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Fiscal Federalism, Governance and Internally Generated Revenue: Examining Weak Subnational Finances in Nigerian States

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Abstract

One of the most crucial challenges to Nigeria's ailing fiscal federalism is the inability of states to raise, retain and manage revenue. Revenue bases at both national and sub national levels are small, volatile and monolithic. But it seems Nigeria suffers the most at its subnational levels. Sub national governments in the country perennially complain of lean resource base relative to their huge fiscal responsibilities. Interestingly, while a lot has been written about intergovernmental fiscal relations and the need for improved allocation to states and Local Governments from the Federation account, not much attention is paid to the management of available funds in states across the country, nor the perpetual inability of states to tap into available resource base through improving their internally generated revenues. This is particularly so for the group of five states in South East Nigeria; which though with some of the best potentials in the country, continue to rely exclusively on the federation account. Beginning with an evaluation of selected indicators of fiscal health, this study examines challenges facing internally generated revenue and taxation system in these states. It argues for closer interaction between government and the private sector to jointly develop industries that will form the base for internally generated revenue.

Keywords: Internally Generated Revenue, South East Nigeria, Fiscal Reform

I. Introduction

Relative to theory and international best practices, Nigeria's fiscal federalism presents multiple paradoxes. Not only are the current provisions of inter-governmental fiscal transfers and management counter-intuitive, they have within them the seed of perverse incentives for the federating units. The country's internal boundaries are continually adjusted in response to agitations for more state creation. Nigeria is a federation in constant evolution and re-creation. There never has been, nor does it seem there is ever going to be, any certainty with regard to the number of states Nigeria will end up having.

Strangely, the incentive for such boundary adjustments is hardly improved economic viability and capacity of existing or the to-be-formed entities to operate. They are rather encouraged as a means to increase the agitating group's access to the 'national cake'. The creation of the first 12 states from the existing 4 regions is seen by many analysts as a means by the Central Government to keep Nigeria united in the face of intense pressures from the powerful regional governments of the first Republic. But soon enough, other motives for state creation set in. Slowly but surely, the number of states in the federation continues to rise – from 12 to 19; to 21 and then to 36 plus the Federal Capital Territory as currently exist. Even with many of the states presently near bankrupt and incapable of even the most basic service provisions, applications and considerations are at advanced stages at the Federal Senate for the creation of more states. But more worrisome, there is neither an understanding of what the optimal number of states in the country should be, nor are there defined criteria for carving out new units. It seems all considerations relating to state creation are initiated and ultimately concluded at the realm of politics. Economic implications, if ever considered, usually come as afterthought, long after the political quest has been satisfied; at which time, it is mostly too late to effect any meaningful changes.

Understandably, exclusive attention to revenue sharing and access to federation account leads to creation of states that do not have the support economic base for independent survival. Indeed, the very existence of the states in all but few exceptions is put into serious question. It seems not to be a matter of 'if' but 'when' the current system will fail. With the whole idea behind the emergence of states being to ensure better access to the oil cake, basic economic sustainability considerations are generally thrown overboard in the geographic and demographic design of states. Unfortunately too, even after creation, the states hardly move to increase internal revenue generation outside of oil accruals. In many states, there is little, if any industry. Taxation systems for the few existing industries are chaotic, irregular and inimical to the existence of the industries. The usual collaboration between businesses and governments is nearly non-existent in many states in Nigeria and sub national governments prey upon the few businesses existing in their domain. Multiple and arbitrary taxation by all tiers of government literally place such burdens on businesses as to threaten their existence.

Despite the above, the fiscal space of states has improved since the return to democracy in 1999 and the trend is towards increasing relevance of states. Sub national governments (including Local Governments) outspent Federal Government between 2003 and 2007 by a ratio of 52:48 on the aggregate and a ratio of 60:40 in capital expenditure. Within the period also, states and local governments, on the average, accounted for 54 percent of total public expenditure on health and 52 percent of expenditure on education. So it becomes necessary that thoughts be channeled towards making the states work. For a long time, discussions on Nigerian federalism have focused exclusively on appropriate methods for distributing oil wealth. Whether among politicians or academics, the issue of concern has often been the determination of proportion of accruals that should go to each tier of government and the justification for such appropriations (Ekpo 1999). While such discussions are relevant, the country's changing economic fortunes due to oil price dips and the need to maintain revenue from sustainable sources demand that considerations be given to options for improving states' capacity for independent funding through internally generated revenue. This is what this paper is about. The discussions are based on internally generated revenue spreadsheets obtained from senior government offices of the five states in South East Nigeria.

The discussion of the results from the field is premised on the broader challenge for improved accountability and capacity for fiscal management in many states. The analysis is based on case study of the five states of South East Nigeria - Abia, Anambra, Ebonyi, Enugu and Imo States. These states represent huge untapped possibilities. The region hosts some of the most innovative human capital in the country and its residents are more intensely engaged in real sector productivity relative to the rest of the country. Despite these, governance among states in the region currently lag many other otherwise less gifted states in the country thereby mirroring the challenge of non-performance in the face of a spectrum of potentials and resources that characterize the larger Nigeria. But in addition, it has severally been acknowledged in both policy and academic circles that the South East holds the key to Nigeria's industrialization, economic growth and development. So it becomes important the workings of government in the region are evaluated.

The rest of the paper is organized as follows: section II discusses the broad issues in fiscal federation in both theory and practice. Section III presents fiscal governance in the five South Eastern states and their implications for raising internally generated revenue. Section IV analyzes data from internally generated sheets of the five states and raises issues for growth and development while section V examines the future of IGR and economic growth given the trends in data and concludes.

II. Theory and Practice of Fiscal Federalism and Revenue Assignment

Discussions about internally generated revenue of sub national government are located within the framework of the theory and practice of fiscal federalism. The rationale for sub national governments derives from the notion that there are geographical dimensions to pure and impure public goods. Local public goods with limited and differential spatial incidence of benefits might not be efficiently provided by a central government (Brown and Jackson, 1994, 255). But two challenges emanate from an economic efficiency perspective of the division of responsibilities and powers of federating governments. First, sub national groupings and local boundaries naturally come with history and geography and are hardly the outcomes of economic efficiency considerations. This leads to the second challenge that even where there are clear delineations of what is pure or impure public goods; they cannot be equitably allocated across all geographical boundaries within the country. As such, the need for deliberate assignment of fund raising, spending and policy powers arises in a fiscal state.

One of the oldest models for responsibility and revenue assignment and sharing among different tiers of government is the Tiebout-Musgrave layer cake model (Musgrave, 1969; Tiebout, 1961). Under the model, stabilization and distribution functions are natural functions of the central government while lower tiers of government take on resource allocation. Given that sub national governments do not have monetary and interest rate policy instruments at their disposal, expansionary fiscal policies would lead to fiscal deficits with improbable financing options and therefore unsustainable debt. In addition, given the high openness and diffusion of resources among the regions within the country, expansionary fiscal policies at subnational levels will result in high leakages thereby thinning out the overall impact of the locally initiated stimulus. Besides, there may be a beggar-thy-neighbour effect arising from other subnational governments pursuing the same set of policies, all in a bid to attract resources to their domains. This, no doubt, leaves the entire system without a net gain; maybe significant income redistribution from governments to the private sector through reduced taxes and increased expenditures, maybe a relocation of a few industries at first and reverse relocation later, but ultimately a zero sum impact on economic growth. Thus, the argument remains that central governments should retain instruments and powers for stabilization while subnational governments are allowed to deliver on resource allocation.

Four areas of assignment of responsibilities create the most challenge for federating units –expenditure assignment, revenue assignment, inter-governmental transfers and the control of sub national debt. The need to determine the share of responsibility that maintains optimal balance in principles of federalism and ensure that units grow at their best while the centre is not rendered ineffective remains a knotty issue. In particular, revenue generation and retention often define the balance of power among different tiers of government. Expectedly then, assigning revenue powers to each tier of government remains a thorny issue and the final outcome in any federating unit depends critically on the history and evolution of the system. On the one hand, the need for the central government to maintain control of macroeconomic performance and reduce regional allocative imbalances and distortions is a key consideration. On the other hand, without effective revenue powers, states and political gladiators at sub national levels may become fiscally impotent, making it difficult to hold them accountable for constitutionally assigned responsibilities. Besides, determination of taxes to be levied should be defined by regional economic realities.

It is largely agreed in the literature (see Guardia and Sonder, 2004) and generally adopted as international best practices that central government's tax base should be unevenly distributed. Central taxes on more mobile bases as well as bases that are sensitive to economic activity will help to reduce tax wars among sub national governments that can lead to inefficiency in factor allocation as well as serve as stabilization instruments. Assignment of sales taxes depends on the nature of tax adopted by the country while it is agreed that personal income taxes are more natural with sub national governments. The eventual decision on this, it is opined, should depend on level of information sharing among sub national governments. Often though, socio-political and economic exigencies and of course country history, translate to tax assignment arrangements that fall short of considerations for efficiency. These areas are independently evaluated in greater details by Ter-Minassian (1997) on the broad macroeconomic implications of such fiscal relations as well as by Ahmad et al (1997) on assignment of expenditure responsibilities; Norregaard (1997) and Vehorn and Ahmad (1997) – on tax assignment and administration respectively. Such other authors as Ahmad and Craig (1997) and Ter-Minassian and Craig (1997) have also independently evaluated intergovernmental transfers and control of subnational borrowing respectively.

Overall evidence on the impact of revenue and expenditure decentralization for developing countries points to varying experiences. Ter-Minassian (1997) for example, tried to pay attention to three aspects of decentralization namely expenditure assignments, taxation powers, and intergovernmental fiscal transfers and covers such countries as Argentina (Schwartz and Liuksila, 1997), Colombia (Ahmad and Baer, 1997), Ethiopia (Brosio and Gupta, 1997), South Korea (Chu and Norregaard, 1997) and Mexico (Amieva-Huerta, 1997). The general consensus from the diverse authors in the collection is that arrangements among developing countries differ widely and range from the constitutional to the ad hoc. The diversity in arrangements also leads to diversity in outcomes with a number of developing countries not reaping the full benefits of fiscal decentralization. But it is also largely agreed that it is not simply a matter of the specific arrangements in place but also the overall trends in fiscal discipline, control of sub national expenditure systems as instruments for macroeconomic coordination and stabilization. In nearly all cases, there are concerns about not giving enough taxing powers to sub national governments in a manner that balances their expenditure assignments to revenue sources available to them. Often, the case is for the former to be larger than the latter, making them largely dependent on intergovernmental fiscal transfers especially from the central government.

A number of studies have been conducted on Nigeria's fiscal federalism. These range from analyzing revenue and expenditure decentralization and financial autonomy of the different tiers of government as in (Agba and Obi, 2006; Ekpo 2004; Adesopo and Asaju, 2004; Jimoh 2003) to Local Government Financing. In Nigeria, the term 'resource control' has almost come to assume a life of its own, defining the contention between proponents of increased revenue devolution and federalists who fear that accountability is still too weak at the sub national level to allow for such high devolution. Agba and Obi (2006) for example analyzed data on the federation account in relation to the unending contention about allocations to the different tiers of government. They calculated indices of revenue and expenditure decentralization and financial autonomy of the three tiers of government and concluded that expenditure power is concentrated at the federal government. They identified the usual non-correspondence between revenue and expenditure assignment especially to other tiers apart from the federal government and recommended conscious effort to allocate more revenues to the sub-national governments.

Few works have documented Nigeria's long history of struggle to find a lasting formula for intergovernmental revenue and expenditure relations among the three tiers of government in Nigeria as much as Ekpo and Ndebbio (1996). Their work presents a classic historical assessment of the journey to a mutually accepted revenue and expenditure assignment criteria from the days prior to Nigeria's independence. The work chronicles the different fiscal commissions that have been set up in the country including the Phillipson Commission of 1946, the Hicks-Phillipson Commission of 1950, the Louis-Chick Commission of 1954 and the Raisman-Tress Commission of 1958 all prior to independence. Immediately after the constitutional declaration of Nigeria as a Republic, the journey started off from where it stopped with the Binns Commission of 1964; Interim Revenue Allocation Review Committee of 1969, the 1977 Technical Committee on Revenue Allocation, the Okigbo Commission of 1979 and the Danjuma Commission all prior to the fourth Republic. Ekpo (2004) draws significantly from this earlier work to conclude that though the formulation and implementation of fiscal relationships in the country have been guided by the principles of federalism, intergovernmental fiscal relationships in Nigeria has been anything but smooth and requires commitment from stakeholders for it to be continually fine-tuned. Part of the challenge is constitutional. Meanwhile, procedures for constitutional amendments can be quite complicated, leading Suberu (2006) to advocate a non-constitutional renewal approach to the solution of the fiscal question in Nigeria's federalism.

III. The Context –Fiscal Management among States in the South East

If fiscal federalism appears challenging for the rest of Nigeria; it is even more so for states in the South East. Among the regions in the country, the South East receives the least resources from the centre and is in deficit even by its population which is perennially underestimated. But even then, there is little evidence of effective management of available resources by governments in the region. Internally generated revenue (revenue assignment) is a component of the broader fiscal relationship challenge facing every federal system. So we take the next few paragraphs to examine the fiscal system in the five states of the region. Attention will be paid to the budgetary and expenditure monitoring system that underpins fiscal responsibility. The data for the analysis is drawn from a policy and business environment assessment of Nigerian states conducted in 2007. The format of presentation for each indicator will be to show the scores of the 5 south eastern states relative to a couple of best performers from outside the region as well as the national average on each indicator. Interestingly, average performance of Nigerian states on most fiscal management questions is not laudable. So the 'best performers' that are shown in the charts are simply those that performed relatively more creditably than others and not necessarily those that can be used as benchmarks for excellence in the indicators shown.

One of the major areas investigated is availability of coherent fiscal strategy in the states. Figure 1 shows the relative performance of the states on the indicator. The first five columns show the South Eastern states in alphabetical order; the next 3 (blue) columns show the best three performing states outside the south east region while the last column shows the national average. As can be seen, only Enugu scored up to 40 percent and compares favourably with the average score for Lagos, Adamawa and Delta, which performed relatively well. Anambra comes next after Enugu in the region with 25 percent score. The national average performance on the indicator was a paltry 17.5 percent. Yet three out of the five states in the region – Abia, Ebonyi and Imo – had scores lower than this national average. This implies that there is no fiscal strategy in these three states.

Budget release and reporting among the states is in no better shape (Figure 2). Both Abia and Anambra have absolutely no mechanisms for timely release of votes or reporting spent funds. Ebonyi and Imo performed better than Abia and Anambra but not better than the meager 28 percent national average. Enugu remained relatively more stable than others though with about 40 percent score on the indicator. However, there are still states outside the region like Gombe, Adamawa and Yobe that scored 90 percent and above, indicating that whatever challenges the South Eastern states had on this indicator are not insurmountable – some states in the country had surmounted them.

Preparation and auditing of public accounts are also neither institutionalized nor regularly conducted. Where such accounts are prepared and/or audited, the state House of Assembly or any other oversight body do not take any action to address shortcomings in the expenditures exposed by audit reports.

Figure 1: Performance of SE Region on Availability of Fiscal Strategy

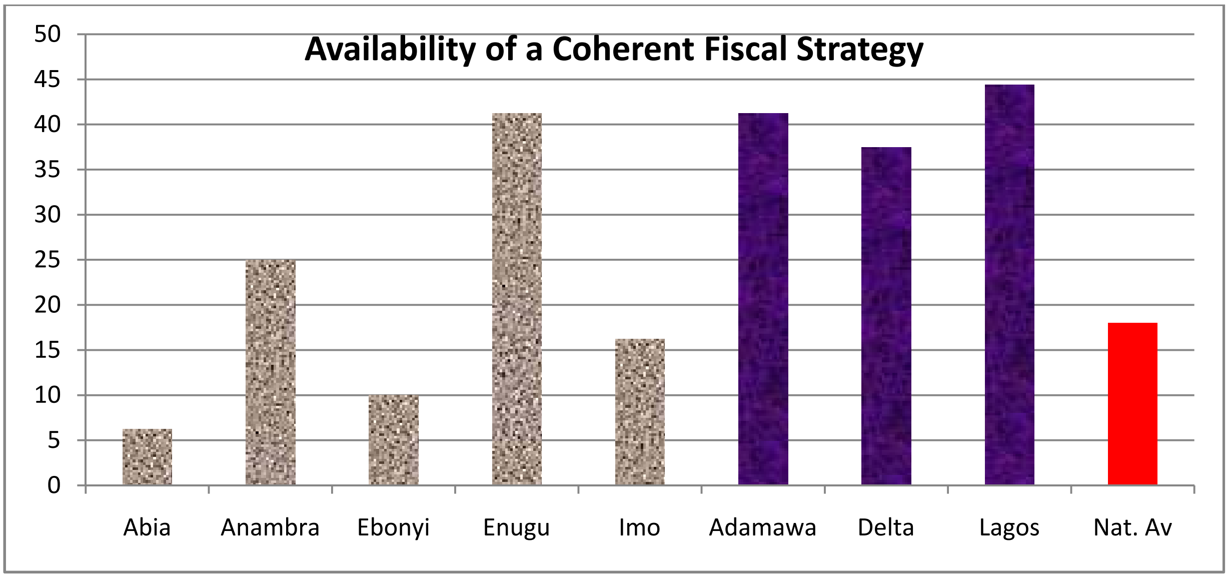
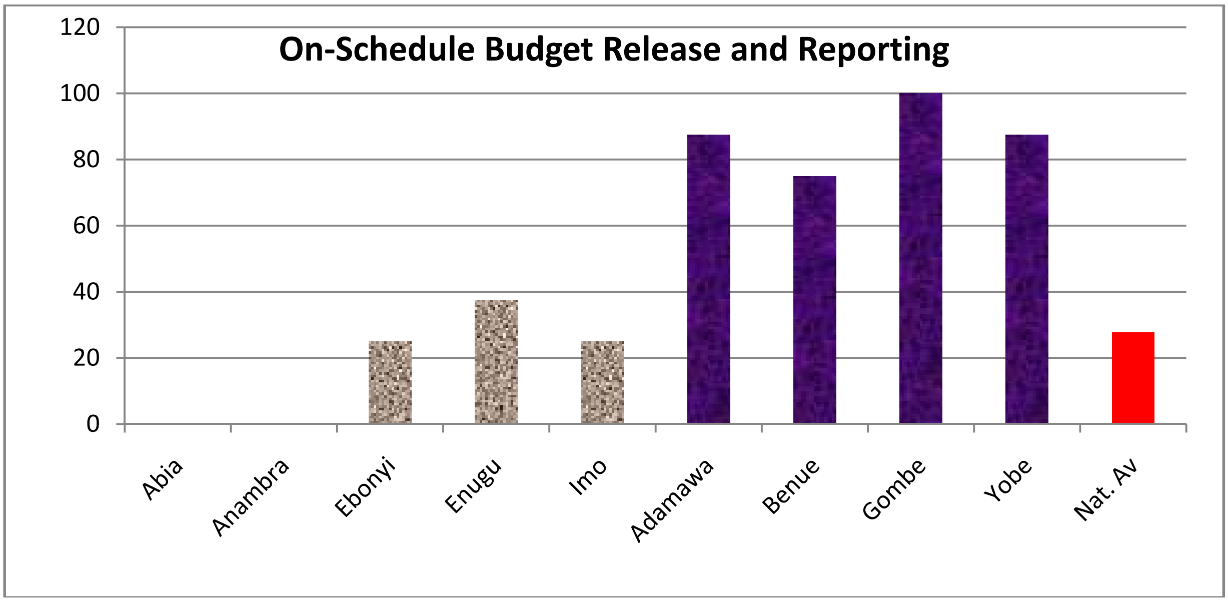


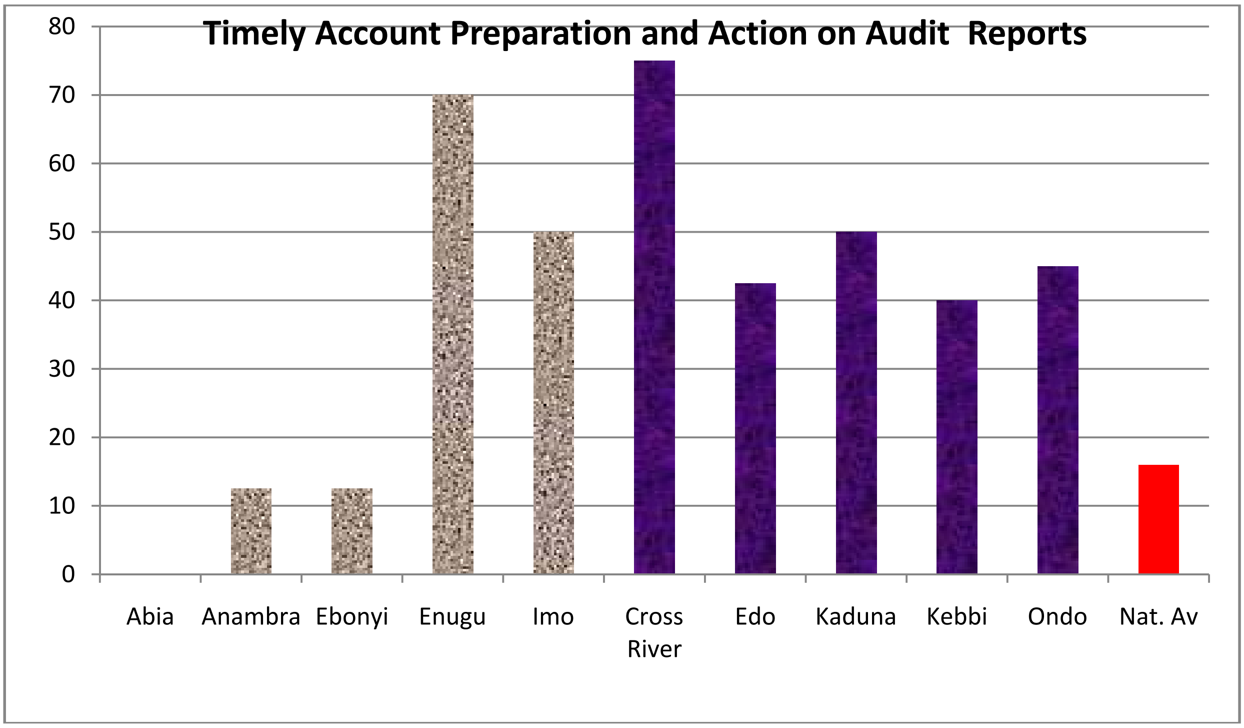
Figure 2: Performance of SE Region on Timely Budget Release



The next indicator aims to evaluate audit regularity as well as actions taken on audit reports by oversight bodies. Part of the requirement of this indicator is that in addition to evidence of certified audit reports for each financial year, there should be evidence that such bodies as the state House of Assembly, which are constitutionally empowered, to monitor and act on audit reports should have done so. In nearly all cases as in previous indicators, it is a requirement that such evidence should be documented. Partial scores were awarded to states that had evidence of audited accounts but could not prove that recommendations from the audit had been acted upon. In this indicator, we see significant floundering among the states (Figure 3). Abia state, for example, had a zero score, implying that there was no evidence of audit of state accounts. Others like Anambra and Ebonyi which had fairly more consistent fiscal strategies as well fared poorly on this indicator. In fact, cases abound of some states that had no audit reports eight to ten years prior to the assessment and this showed up in the national average which stood at a little above 15 percent score. It also seemed most of the State Assemblies were not very concerned with monitoring audit reports either. Enugu and Imo respectively with scores of 70 percent and

50 percent fared much better than the rest of the states in the region. But states like Cross River, which is outside the South East region, set the pace for others.

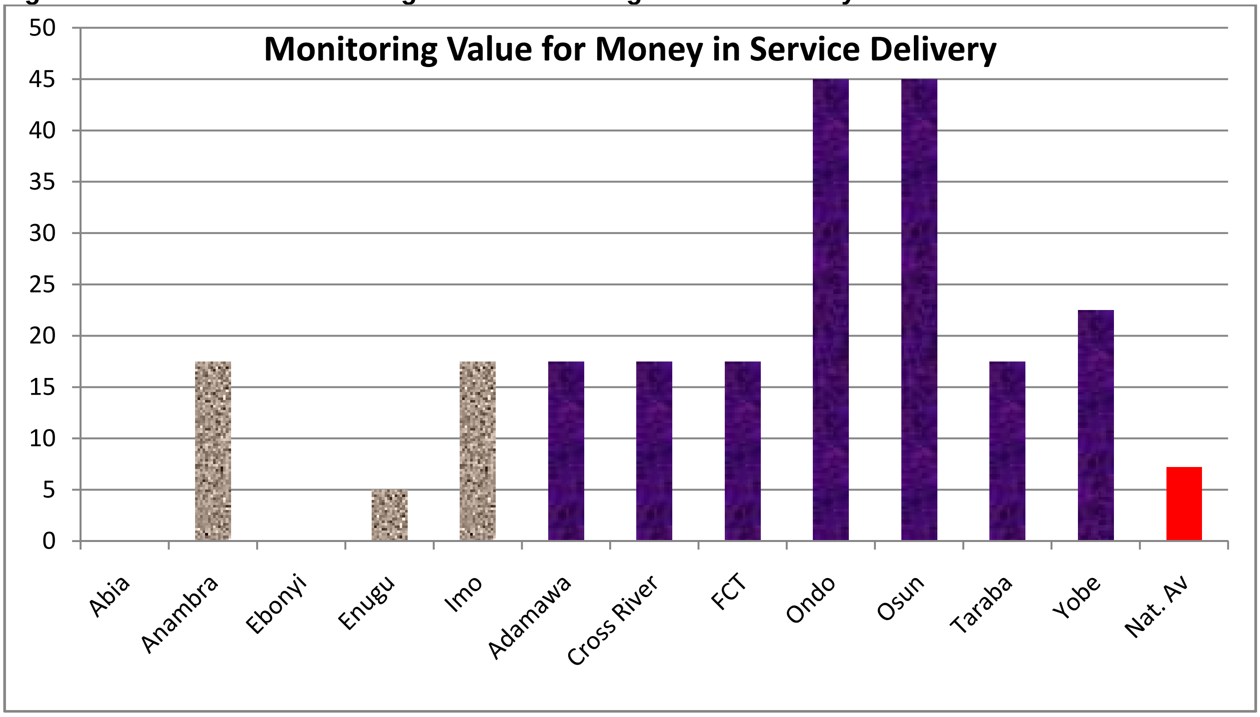
Figure 3: Performance of SE Region on Accounting and Auditing



The same trends are evident on the indicator requiring evidence of monitoring value for money in service delivery on government projects. In fact, it seems few states in Nigeria, and really no state in the South East, take such value for money monitoring serious. Interestingly, one of the sad commentaries of the Nigerian federation since the oil boom of the 1970s is the multiplicity of partially or wholly unexecuted contracts, abandoned projects and failed initiatives. Many of these (as well as successfully concluded) projects are executed at multiples of their market costs, and often with far lower qualities than would obtain in the private sector. It is fashionable for state officials to quote amounts spent on projects as evidence of achievements instead of specifying outcomes or outputs of such expenditures. This indicator therefore aimed to assess the institutional mechanisms put in place in states to get the public sector to relate public expenditures to intended targets and ensure that effective value is obtained for funds spent. Performance in the indicator turned out worse than in any of the previous indicators (Figure 4). Abia and Ebonyi states, for example, scored zero and even Enugu could not score more than 5 percent. Anambra and Imo managed to scrape up 17.5 points apiece. Outside the region, Ondo and Osun in the South West region, scored 45 percent apiece followed by Yobe in the North East with 22.5 percent and the quarto of Adamawa and Taraba (North East), Cross River (South South) and Abuja Federal Capital Territory with 17.5 percent each. The hilarious national average score of 7.5 percent is evidence that Nigeria's premier position in abandoned projects is by no means an accident. It is a natural outcome of a system riddled with poor planning, poorly supported implementation and weak value for money monitoring system. Virtually every state in the federation is a culprit, and states in the South East seem to fare particularly badly. Best performing states in the indicator are Ondo and Osun, both in the South West, and they have no more than 45 percent each.

In sum, sub national fiscal management is weak in Nigeria, but in a number of indicators, South East states lag much behind far less endowed states in the country. The national average in all but a few indicators is very low. Yet majority of states in the South East region still performed below these weak national averages. For example, the national averages in the two indicators – availability of coherent fiscal strategy and timely preparation of accounts and action on audit reports – were quite meager at only 17.5 percent. Yet three (60 percent) of the five states in the region scored below these averages. Only one state scored marginally above the 28 percent national average in on-schedule release of budgeted votes and reporting same. The rest were below the average with two states scoring zero. The national average in monitoring value for money in service delivery was only 7.5 percent. Yet another 60 percent of the states in the region (two of which scored zero) fell below that. There is also little consistency among the states in performance. Relatively good performers in any one indicator fall short in others.

Figure 4: Performance of SE Region on Monitoring Value for Money



Clearly it will be difficult to imagine that such weak fiscal management system would not impact the taxation and internal revenue generation. Without struggling to prove a cause-and-effect relationship, we simply try in the next section to show the state of internally generated revenue among the five states in the region. Of course, it is logical to insist there is a relationship between overall fiscal position of a state and its ability to raise and utilize internally generated revenue for growth, but we try not to belabor this relationship. The reader can make his judgment as we together go through the next sections.

IV. Findings on Internally Generated Revenue in the Region

Given that generation and management of internally generated revenue (IGR) are simply components of overall fiscal strategy of a government, it is natural that such weak fiscal statistics as we have seen in the preceding section should also produce weak internally generated revenue statistics. The inconsistencies in fiscal management should translate to inconsistencies in IGR management and overall performance. It might be unrealistic to expect that IGR strategies will be more consistent than overall fiscal strategies. With a predatory government, this is possible. But it requires that government is able to put its acts together enough to systematically exploit revenue sources while keeping the attention of the private sector from its profligate expenditure profile. But then these are all assumptions. In this section, we explore actual IGR performance in relation to these assumptions. The aim is to evaluate the consistency or otherwise of the IGR policies and programmes and to see if the trends in IGR management reflect the overall weak fiscal strategies of the states. The discussion in the section shall be issue-based though examples are drawn from specific state or group of states at each point.

Table 1 presents a summary of IGR in the South East. Some of the items covered include estimated IGR in millions of Naira (column 2), actual IGR in millions of Naira (column 3), actual IGR as a ratio of estimated IGR summarizing proportional success achieved in realizing IGR goals of each state (column 4), each state's IGR as a proportion of the IGR of the entire region (column 5), population of each state in millions (column 6), proportion of the region's population in each state (column 7) and no of local governments in each state (column 8). From the table, it can be seen that the highest IGR estimate is usually by Imo State with nearly four times its actual IGR revenue as estimated revenue. Data was not available for estimated revenue for Anambra. However, in terms of actual collection, Anambra tops the list collecting as much as 32 percent (NGN 6.1 billion) in regional internally generated revenue. Imo follows closely with NGN5.4 billion internal revenue collection representing 28.4 percent of the regional IGR collection. Abia comes next with NGN3.2 billion or 16.9 percent of regional internally generated revenue followed by Ebonyi with NGN2.3 billion representing 12.3 percent of regional internally generated revenue while Enugu is the least with NGN1.98 billion internally generated revenue representing 10.4 percent of the region's IGR.

While the distribution is a bit surprising given the structure of population distribution in the region, a lot of the data is easy to explain by the level of economic activities going on in each state. Anambra state has the highest population (though it is the least in landmass) and constitutes about 25.5 percent of the regional population. However, its 32 percent share of internally generated revenue is much higher than its share in the regional population. The difference represents the generally more intense level of economic activity, higher income level in the state and possibly greater government efforts to raise internally generated revenue. Anecdotal evidence indicates that Anambra, for example, has the highest income per capita among all states in the country. So the level of income welfare is much higher, constituting a larger tax base for the state than exist in other states of the region. Imo state is home to 24 percent of the regional population, but it posts 28.4 percent of regional IGR which, again, is also higher than its share of the regional population. However, it is more difficult to explain Imo state's performance purely on the basis of higher economic activity. While reliable data on state GDP is not available, it is doubtful that Imo state has higher income per capita or more business activities than Abia or even Enugu state. Abia state hosts some of the most burgeoning markets (the Ariaria and New markets) and formal industrial concerns, which are widely influential not just in the country but across the continent. Anecdotal evidence suggests that the state is second to Anambra in per capita income level as well as the level of economic activity in the region. Even though it has much less population compared to Imo, its distant third position in IGR collection is a lot more difficult to justify than in other cases.

The performance of Ebonyi relative to Enugu is probably the most striking. Ebonyi state is understandably the least developed part of the region and boasts also the least income per capita among the five states. Economic activity in the state is also mostly agrarian, agro-based or natural resource dependent. It also has the least population, having over a million persons less than the population of Enugu state. So it is baffling that its IGR is higher than that of Enugu except if the blame is to be placed at the doorstep of data or weak government efforts on the part of Enugu to raise its IGR. Indeed, though it is a highly commercial state, Abia state is still much lower than Enugu state in population. It is also not possible to tag Enugu a state without much economic activity; the fact that its kind of economic activity is slightly different from what exist in Anambra and Abia states notwithstanding. While economic activities in Anambra and Abia are mostly commercial and partly industrial, basic economic activity of Enugu state is concentrated in the services sector, particularly those relating to education, real estate and public service. However, the size of the services sector in Enugu is substantial enough to warrant significant competition with the duo of Anambra and Abia. But this does not seem to show in the government finances sector. The economy of Ebonyi state is known to be concentrated around the primarily sector and does not have much of developed secondary and tertiary activities. So it is wholly strange that it outperforms Enugu state in internal revenue.

Table 1: Relative IGR and Population Shares of SE States

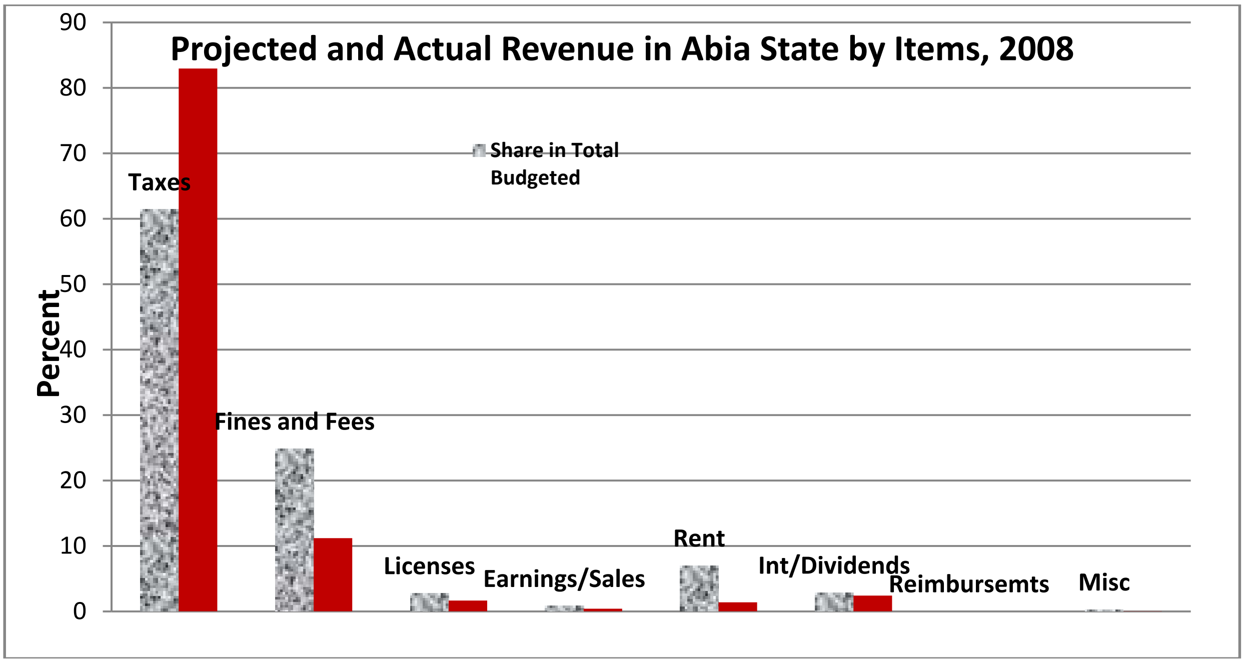
State	*Estimated IGR (Nm)*	*Actual IGR (Nm)*	*Actual/ Estimated (%)*	*% of Actual in Regional IGR*	*Pop (millions)*	*% of Regional Popn*	*No of LGs*
Abia	3,511	3,193	91	16.86	2.83	17.29	18
Anambra	-	6,056		31.97	4.18	25.53	21
Ebonyi	1,837.75	2,334.22	127	12.32	2.17	13.26	12
Enugu	8,205.13	1,976.89	24	10.44	3.26	19.91	16
Imo	18998.17	5,383	28	28.42	3.93	24.01	27
Total/Av.	24,347	18,943	67.5	100	16.37	100	94

There is significant skewness in revenue sources of the states. Revenue sources for states range from income and other taxes to dividends and repayments from investments. However, there is clearly inadequate exploitation of many of these sources of income and over-exploitation of others. This is buttressed by the huge discrepancies among revenue sources and the near complete reliance on one or two internal revenue sources. In addition, gyrations in inter-temporal performance of the revenue sources are too huge for comfort. Table 2 and Figure 5 show the item composition of internally generated revenue in Abia State. As can be seen from the table, about 83 percent of all income from internal sources is from taxes. Meanwhile such sources of income like earnings and sales and even rent from government property, interest repayments and other sources have proportions of between 0 and 2 percent of all income. Approved projections for income from rent on government property in the 2008 budget, for example, was as huge as NGN245 million representing 7 percent of all projected income. Yet realizations from that source was only NGN44 million representing only 1 percent of actual overall revenue. It is difficult to imagine that there were no government properties that were to be rented based upon which the projections were made. The question bothers on what could have happened to such properties and why they were not able to yield more than 18 percent of projections.

Table 2: Approved and Actual Internal Revenue by Item Heads in Abia State, 2008

Revenue Heading	*Estimates 2009 (N m)*	*% of Total*	*Actual Revenue, 2009 (N m)*	*% of Total*	*Difference b/w Actual and Budgeted*	*% Perfor mance*
Taxes	2,156.97	61	2,648.87	83	491.91	122.81
Fines and Fees	872.88	25	357.51	11	-515.37	40.96
Licenses	96.79	3	52.9	2	-43.80	54.75
Earnings and Sales	28.93	1	12.58	0	-16.36	43.47
Rent on Govt Property	245.42	7	44.16	1	-201.26	17.99
Interest Repayments and Dividends	100.00	3	76.50	2	-23.50	76.5
Reimbursements	0	0	0	0	0	0
Miscellaneous	10.00	0	0.34	0	-9.66	3.41
Total	3,510.99	100	3,192.95	100	-318.04	90.94

Figure 5: Budgeted and Actual IGR in Abia State by Sectoral Headings



Definitely, the non-performance of the other sources has more to do with a faulty IGR management system than it has to do with availability of such sources. This becomes clear from the differences between IGR projections and realizations in nearly all the headings. For example, while taxes far exceeded its projections by 22.8 percent, virtually all other sources of income fell far short of projections. Realizations from fines and fees represented no more than 41 percent of projections while 55 percent and 43 percent of the projections in licenses and earnings and sales were realized. The poorest performances were on licenses and miscellaneous income where no more than 18 percent and 3 percent of projected revenue were realized. As can be seen from Figure 6, the same challenges face Imo state with the board of internal revenue generating over 90 percent of all actual revenue despite tendering only 40 percent of the budget. Pools betting and gaming board hoped to raise a whopping 28 percent of all revenue for the state through the 2005 – 2009 fiscal years, but generated nothing…nothing! The same applies to several other MDAs in many other states. Figure 7 shows the item classification of consolidated realized revenue in Enugu state for the 2005 to 2009 period as well and over 70 percent comes from taxes while another 15 percent is from fees and fines. The rest of the sources share the other 15 percent. In other words, the same reliance on a single source of income that plagues the entire country is replicated (at a lesser but no less dangerous level) at the internal revenue generation system of the states. Strangely, it seems easy to understand the implications of a mono-source government revenue system, but just like the case with the rest of the country's government revenue system, it seems very difficult for most states in the region to diversify.

Figure 6: Budgeted and Actual IGR in Imo state (2005 – 2009) by Source Ministries

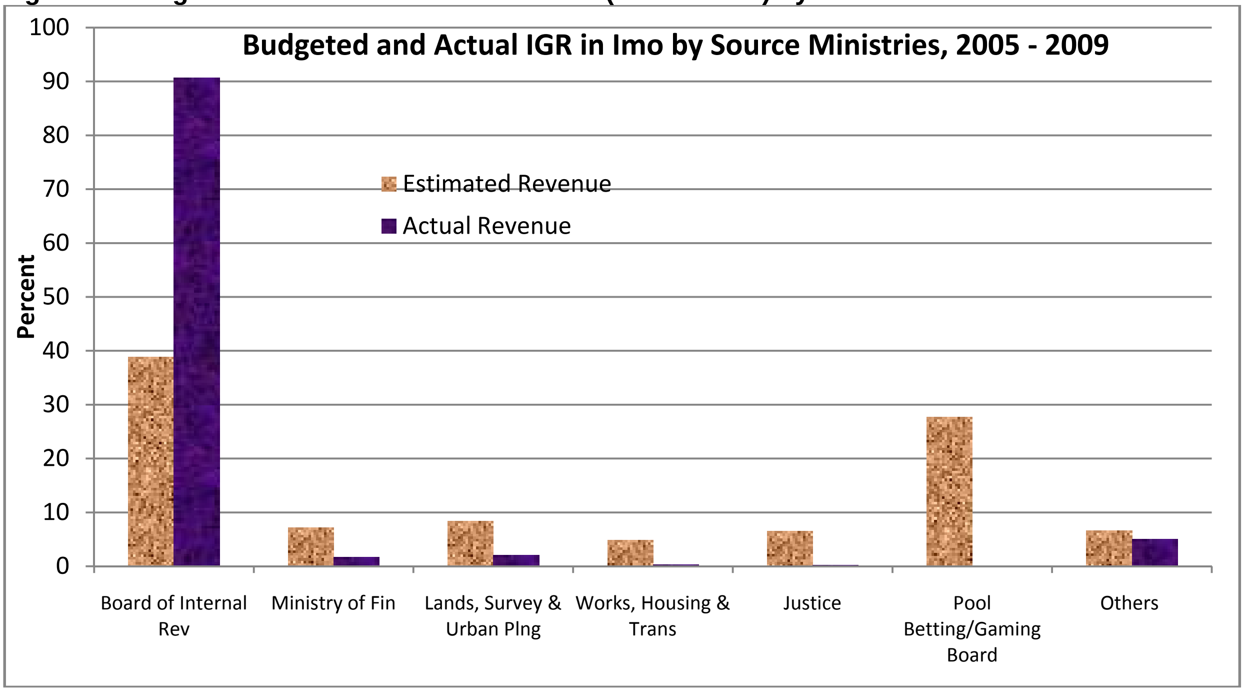
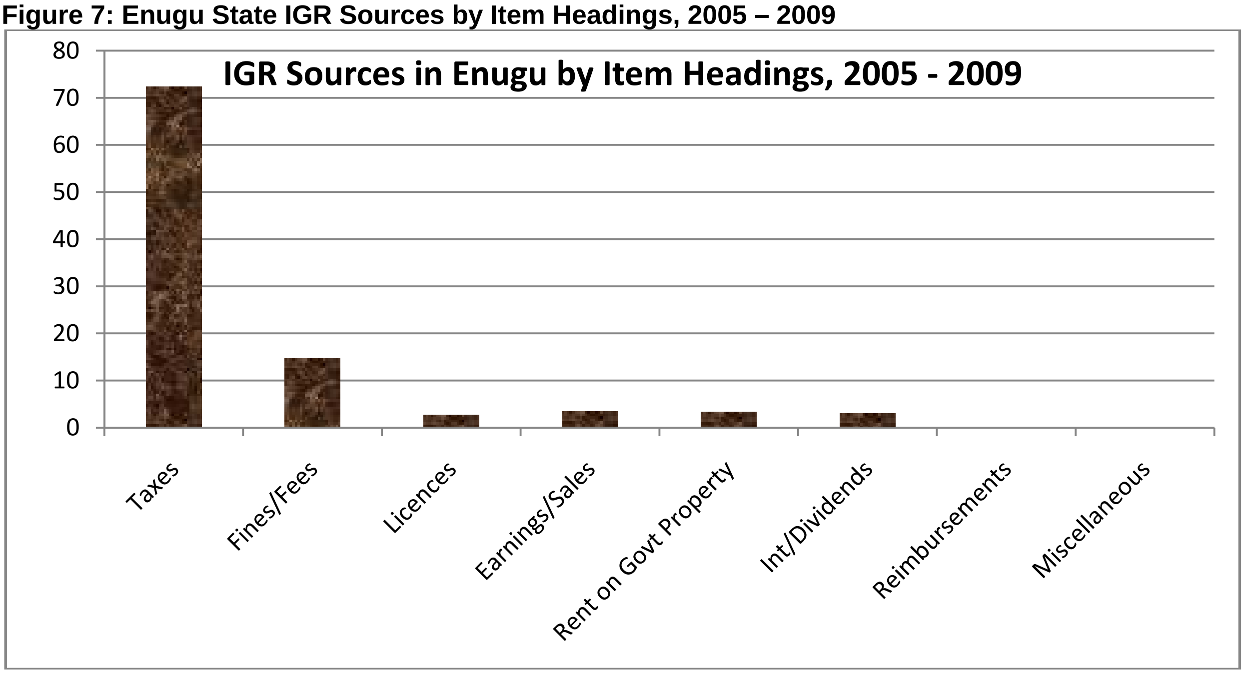


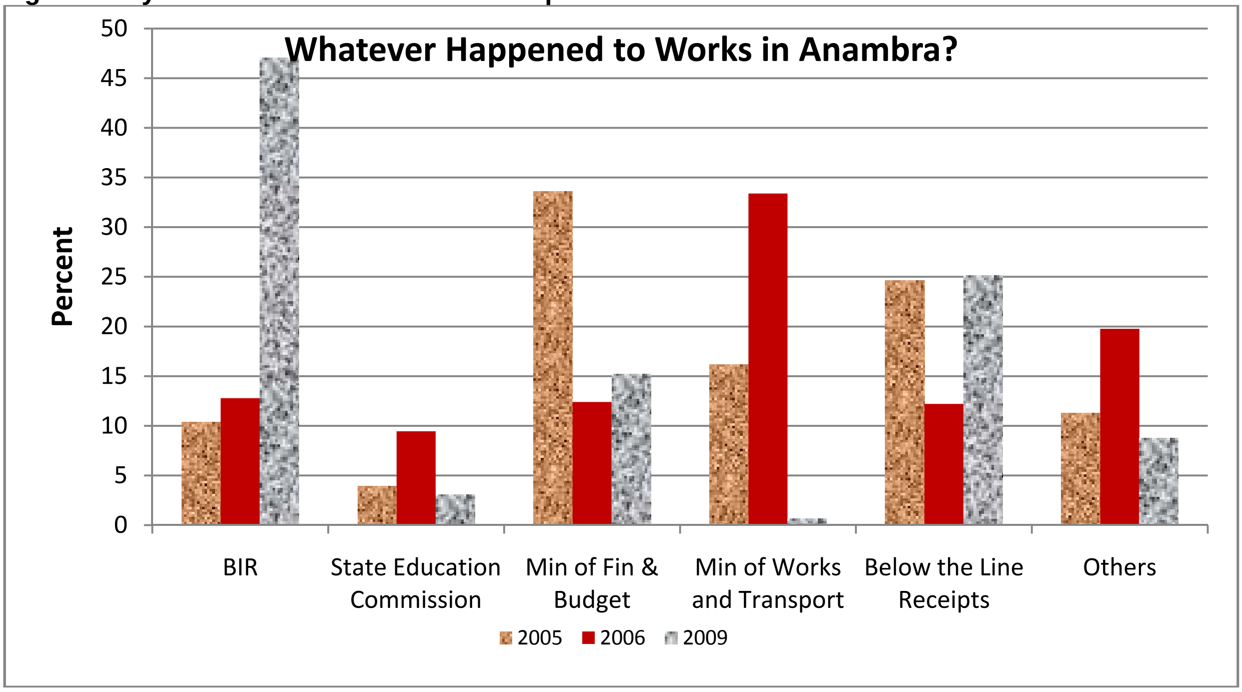
Figure 7: Enugu State IGR Sources by Item Headings, 2005 – 2009



The noted instability in revenue sources seems to be a region-wide affair and pops up in nearly the IGR system of all states in the region. The gyrations in realized revenue from all sources are way too significant to be ignored and seem to be a major challenge for internally generated revenue in the region. We rehearse some of the revenue shares of different sources of revenue as shown in Figure 8 to buttress this point. Revenue to the board of internal revenue (the board in charge of taxes) moved from only 10.4 percent of all revenue in 2005 to as much as 47 percent just four years later (in 2009). At the same time, revenue from the state education commission moved from 3.9 percent in 2005 to 9.5 percent in 2006 but dropped back to 3.1 percent in 2009. The ministry of finance and budget raked in 33.6 percent of the revenue in 2005. That dropped sharply, for unexplained reasons to 12.4 percent in 2006 and rose marginally again to 15.3 percent of total revenue. One of the most dramatic gyrations is in the

Ministry of Works and transport which was responsible for 16.2 percent of all revenue to the state in 2005, raised that to 33.4 percent in 2006 but fell flat to only 0.7 percent in 2009. Likewise, below the line receipts moved down to 12.2 percent in 2006 from 24.6 percent in 2005 and by 2009 had recovered to 25.2 percent while 'other' receipts shot up to 19.8 percent in 2006 from 11.3 percent in 2005 but fell again to 8.8 percent in 2009.

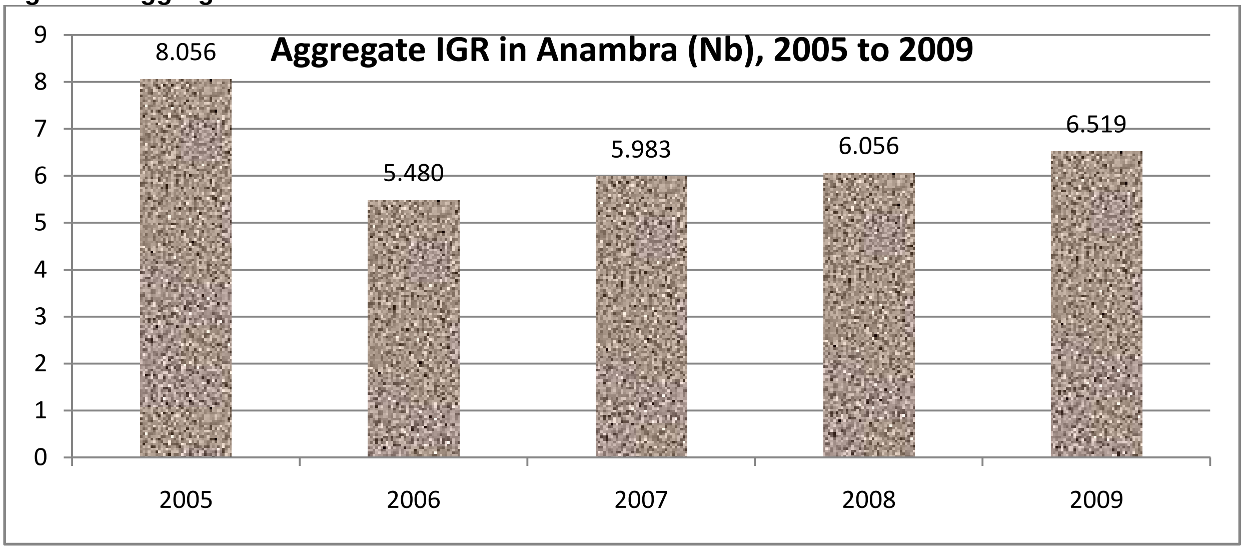
Figure 8: Gyrations in Sectoral IGR – Example from Anambra State



These sharp movements in very short periods are quite inexplicable except if they indicate a fundamental flaw in the internally generated revenue system of the states. Collections are not based on systematic and institutionalized procedures. Sometimes, they are matters of chance and the amount of coercion the relevant authorities are willing to exert to realize revenue for a particular year. Often, when a commissioner or a unit head is sacked (which happens way too often at the sub national level and can be for any and all reasons), there is a dramatic transmission of the political changes to revenue – and indeed overall administration. Put otherwise, the gyrations in the movements of revenue shares represent a more fundamental challenge with political and civil administration at the sub national level namely, outcomes do not depend on institutions, which are more stable, but on individuals, which come and go. Revenue efforts, and even administrative excellence, are often a matter of the individual in office. This would be less of a challenge if the individuals are stable; but the rate of change of the office holders is too high for any form of stability in the polity. It is customary that when a political office holder in a developed country appoints an aide, such aide usually stays out the office tenure of his boss except where there is a major scandal, abuse of office or some other change forces a relocation. In Nigeria, it is the other way round, particularly at the lower tiers. Commissioners hold offices to satisfy constituencies and such office holding are sometimes rotated among different constituencies based on understanding. So a political office holder may be mandated by the political structure to change his aides several times in one political cycle of four years. Besides, some appointees do not qualify for the offices they are given but cannot be changed on account of the constituencies they represent. These arrangements affect all facets of administration, not the least internally generated revenue.

When political changes affect the chief executive of a state, the impact is even more felt. Figure 9 shows aggregate IGR from Anambra from 2005 to 2009. There is gradual growth in the absolute value of IGR from 2006 to 2009 from NGN5.4 billion to NGN6.1 billion in 2008 and then to NGN6.5 billion in 2009. But strangely, aggregate IGR in 2005 which stood at 8.1 billion (a value the state has not been able to reach again since) is more difficult to understand. Even more puzzling is the sharp drop from the NGN8.1 billion in 2005 to only NGN5.5 billion in 2006 --- again, that is except the explanation lies in political changes. The election of Chris Ngige who governed the state between 2003 and 2006 was annulled by the courts in 2006 after long and tedious legal battles, and Peter Obi was installed as the duly elected governor. But Mr. Ngige had prior to the annulment of his elections, performed excellently in virtually all spheres of administration. Obviously, the transition in government impacted the machinery put in place for internally generated revenue by Mr. Ngige. Consequently, revenue in 2006 fell to only 68 percent of its value in 2005 and has had substantial difficulty recovering back to the 2005 value.

Figure 9: Aggregate IGR in Anambra State – 2005 – 2009



States in the region do not only have problems with instability in the political system or absence of structured institutions for generating IGR; they also have problems with the sustainability of the sources of IGR. IGR sources in many of the states have questionable sustainability. We demonstrate this with IGR from Ebonyi state. Ebonyi state have few sources of internally generated revenue; but even these few are neither sustainable nor ideal sources. Ebonyi state for example, is probably the most educationally backward state in the region, just as it is the most economically backward. The government of the state has in recent times worked hard to raise the level of education in the state. But while like the rest of the states its board of internal revenue raises about 30 percent of its revenue through taxes, it is worrisome that Ebonyi state university and the teaching hospital respectively constitute 28 percent and 5 percent of the state's entire internally generated revenue. As much as 42 percent of the state's revenue comes from unclassified 'others'. Interestingly, for the 2008 fiscal year from where these figures were obtained, there was no budget proposal for income from either the state university or the teaching hospital! Plainly put, the state either did not expect any income from these sources or the expected income was so small that it was not considered worth including in revenue projections; yet they formed the major pillars of revenue generation for the year. Clearly, every analyst would worry about a revenue source that was not in the plan but ended up producing 28 percent of all revenue for a particular year. There is also the challenge of what constitute these 'others' in the 42 percent revenue basket. Can they be relied upon for planning in subsequent fiscal years? For one state University to form as much as 28 percent of revenue sources imply that there were not many other sources with sufficient backbone to carry the finances of the state.

Revenue authorities in the state seem to face this unpredictability in revenue yields from different sources in planning as is evident from the differences between projected and actual revenue shown in Figure 10. Projected revenue from the ministry of lands for example stood at nearly 10 percent, but actual revenue from the ministry was less than 2 percent. Likewise, actual revenue fell short of projections in the board of internal revenue and Accountant General's Office. Meanwhile, while expected revenue from 'other sources' was about 28 percent, this amorphous segment ended up yielding 42 percent of revenue. As earlier noted, the state university and teaching hospital from which a combined 33 percent of the revenue for the fiscal year was realized did not even feature in revenue projections. The state projected to realize 30 percent of its internally generated revenue from taxes, but ended up realizing 45 percent from this source. Likewise, it projected to receive only 16 percent of its revenue from fines and fees but ended up receiving 47 percent from that source. Meanwhile, the state projected to receive 32 percent of its revenue for the same 2008 from interests, dividends and capital repayments, but got only 4 percent from the same source. Earnings and sales from which the state expected to get as much as 16 percent revenue ended up yielding only 3 percent. Projections for revenue from rent on government property were also as high as 7 percent, but nearly was realized from that source. Such huge variations between approved estimates and actual revenue either question the validity of assumptions underlying IGR projections or show complete lack of understanding of the revenue base of the state by the planners.

But beyond the assumptions and the questions they engender for IGR sustainability, there is even a more fundamental issue raised by the Ebonyi (and other states') data. The content and manner of revenue generation through fines and fees as sources of income are anti-growth. Fines are collected as penalties for infringing on the legal system while fees, as in the state university case, are levies for services. Whether it is the fine component or the fee component of that item heading that forms the majority, there is reason to worry. Fines imply that the state relies more on residents who are not law-abiding for its income while fees, particularly from education and health sectors, as seen in Figure 11 implies substantial tax on the most basic social infrastructure that government provides for its citizens. To be precise, there is nothing wrong with taxes on education and health if such taxes are relatively low or do not form a total disincentive to the use of public sector facilities. For a poor state like Ebonyi with all its social infrastructure (particularly education and health) challenges, this is no mean an issue. It implies that government extracts its major income from services rendered to the poorest of the society. Government ought to get funds from such services, but when the funds form as much as 47 percent of all government revenue, there is reason to worry. This is especially so if, as is the case in the state, there are some less growth-restraining sources of income that remain untapped by the same government.

There is also reason to worry about the manner such fines are collected. In other climes, it is customary to issue ticket to an offender and he appears at the revenue (or other relevant) office to pay a fine. In the south east, such courtesies are not in the menu of government approach to affairs. A typical fine and/or fee for motorists, say, would be collected by crossing the road with nail-infested logs of wood. Motorists are forced to stop and face touts, who double as both enforcer, arbiter and final judge, determining and enforcing the rules, interpreting offences and meting out punishment to offenders in whatever way deemed fit. There is little courtesy to end users and there are little, if any, considerations to the person or business of the payee in the manner of collection of the accruals to government. In part, this affects cordiality between government and residents funding its activities. So beyond the sustainability of the sources, there is also the challenge that sources such as the ones that make up the bulk of revenue for Ebonyi state constitute an impediment to conducive business environment. They pit government against its people and make the payment of funds of any kind to government a pain to residents.

Figure 10: Revenue Generating MDAs in Ebonyi State, 2008

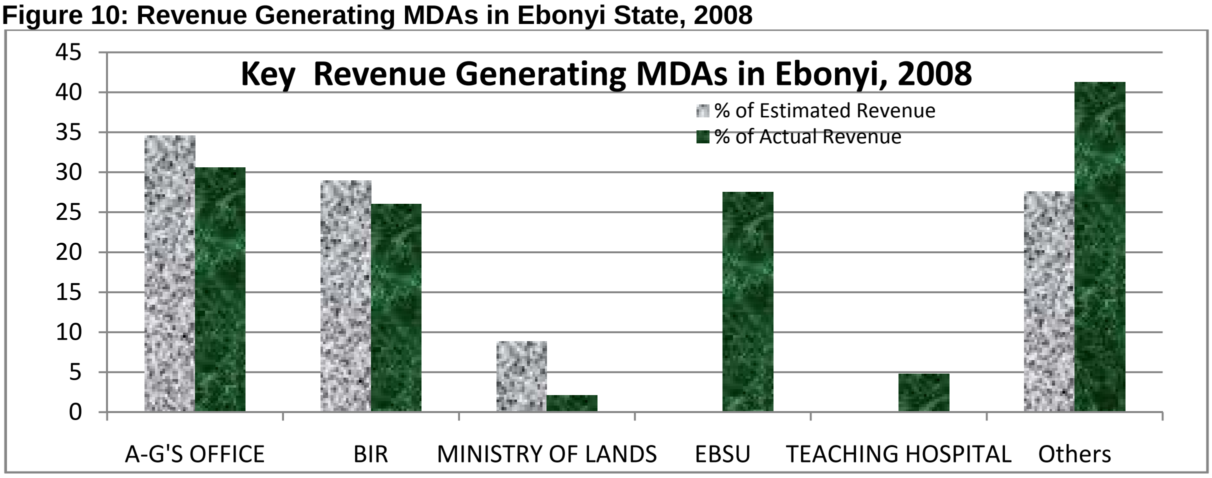
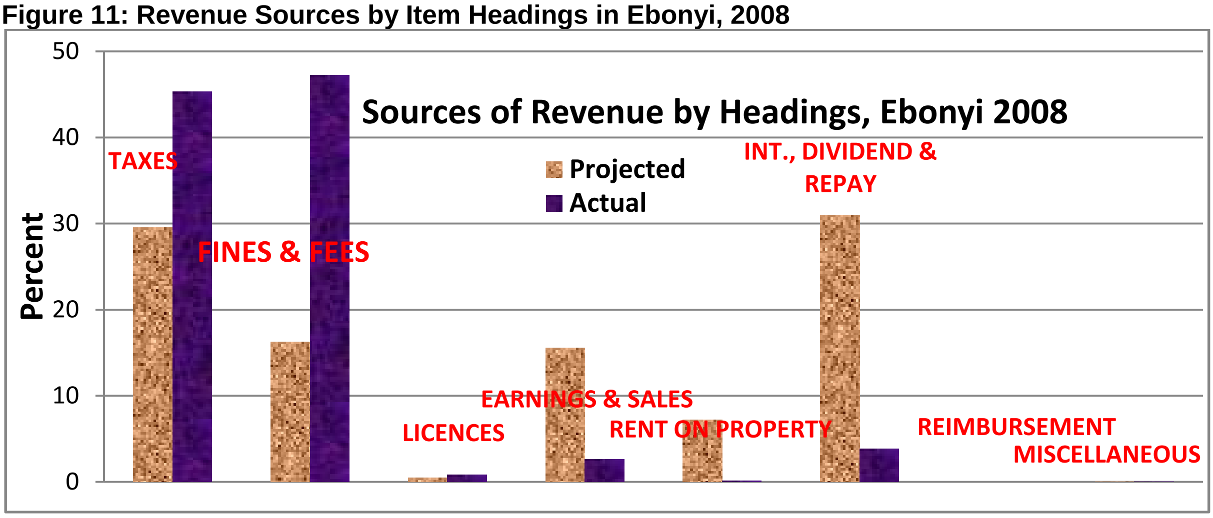
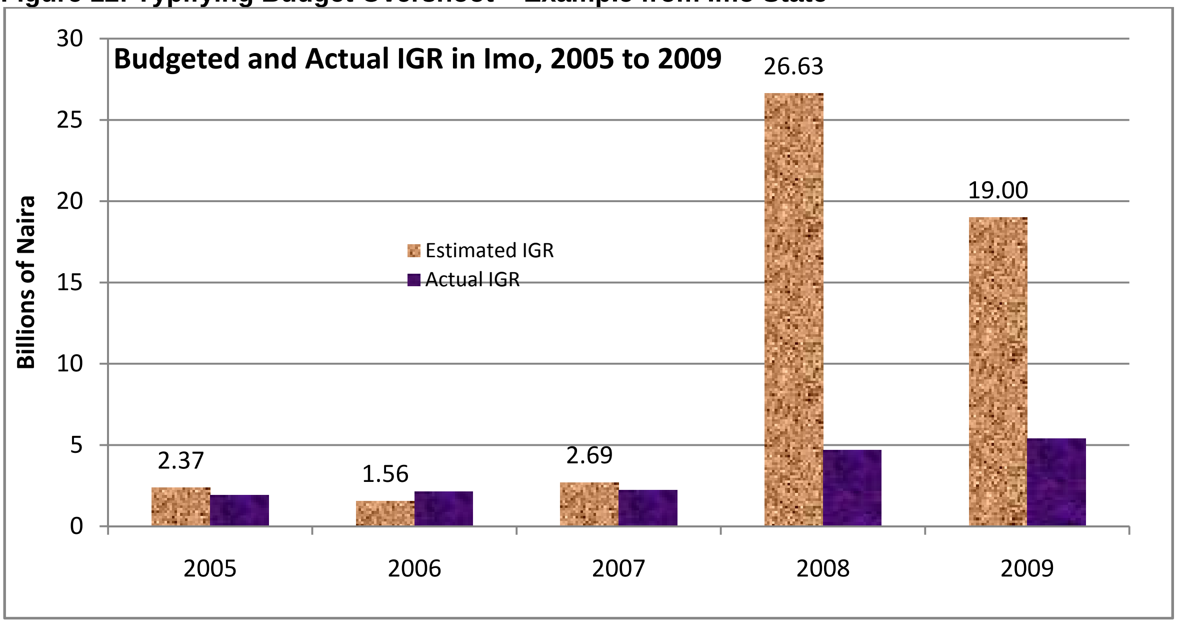


Figure 11: Revenue Sources by Item Headings in Ebonyi, 2008



Before leaving this segment of the discussion, we consider it important to briefly examine IGR budgeting which has cropped up as an issue previously. Figure 12 shows approved estimates and actual revenue in billions of Nigerian Naira for Imo state from 2005 through 2009. It seems the state changed the structure of its internal revenue from 2008 as the figures indicate significant upward deviation in 2008 relative to the years before it. For example, while internal revenue was around NGN2 billion for the three years 2005 to 2007, it shot up to around NGN5 billion in 2008 and remained there in 2009. Indications from senior government officials in the state are that the state used private consultants for revenue in 2008[1]. Whatever the arguments for or against the use of consultants, an unsettling fact that emerges from the figure is that approved revenue projections shot up to very unreasonable levels. For a state that raised only 2.7 billion in 2007 to project to raise 26.6 billion in 2008 is completely unreasonable, particularly when there has neither been a major economic revolution nor a population explosion that raised potentials to match the levels being projected for revenue. Interviewed state officials argued that private consultants needed to make those projections in order to convince the government to give them the job. But the loophole in this argument is that final approval for the budget was given by the state government. Even where a private consultant in pursuit of business opportunities steps out of order, it is the responsibility of the government agency engaging its services to call it to order. But such call to order can only be made after careful consideration and analysis of previous trends which, it seems, many government institutions are either ill-equipped or outright unwilling to do. It is no surprise that though efforts were stepped up (possibly with an approach where the end justifies the means); actual collection of NGN4.7 billion represents no more than 17.6 percent of the approved estimate for the year. The projection was marginally scaled down to NGN19 billion in 2009. Yet, given that the tax base did not grow as exponentially as the revenue projections, only 28.3 percent of the NGN19 billion was realized. The same trends are seen in Enugu state where in 2009 alone, the state's revenue projection was NGN8.2 billion, but actual revenue was only NGN1.98 billion, an intriguing 24 percent of the projection. The board of internal revenue of the state projected to raise NGN5.6 billion but realized barely NGN1.3 billion. Performance was the same across nearly all MDAs. For example, examination development centre was projected to rake in NGN119.7 million but there is no record of its bringing in anything for the fiscal year --- and no justifications were given for the failure.

Figure 12: Typifying Budget Overshoot – Example from Imo State



The way-off projections on IGR receivables underscore the more technical question of lack of capacity for rigorous analysis that should underpin IGR policy design and implementation at the state level. Such unrealistic projections as shown in Figure 12 present a puzzle in the light of the strategic importance of explicit financing options in the determination of overall political and financial health of a state

[1] There are significantly conflicting positions on the use of external consultants by states. While the Federal Inland Revenue Service (FIRS) seems to kick against it for varying reasons, many state governments consider that generating revenue by using their own employees has historically been ineffective. Enforcement by ministry staff is considered insufficient to raise funds needed by government. Kiabel and Nwokah (2009) make a case for the use of external consultants for internally generated revenue in Nigeria. The issue, though, is far from settled; but the reality is that more states increasingly resort to private consultants for their revenue needs.

government. The jump from NGN2.69 billion (which was less than fully realized in 2007) to NGN26.63 billion a year later for an economy which exact gross output is probably not known to the planners and where no major improvements occurred over the one year is a complete give-away of the poor statistics and assumptions that underpin IGR planning in many states. It indicates the lack of structured policy, critical thinking, institutions and instruments for IGR and a dependence on ad hoc mechanisms for IGR programmes in the states.

V. Conclusion: Future of IGR and Economic Growth in the South East

The challenge of IGR in the south east is obviously the need for a full fiscal overhaul and a re-assessment of government-private sector relationship. Such reassessment should improve government's role as a facilitator of private enterprise and a greater partaker of its profits. In the past, a number of studies have been conducted on improving states' revenue. Recommendations of these studies include improving efficiency in revenue collection from already existing sources, increase in the rate of existing taxes and broadening the revenue base by introducing new taxes, increasing financial transfers and additional revenue sources from the center to the governments, greater fiscal discipline, among several other means to increase revenue of sub national governments (see Anyanwu, 1999; Alade, 1999; Ekpo, 1999; among others).

But as a group, states in South East Nigeria have a number of potentials that make them stand out and that would necessitate more than just taking conventional steps to improve revenue. For example, increasing tax rates would be useful, but that would only milk the same set of cows that are already over-milked. In many instances, broadening the tax base by introducing new taxes would mean inventing new names for getting more revenue from tax payers. For a private sector that is already bleeding heavily from cuts inflicted on it by an arbitrary and multiple tax system, this might be one blow too many. As far as we know, increasing intergovernmental transfers when revenue source at all tiers of government is still monolithic seems like a non-recipe. So options like improving efficiency of collection and improving use of collected revenue remain some of the only ways out. There is the need to move away from conventional measures as governments strive to improve internally generated revenue in the region. Three key measures that can be considered include exploiting unexploited sectors, improvement in accountability of collected funds and providing support to the private sector. It seems the most important need for revenue upshot in the MDAs is development of the revenue yielding sectors. Important as improving staff skills and providing funding to aid tax pursuit are, without increasing the yield of available sectors and exploring hitherto unexploited sectors, internal revenue generation in the region might not improve much.

Put in other words, the need is for a full fiscal and macroeconomic overhaul of the region to make policies supportive of private sector growth. Fortunately, there are humungous untapped resource deposits, human capital and ingenuity that can be triggered to unleash a full scale economic transformation. South East Nigeria is probably the best resource-equipped but least directed region of the country. The Nigeria civil war brought out the best and worst of the region – its resourcefulness, innovation and criminality. Over the last three decades, the region has not only risen and rebuilt itself from the ruins of the war; it has been able to grow credible industrial outposts around Nnewi, Aba and Onitsha axes. But optimal performance of these outposts is affected by phenomenal infrastructural and policy neglect. Yet while these resources lie fallow, states in the region scrap up revenue from far less reliable sources. Fiscal overhaul implies strengthening the institutional capacity for accountability in MDAs so as to raise the trust of the private sector on government. Macroeconomic overhaul implies examining dormant sectors, examining means of improving the efficiency of sectors that are working presently, and aiding private operatives to extract and add value to the region's resources.

Such macroeconomic and fiscal overhaul as being expounded first takes for granted a change in mindset to fiscal federalism by the region. The mindset to fiscal federalism in many states in Nigeria wants to quickly translate oil funds to present consumables. But it has already become imperative that such underground exhaustible resources be translated to over-ground sustainable resources. A key means of doing that is through physical and social infrastructure that supports private enterprise; not for government to go into business but for government to partner with businessmen. This needs coordination and planning. It is completely unjustifiable that Nigeria burns millions of cubic feet of gas when it cannot provide basic energy for its industries. Since energy is a major challenge facing businesses in the South East, a regional energy programme might be very useful. Being contiguous, the five states in the region can easily pool resources and exploit economies of scale to design a phased programme for regular power provision for designated industrial zones. Part of the expected partnership must also go as far as streamlining measures to avoid double or multiple taxation on firms within the region. Designing a collaboration that protects the investor and ensures that evidence of taxes collected in one state should be valid in partner states will help a lot to reassure the private sector and boost economic activities in the region.

Clearly, the biggest asset of the region is its people – the widely acknowledged resourcefulness of the people. This is yet to be tapped and for full economic turn-around. It has to be. But it requires coordination and innovation. For example, all the states in the region are in the high migration stratum of the country. A 2010 migration survey shows that the South East tops all regions in the country on migration (Agu and Onodugo, 2010). Regional internal migration rate is as high as 60 percent while international migration rate in the region is about 10.3 percent. This compares favourably with internal migration rate of 46 percent and international migration rates of 16 percent for the South South, which is the next in rank. In addition, the south easterner is culturally tied to his roots. Almost every responsible man from the South East goes home at least once a year no matter where he is located; unless of course economic or social circumstances force him to do otherwise. Such strong ties to roots and willingness to spend resources to keep touch with home can be reasonably exploited through Diaspora bonds.

As distortionary politics, so is weak collaboration. Weak collaboration is not limited to that between government and the private sector (or other stakeholders), but extends to poor collaboration among MDAs. Fact is there is usually very poor delineation of 'ownership' of sources of revenue for MDAs. The Ministry of Agriculture could tax some agricultural products only for the ministry of trade and industry to also impose sales tax on the same commodities at the point of sale. In many of the states in the country, there is a continuous contention and internal friction for dominance and independence between the Board of Internal Revenue and the Ministry of Finance, particularly the Office of the Accountant General. If these internal squabbles end among the officials of the ministries, they probably might pose no problem. But often, they are carried on to the field and greatly affect collection approaches, remittances and accountability for internally generated revenue. So as efforts need to be made to enhance collaboration with non-government stakeholders, it is also important that reporting and relationship lines be clearly drawn among the MDAs on revenue responsibilities and for the sake of the taxpayer, that such lines be respected.

A change in the federalism mindset for states in the south east also entails looking at federalism from the standpoint of a strong state. In most federal economies, and indeed even in China which is a unitary but decentralized state, revenue moves from the lower tiers to the higher tiers of government. While this does not necessarily have to mean raising all revenues needed for governance, it definitely means striving for fiscal independence and complementing own resources with federal allocations and not the other way round as presently exists. The good news is that personal income tax is under the purview of the state. Indeed, should oil dry up today, the so-called lucrative sources of revenue for the federal government would shrink so drastically that dependency will be turned in favour of the lower tiers of government[2]. Everywhere in the world, the most important source of government funding besides corporate tax is the personal income tax. But tapping into the possibilities of personal income tax in the region would have to mean growing the income even more. Presently, per capita income in the South East is higher than that in many other regions of the country. But many of these are masked by informal, self employment. The government needs to find a means of formalizing these, improving on their yield and taxing them. In addition to personal income tax, sociologists have been worried about the rising spate of ostentation in the South east. Taxation could be a way of curbing big appetites and retaining a significant part of the region's income within the country.

In sum, getting the IGR system in South East Nigeria to work in favour of both the collector and the payer is possible, but it requires significant work. The system is currently flawed in more ways than one and a large measure of collaboration is required to systematize and organize the system of revenue collection and use. There is need for collaboration among the states as well as between the states on the one hand and organized private sector and civil society on the other. Strange but true though; the answer to sustainable fiscal federalism in Nigeria does not lie in 'better' sharing of the national cake! Indeed, even if the national cake were to be shared 'more equitably' from the perspective of south eastern states, it will still be far from sufficient for the growing needs of the states.

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[2] Several analysts including Olowononi (1999) are of the view that tax assignments in the country is in favour of the Federal Government, which has assigned to itself the best sources of revenue

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