Local Government Tax Mobilization and Utilization in Nigeria: Problems and Prospects

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LOCAL GOVERNMENT TAX MOBILIZATION AND UTILIZATION IN NIGERIA: PROBLEMS AND PROSPECTS

ABSTRACT
The federal structure in Nigeria constrains local governments' ability to mobilize and use revenue to meet their obligation in a sustainable way. Local government system as the third-tier of government deserves adequate finances to enable it cope with numerous developmental activities within its jurisdiction. This paper is divided into five segments. Part one is the introduction of the theme, while part two deals with theoretical issues. Part three concentrates on the local government finances and revenue utilization. In order to finance some viable projects, local government must be given adequate tax power and also share major tax bases with other tiers of governments. Part four highlights the problems and prospects of local governments, Revenue, Mobilization, Utilization and Corruption.

INTRODUCTION/HISTORICAL BACKGROUND
One of the recurrent problems of the three-tier system in Nigeria is dwindling revenue generation as characterized by annual budget deficits and insufficient funds for meaningful growth and viable projects development. Local governments are the nearest government to the people at the grassroots in Nigeria, they are strategically located to play a pivotal role in national development. Since they are responsible for the governance of about 70 percent of the population of Nigeria, they are in vantage position to articulate the needs of the majority of Nigerians and formulate strategies for their realization.

Local administration in Nigeria can be traced to the colonial period. Available record shows that the first local administration ordinance was the Native Administration Ordinance No. 4 of 1916 which was designed to evolve from Nigeria's old institutions the best suited form of rule based on the people's habits of thought, prestige and custom (Bello-Imam 1990). These local administrations were used in the north eastern and western parts of the country while the indirect rule was introduced in the rest of the north.

For example, in 1926, a centralized budget system was introduced. Following the creation of Northern, Western and Eastern regions in 1946, a decentralized public revenue structure began to emerge. The first revenue commission was set up in 1946. During the colonial period, four revenue commissioners were created. The principles, criteria and allocation formulas recommended by the commissions are well documented (see, Ekpo 1994).

Macpherson constitution of 1948 initiated some remarkable changes, the regions introduced some reforms in their local administrations in the 1950s which aimed at enhancing performance. Though, the reforms gave local administrations to collect rates and levy pools and income taxes to finance their activities, the regions had overall control of the taxes. Local administration lacked self-determination, hence their resource were inadequate. Though, the local authorities were partially successfully in the North but unsuccessfully in the Eastern and Western regions.

Adedeji (1970) blames the ineffectiveness of local administration on the following reasons.

(a) Lack of mission or lack of comprehensive functional role
(b) Lack of proper structure (i.e. the role of local governments in the development process was not known).
(c) Low quality of staff; and
(d) Low funding.

According to him, these problems led the local governments into a vicious circle of poverty because inadequate functions and powers lead to inadequate funding which result in the employment of low skilled and poorly paid staff.

Local government administration n the country experienced fundamental changes in 1976. The 1976 local government reform created for the first time, a single-tier structure of local government in place of the different structure in the various states. Our interest in the 1976 reform hinges on the restructuring of the financial system. The reforms instituted statutory allocation of revenue form the federation account with the intention of giving local government fixed proportions of both the federation account and each states' revenue. This allocation to local government became mandatory and was entrenched in the recommendations of the Aboyade Revenue Commissions of 1977.

The 1979 constitution empowered the national Assembly to determine what proportion of the federation account and revenue form a state to allocate the local government. In 1931, the National Assembly fixed these proportions at 10percent of the federation account and 10 percent of the total revenue of a state. In 1985, the state's proportion was reduced to 10 percent of the internally-generated revenue, local governments' allocation from the federation account was later adjusted to 20 percent. It was further increased to 25 per cent with the arguments that local governments are expected to take on larger developmental responsibilities. The revenue allocation has continued to vary in proportion over time.

At present, local government receive 20 per cent of the federation account. In addition, proceed from the value added tax (VAT) are also allocated to them. Presently, VAT's allocation is 35 per cent based on equity of states (50 per cent), population (35 percent) and derivation (2 percent).

The 1976 local government reforms states the internal revenue sources of local governments to include:

(a) Rates, which include property rates, education rates and street lighting.
(b) Taxes such as community, flat rates and poll tax.
(c) Fines ad fees, which include court fines and fees, motor park fees, forest fees, public advertisement fees, market fees, regulated premises fees, registration of births and deaths and licensing fees; and
(d) Miscellaneous sources such as rents on council estates, royalties, interest on investment and proceeds from commercial activities.

Despite this clear demarcation, states and local government still clash over sources of internal revenue.

There has been a significant increase in the number of Local Governments over the years. There were 96 divisions in 1967. By 1976, they had increased to 300. The number was increased to 774 after five yeas (Adedokun A.A. 2004) we will like to emphasize here that the rise in the number of Local Governments as implications on the assignment of public revenue responsibilities among the tiers of government.

THEORETICAL FRAMEWORK

Local government system in Nigeria needs a moderate amount of financial autonomy to be able to discharge its responsibilities effectively. Public revenue in a federal system assumes that there are benefits to be derived from decentralization. Public revenue decentralization occurs when lower tiers of government have statutory power to raise taxes and carry out spending activities within specified legal criteria.This is referred to as the Overlapping Authority Model propounded by Deil.S.Wright (1978) on Intergovernmental relationships. Public revenue decentralization occurs when much of the money is raised centrally but part of it is allocated to lower levels of government through some revenue-sharing formula otherwise known as administrative decentralization.

The main reason for decentralization is anchored on allocation sharing or efficiency grounds so it is possible to advance argument for decentralization in Nigeria where there are many ethnic groups.

Oates (1993:240) contends that "there are surely reasons, in principle to believe that policies formulated for the provision of infrastructure and even human capital that are sensitive to regional of local conditions are likely to be more effective in encouraging economic development than centrally determined policies that ignore these geographical differences” There is a great relationship between decentralization and economic growth and behaviour for economic fundamentals within the decentralized jurisdiction is a matter that remains an empirical issue and discussions must be country specific.

Kim (1995) quoted in Oates (1996) has shown that in his mode of explaining rates of economic growth, revenue decentralization that there are positive and statistical significant change, using a sample of countries. His results also shows that, other things being equal, more public revenue decentralization was associated with more rapid growth in GDP per capita during 1974-1989 period.

Prud’homme (1995) on the other hand, argues that decentralization can increase disparities jeopardize stability, undermine efficiency and encourage corruption. He maintains that local authorities, for example, have few incentives to undertake economic stabilization policies. The instrument of monetary and public revenue policies are better handled by the central government.

Oates (1993) opines a contrary view that the principles of centralization is costly because it leads the government to provide public goods that diverge from the preferences of the citizens in particular areas (regions, provinces, states, local governments). He also argues that “when these preferences vary among geographical area, a uniform package chosen by a nation’s government is likely to force some localities to consume more of less than they would like to consume.

According to Tanzi (1995) the interpretation of both Oates and Prud’homme assumes that subnational government levels already exist, hence the crucial problem becomes which of the existing government levels ought to be responsible for particular forms of spending.

The function of government can be divided into three-allocation, distribution and stabilization function (Musgrave 1959). Using this stratification, stabilization and distribution functions are expected to be under the peripheri of the central government while lower government undertakes allocative functions. Hence, any spending and taxing decisions that will affect the rate of inflation, level of unemployment, etc. are better handled at the centre, while other activities that will affect social welfare are more efficient if undertaken by subnational governments.

Theoretically, the scope of benefit is the basis for allocating responsibilities governments. Public goods and services which are national in nature (foreign affairs, environment, immigration and defense) should be provided by the central government while those whose benefits are mainly localized should be assigned to the lower levels of government. Quasi-private goods or intermediate goods and services such as administration, health and welfare services should on account of efficiency delivery, be assigned to lower levels of government. (Vincent. O. 2001).

Studies on tax and public revenue mobilization in Nigeria have shown a high degree of centralization. According to Emenuga (1993), the allocation of revenue to the tiers of government has no adhere strictly to the expenditure requirements of each tier, thus the federal government has become a surplus-spending unit while other functions, he proposes the determination of a tier's share through the aggregation of its basic expenditure needs.

To reduce the gap between tax power ad responsibilities, tow types of revenue sources are allocated to each tier. These are independent revenue sources and direct allocation from the federation to which centrally collectable revenues are paid. Local government also receives allocations from state Internal Revenues. An agreed formula for vertical revenue sharing is used in sharing funds from the federation account.

Another key issue in the practice of public revenue mobilization in Nigeria is how to distribute the bloc share from the federation account among the constituent units of each tier i.e among the 36 states and the 774 local governments. This is called horizontal revenue sharing.

In Nigeria, there are four categories in the vertical allocation list – federal, state, local governments, and the special fund. The allocation to the Federal Capital Territory (FCT) is accounted for under the special fund which is administered by the federal government.

Local Government Finances and Revenue Utilization

Public revenue mobilisation is one of the most keenly contested issues in Nigeria. A comprehensive review of the reports of the various commissions and government policies from the 1946 Philipsons commission to the activities of the National Revenue Mobilisation, allocation and fiscal commission established in 1989 could be found in Kayode (1993), Emenuga (1993) and Ekpo (1994).

Local governments in Nigeria receive statutory allocations from the two higher tiers of government (federal and states). At the present, revenue sharing formula, local governments receive 20 per cent from the federation account. They are also statutorily entitled to 10 per cent of states' internally generated revenue. As regards to Value Added Tax, local governments receive 30 percent in 1998. This was shared to local governments, on the following basis: equality (50 per cent): population (30 per cent) and derivation (20 per cent). In 1999, local governments received 35 per cent of the VAT proceeds.

The federal government controls all the major sources of revenue like import and excise duties, mining rents and royalties, petroleum sales tax, petroleum profit tax and companies income tax among other revenues sources (see table 1). Local Government taxes are minimal hence this limits their ability to raise independent revenue and so they depend solely on allocation from the federation account.

Much of the revenue collected by the federal government and distributed among the different tiers of government using the vertical revenue allocation formula is from the federation account. But the federal government seems to exercise too much control over its distribution. So many deductions are made from the total revenue collected before the rest is distributed according to the sharing formula.

Table 2 summarizes federal allocation to local governments for the period 1976 to 1997. The federal allocation showed steady increases during the periods. In nominal terms, the allocation which stood at N100 million in 1976 jumped to N352.6 million in 1980, reflecting a compound growth rate of almost 29 per cent. During the structural adjustments programme (SAP), federal allocation to local governments increased remarkably by 45.7%. This jump could be as a result of the increase in the number of local governments.

Table 1: Jurisdiction of Major Taxes in Nigeria 1990

S/N	Type of Tax	Administration and collection
1	Import duties	Federal
2	Excise duties	Federal
3	Export duties	Federal
4	Mining and royalties	Federal
5	Petroleum sales and profit tax	Federal
6	Companies' tax	Federal
7	Capital gains tax	Federal / States
8	Personal income tax (other than listed in 9)	States
9	Personal income tax: armed forces, external affairs officers, on-residents, residents of the Federal Capital Territory and the Nigeria Police.	Federal
10	License fees on television and wireless radio	Local
11	Stamp duties	Federal / States
12	Capital transfer tax (OTT)	States
13	Value Added Tax	Federal
14	Pools Betting and other Betting taxes	States
15	Motor Vehicle and Drivers' Licenses	States
16	Entertainment tax	States/local
17	Land registration and survey fees	States
18	Property taxes and rating	Local
19	Marketing and trading licenses and fees	Local
20	Motor park duties	Local
21	Advertisement fees	Local
22	Gift tax	States

Source: Constitution of the Federal Republic of Nigeria.

Table 2: Nigeria Federal Statutory Allocation Revenue to Local Governments, 1976-1996 (₦ million)

Year	FA	FR	FA/FR%
1976	100.0	6765.9	1.5
1977	250.0	8012.2	3.1
1978	150.0	7469.3	2.0
1979	261.4	10913.5	2.4
1980	352.6	15234.0	2.3
1981	1085.0	12190.2	8.9
1982	1081.7	11764.4	9.2
1983	876.9	10508.7	9.3
1984	1061.5	11766.8	9.0
1985	1327.5	14680-.8	9.0
1986	1166.9	12837.6	9.1
1987	2117.8	25099.8	8.4
1988	2727.1	27310.8	10.0
1989	3399.8	50272.1	6.8
1990	7680.0	66895.4	11.5
1991	10764.8	100991.6	10.6
1992	16488.0	90453.2	8.7
1993	18316.4	192769.4	9.5
1994	17321.3	201910.8	8.6
1995	17983.4	459987.4	3.9
1996	21590.6	520190.0	4.1
1997	22881.5	452000.0	5.1

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts (various issues)

Table 3: Nigeria; Local Government Finances 1993 – 1997 (N Million)

Year	FA	FR	FA/FR%
1993	253.1	1035.6	-
1994	466.4	1205.9	2645.0
1995	633.9	2012.2	4274.0
1996	575.6	2694.2	7072.3
1997	-	-	8648.9

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts, 1996

Table 4: Nigeria; Fiscal Balance of Local Governments 1993 – 1996
(N Million)

Year	Revenue	Expenditure	Surplus
1993	19915.6	19544.7	370.9(+)
1994	19072.7	18776.4	296(+))
1995	25227.1	24191.5	1035(+)
1996	33232.3	29809.9	3422.4(+)

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts, 1996

1993 state allocation to local governments stood at N253.1 million while it had increased to N633.9 million in 1995. In effect between 1993 and 1996, states' statutory allocation showed a compound growth rate of 22.8 per cent while federal allocation was 4.2 per cent.

The internally generated revenue sources of local governments consists of taxes, rates, fines, fees, and licenses. The study shows that taxes continue to form the bulk of internal revenue, followed by fines and fees. There is also a list of users' charges, royalties and proceeds form stocks and shares, which are categorized as "others".

Internally generated revenue increased from N1035.6 million in 1993 to N2694.2 million in 1996, representing a growth rate of 27 per cent. "For all the local governments, taxes rates, fines and licenses increased during the period under review. In Ijebu-North Local Government, taxes jumped form N31,000 (N55,259.19 in real terms) in 1980 to N121,000 (N67,760.00 in real terms) in 1984 and by 1991 taxes stood at N13,000 (N74,745.19 in real terms). The taxes grew by 12.8 per cent between 1980 and 1991. During the same period, taxes and rates grew by 31.2 per cent and 18.9 per cent respectively. However, in metropolitan Calabar, taxes and rates grew by 5.1 per ce3nt and 9.8 per cent respectively, during the same period. On the other hand, licenses declined by 4.4 per cent (Ekpo and Ndebbio 1998: 16).

Value Added tax also constitutes an additional source of revenue to local governments. There is a limit to the imposition of taxes on the people in order to provide infrastructures. One should try to strike a balance between aggressive internal revenue sources through increased taxation and the need to avoid governance problems.

The viability of local governments have implications on the management of the wider economy. Budget deficits at the local level may create or aggravate public revenue mobilization problems. In Nigeria, major tax bases remain under the central government. Some taxes are shared by state and local governments, for example, property taxes and rates. (See table 1). On the other hand, licenses and fees on television and wireless radio are shared between the federal and local governments. But the Federal government may manipulate tax rates to solve macro-economic problems without bothering about the lower levels since the latter have no major tax bases assigned to them.

It is evident from the available data that for the period 1993-1997, local governments had fiscal surplus. This situation may be different when specific local governments are examined. Hence, it is difficult to conclude whether decentralization may result in stability or instability.

There are several other off-budget accounts that have been operated by the federal government. Some of these are the oil surplus account opened at the beginning of the Gulf War in 1990. Another one is the special debt account intended for repaying part of the countries external debt. This discretionary powers exercised by the federal government has caused pubic resources to be over-concentrated at the centre. This concentration can be seen from the distribution of total public sector expenditure among the three tiers of governments from1993 to 1997 as shown in table 5.

Table 5: Distribution of Total Public Sector Expenditure among the Federal, States and Local Governments, 1993 – 1997 (N Million).

Date	Federal	%	States and FCT	%	Local	%	Total
1993	1912229.1	75	44180.9	17	19475.5	8	254885.5
1994	160893.2	68	55916.4	24	18967.1	8	235776.7
1995	248767.8	71	79591.6	23	22443.3	6	350802.7
1996	288289.3	73	84177.1	21	24261.7	6	396528.1
1997	356262.3	74	92647.6	19	30833.0	6	479742.9

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts, 1997.

Table 5 shows that from 1993 to 1997, the Federal Government controlled between 68 and 75 per cent of total public expenditure while the other two tiers accounted for the remaining 32-25 per cent. All the local governments in the country had control over only 8 per cent of total public spending in 1993 and 6 per cent of same in 1997. At this same time, local government internal revenue only increased marginally from 5 to 8 per cent as shown in table 6.

Table 6: Relationship between Direct Allocations and Internally-Generated Funds at the Local Government Level.

Date	Direct Allocation less	%	Grant	%	Internal Tax Efforts	%	Total
1993	18569.5	93	269.4	1	1035.6	5	19874.5
1994	17787.7	93	229.5	1	1205.9	6	19223.1
1995	22059.0	90	242.9	1	2110.8	9	24412.7
1996	21842.5	92	72.5	0	2027.1	8	23642.1
1997	28300.7	91	202.0	1	2515.6	8	31018.3

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts, 1997.

Also, local governments are not allowed to borrow externally, to develop any viable project; though they may borrow domestically. Since local governments are very crucial for national development, then revenue and expenditure decentralization must accompany each other. Therefore, Nigeria's public revenue mobilization and utilization should be restructured such that assigning of tax powers, tax bases and borrowing would be left to the appropriate tier of government. A situation where the federal government is so far from the people and yet collects virtually all revenue is unhealthy. Certain lucrative taxes should be left to local authorities. The weak administrative machinery should be strengthened to enable them collect major taxes for further development.

The federal government should complement the revenue raised locally with special grants to enable local government with good projects execute it to the benefit of its people. In this case, the federal government can do the necessary follow-up of the project by providing logistic support in terms of monitoring and evaluation modalities.

Capital projects naturally generate employment and prevent migration to urban centres. The involvement of local governments in education also contribute to human capital development. Since 70 per cent of Nigerians still live in the rural areas and local governments are the closest to the rural people, its revenue mobilization drive and utilization strategies should be improved considerably to enable them meet the challenges ahead. Local governments responsibilities for economic planning and development, citizenship development and empowerment through primary, adult and vocational education and capacity enhancement through health care provision cannot be effectively executed just with 6 per cent of total public sector spending. Thus, about 95 per cent of the local governments do not have adequate funding.

In a study carried out by the United Nations Development programme (UNDP) and the states/local government department of the Presidency, out of an aggregate of 23,602 t owns claimed by the respondent local governments, only 5,291 are linked to the national grid for electricity supply while about 33 per cent do not have electricity at all even in their headquarters (UNDP 1989).

Yet, between 1995, and 1997, the local governments executed only 122 rural electrification projects nationwide. Sixty per cent of the local governments had no access to telecommunication facilities yet no local government executed a project in this regard during the three years mentioned. No doubt, the local governments are still confined to their traditional areas with just a little improvement.

Problems of Local Governments Tax Mobilization and utilization in Nigeria.

There is shortage of well trained and qualified personnel which suppose to serve as tool for collection of taxes and rates at the local level, even the few available are not properly trained in efficient budgetary and financial management systems. Also most of the local government\s are short staffed to carry out their duties.

Local governments lack the capacity to attract and retain the right caliber of staff to articulate plans and execute programmes and projects in order to transform the lives of the grassroots people in a short period. For instance, out of 750 respondent local governments in the UNDP – presidency survey, only 541 prepared rolling plans in1995, 1996 and 1997. of this number still, only 151 had planning boards (Composed largely of educators and community health do officers). There were no professionals like economic planners, medical doctors, engineers and so on. NO doubt, the basic educational background of members of the planning boards across the local governments is very disturbing.

Despite the fact that there are constitutional provisions for statutory allocations and internally generated revenues, Local governments are tightly controlled and subordinated by state governors through sundry mechanisms, including manipulation of the disbursement of financial transfers to them.

Local governments in Nigeria mobilize their funds solely from external sources. The external sources include federal and state governments financial transfers like grants, statutory allocations, share of value added tax (VAT), receipts and loans. These external sources introduce a dependence syndrome in local government revenue mobilization effort. Any setback from the external sources would have adverse effect on the administrative machinery and execution of some viable projects. This also has weakened their internal revenue mobilization capacity.

Another constraint is imposed on local government revenue mobilization capacity through state control over local government budget, which is made to pass through many levels of approval in the hands of the state government. Even after approval, post-budget controls still impose further restrictions on what local governments can do (Roberts, 1998).

The delay in the passage of annual budget for local governments poses a great problem in the sense that budget sometimes take 3 months before approval. Invariably, this will cause delay in execution of local government functions including payment of the staff salaries and hinder infrastructural facilities to be put in place.

In 1996, some newly elected Chairmen of Local Governments in Nigeria condemned in its entirety the horizontal sharing formula of the local government's allocation from the federation account which was equality (40 per cent) population (30 per cent), land mass/terrain (10 per cent) social development factor (10 per cent) and internally generated revenue (10 percent). This formula will continue to yield less revenue for many local governments especially when more local governments are created.

In addition, insincerity of council staff on field assignment poses greater problem because most of them usually divert collected council fund for their perusal usage thereby denying the council of the needed funds for its operations. Some local governments Chairmen deposited local governments subventions into savings and loans companies in which the local governments had no account. Some local governments see this as an avenue to divert councils funds for personal use.

Prospects of Local Governments Revenue Mobilization and Utilization in Nigeria.

The increase in revenue from local government statutory allocations definitely enhanced their economic fortunes and service delivery ability. No doubt, the institution of statutory allocation as a local revenue mobilization mechanisms, the increase of the allocation form 10 – 20 per cent of the federation account, the direct disbursement of federal revenues to local governments and the removal of some political bottlenecks and abolition of other administrative hindrances have boosted the revenue profile of local governments in Nigeria.

Local governments in Nigeria are no longer there to discharge administrative functions they are deeply involved in collective participation in governance, encourage physical and economic development, create the conditions for employment within their localities and provide social services that will improve the well-being of their people.

The 1976 Reform has given local governments in Nigeria a short of radical transformation form being an appendage of state governments to a very important and autonomous third tier of government. With this reform, local government became a legal and constitutional entity with properly defined functions as well as guaranteed sources of revenue.

However, for the local governments to function effectively in Nigeria, the revenue allocation formula should be changed. Larger percentage (%) of the revenue allocation should go to the local government in order to enhance grassroot development. The percentage should be changed from the present percentage (15% in 2006 to about 52% to allow for the development of the rural areas which would prevent the rural shift to urban centre.

Conclusion

This paper has examined local governments tax mobilization and utilization in Nigeria. Local Governments in Nigeria receive statutory allocation from both the federal and state governments. They also generate internal revenues through taxes and fees, etc. It is opined that expenditure assignment should match with revenue generating powers in order for local governments to discharge their functions effectively. In essence, revenue and expenditure decentralization must support local government public revenue profile.

Local government’s revenue generation in Nigeria needs restructuring so that taxing powers be given to local authorities and also she should be allowed to share major tax bases with other levels of government to enable enough independent funds for development

Local governments should strive towards improving internally generated revenue and instill transparency and accountability in their management structure. This can be effectively carried out through community participation in their various activities. Need to carry people along in the execution of the projects would encourage administrative openness and accountability.

Local governments which constitute the areas mostly endowed with natural resources should be allowed to woo foreign investors for the development of their abundant resources. This will improve their revenue generation base and create job opportunities for the people.

In conclusion, for local governments to act as agents of development at the grassroots, their share of total public sector expenditure should be substantially increased through increase allocation from the federation accounts.

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