 per annum;
- The federal government collected import duties and corporate income tax: and
- The regional governments determined the relationship between the regions and the provinces.

The implications of these measures were an increase in regional revenue from 17.7 percent of total government revenue in 1945(49 to 41.6 percent in the 1966/ 67 financial year and a decrease in the share of the federal government from 82.3 percent to 58.4 percent in the same period.

The military intervention in 1966 brought new changes as the federal constitution of 1963 was suspended. First, in most instances, the federal government took over state and local government functions for a variety of reasons. Consequently, new tax measures were introduced as follows:

- The transfer of legislation and administration of mining rent and royalties to the federal government.
- Centralization of the marketing boards and administration of all taxes, surpluses and fixing of producer prices by the federal government.
- The vesting of right to revenue emanating from company income tax. import, export, Petroleum Profit Tax (PPT), excise taxes and mining royalties and rents in the centre;
- Introduction of uniform rates in personal income and sales taxes while the states were to administer the taxes; and.
- Replacement of sales tax with value-added tax (VAT) in 1994 and its subsequent transfer to the federal government for purpose of regulation and administration while the proceeds are paid into the VAT account for distribution among the tiers of government.

Subsequently, the revenue potentials of the state governments were eroded, as their sources of revenue between 1993 and 1999 stood at 7.4percent of total revenue while that of the local councils between 1996 and 1999 averaged 6.7 per cent of total expenditure. It can be said that Nigeria stopped operating a truly (fiscal) federal system of government in January 1966 (Edame, 2009).

## 6. Revenue Sharing in Nigeria

Revenue sharing arrangement is at two levels. First, between federal, state, and local councils; and second, between the states and local governments. The Distributable Pool Account (DPA) was established in 1957 and received 30 percent of regional proceeds from mining rents and royalties and 30 percent of federal government imports and corporate income taxes. Amounts outstanding on the DPA were shared among the regions at 40, 31, 24, and 5 percent for Northern, Eastern, Western, and Southern Cameroon regions respectively. The formula was adjusted in 1961 to 42, 32.6, and 25.6 for North, East, and West, following the withdrawal of Southern Cameroon. Further adjustment was made in 1964, after the creation of the Mid-West Region. The formula was 42, 32.6, 18.9, and 63 percent for the North, East, West, and Mid-West, respectively. The acceptance of the Okigbo Commission Report in 1980 made it mandatory for all federally collected tax to be paid into the Federation Account (formerly DPA) except for the independent receipts of the federal government. The vertical distribution formula was adjusted in 1980 to 55. 34.6, 8, and 2.5 percent, and changed again in 1993 to 48.5, 24, 20, and 7.5 percent for federal, state, and local governments and special funds respectively.

The horizontal distribution formula has remained stable since 1981, except for the increase in derivation principle for mineral revenue to 13 percent in 1999. The distribution of revenue among the states and local governments is based on the following principle and weights. These include equality of states and local governments (40 percent); population 30 percent); social development factor (10 percent); mass terrain (10 percent); derivation of mineral revenue, and internal revenue effort (10 percent). Value-added tax (VAT) proceed area so shared among the three tiers of government. Initially, the federal government received only 20 percent of the proceeds to cover administrative costs of the collection while states and local governments received 50 and 30 percent; respectively. In 1996, the formula was revised again to 35, 40, and 25 percent for the federal, state, and local governments, respectively. This formula was further changed to 15, 50, and 35 percent for federal, state, and local governments, respectively. The indices employed for the distribution of VAT proceeds among states and local, governments are derivation (20 percent), equality (50 percent), and population (30 percent).

A major phenomenon in revenue distribution in Nigeria since 1989 is the deduction made for “first charges”. These charges included external debt service, dedicated accounts, such as Joint Venture Companies (JVCs), cash calls, NNPC priority projects, national priority projects, and excess crude oil earnings. This dictatorial practice of “first charges” illustrates quite clearly that the military was not interested in Nigeria operating federalism and its corollary, fiscal federalism. The military believed and operated on the basis that the Federal Military Government owned the country, her resources, and all that dwelt in the land. This is a bogus and pernicious notion. The federation is a cooperative endeavor, so it should be run as such, and its revenues shared equitably among all the stakeholders. Without further ado, the practice of "first charges" should forthwith be abolished now that Nigeria is supposed to be operating a democratic system of government. The principle of "fair shares" at both the vertical and horizontal levels that underlay, however imperfectly, the revenue allocation system under the 1963 Constitution should be reinstated forthwith.

Again, to show that conflict does arise as to the third hypothesis, judicial activism by the Supreme Court of Nigeria played a good role to enforce true fiscal federalism. This involves the determination of the constitutionality of legislative and executive actions which can be declared null and void if they conflict with the constitution. This role of the Judge can be illustrated by the celebrated case of the Attorney General of Bendel State Vs Attorney General of the Federation and 18 others (1983, 6 Sc.8) – Revenue Allocation Formula. The plaintiff, the Bendel State Government inter alia sought:

(a) A declaration that sub-sections 1 and 2 of the Allocation of Revenue (Federation Account etc.) Act 1981 is unconstitutional and void in so far as the said sub-section makes provision for a fund to be administered by the Federal Government.

(b) A declaration that the Government of Bendel State is entitled to have from time to time a true and correct statement of all monies paid into the Federation Account kept under section 149 of the 1979 Constitution (Egonmwan, 2000).

From this perspective, one observes that a Federal Government such as ours is a government of delegated powers. The Federal Government has neither landmass directly nor the power of its own unless a source for it is found in the Constitution. But where power has been granted the federal power and authority is supreme. The granting of power of collecting large revenues to the Federal Government has led to what some critics described as a "federal octopus". Thus, the fiscal domination of state and Local Governments is associated with the constitutional granting of the "power of the purse", to the Federal Government. The State and Local Governments which own the resources by natural location become dependent on the "federal octopus" for resource transfers and sharing. However, it is to be realized that once a federal union has been forged, all resources within the federated territory belong to all units, the location of the resources notwithstanding.

## 8. Conclusion

Fiscal federalism has been a perennial problem, particularly because of different levels of resource endowments among different levels of government and partly because of intergroup struggles to have an adequate and fair share of the central revenue. The persistent agitation of resource control and true fiscal administration by the rich states and ethnic minorities of the South-South geopolitical Zone can be ignored only at great cost to national unity. The people are interested in the development achievable with revenue. As such, the political leadership of Nigeria should be committed and patriotic and stop cutting corners when the issue of trace federalism is on the table for discussion. This is the only way Nigeria can witness positive peace and equitable development. Political instability leading to political corruption in the country is often the direct product of the tensions over resource allocation and control in the country. Moreover, the inter-tier distribution of revenue has been lopsided, and the revenue allocation criteria often reflect sectional, rather than national interests. The two lower tiers of government have been treated as mere appendages with highly restricted revenue powers rather than a part of a truly federal system whose fiscal autonomy is guaranteed.

The federal power, as currently constituted, has predicated a high level of distrust among the people. This is evident in the persistent pressure on the government for deregulation, privatization, liberalization, and greater private sector participation. The federal government seems to have accepted the idea of a private–sector-led economy but remains unyielding in changing the intergovernmental power structure. This derives from its misperception of the call for devolution of fiscal responsibilities as a design to weaken the centre. Devolution of power should not be seen as a calculated attempt to weaken the centre, but rather as an approach to limit the direct involvement of the federal government in the provision of goods and services across the country. To correct the situation, there should be a redefinition of the statutory roles of each tier of government and a modification of the current fiscal jurisdiction. The changes must be reflected in a new Nigerian Constitution if the country is to achieve fiscal sustainability, balanced development, and equitable distribution of the federation revenue in the years ahead.

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