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FISCAL FEDERALISM AND ECONOMIC GROWTH IN NIGERIA

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Abstract: *Persistently, it is being insinuated that Nigerian federalism is one of the major challenges hindering the country's economic growth and development. This study analysed the effects of fiscal federalism on the growth of the Nigerian economy. This study made use of data on annual revenue allocations to the federal, state, and local governments, and annual investments, as the independent variable, and annual real Gross Domestic Product as the dependent variable. The study employed the Ordinary Least Square method for estimation, and the Augmented Dickey-Fuller Unit Root Test to check for the statistical properties of the variables. . The results show that it is only at the federal level that allocation is positive and significant. At the local government level, the allocation is positive but not significant and at the state level, it is even negative but not significant. Recommendations were made to improve the impact of fiscal federalism on economic growth in Nigeria; among such include the establishment of agencies to check for fraudulent activities in the lower levels of government, and a development of self-sustainable income levels by the lower levels of government.*

Keywords: *Fiscal; Federalism; Economic Growth*

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INTRODUCTION

Over the years, Fiscal federalism has been in practice in Nigeria and its relevance has been a subject of debate. Fiscal federalism refers relations between units of governance in a federal system of government.A country's level of economic growth and development can be measured using some criteria such as increase in the level of output, per capita real income,

economic welfare, ratio of industrial output to total output, and so on. Nigeria's performance using these criteria is below average compared to other countries of the world that share Nigerian experience. When considering per capita income, Nigeria has approximately 5,360 purchasing power parity,(PPP dollars) with a population of 173.6 million as at 2013 (World Bank, 2014). India's performance is relatively better than Nigeria, with population of 1.252 billion and a per capita income of $ 5,350 as at 2013 (Ibid.). China with a higher population is even a better example, with a population of 1.357 billion and a per capita income of $ 11,850 (Ibid.). These could be due to well-planned economy in India and China, primarily in the area of resource management. Nigeria possesses some similar traits with India, especially when considering years of independence, and high ratio of population to land area, and so on. Despite these similarities, Nigeria has not attained a commendable level of development, despite its vast human and natural resources. This observation calls for a study to identify the root of the problem and to subsequently proffer solutions.

LITERATURE REVIEW

Conceptual Issues

Federalism connotes a political system in which two or more levels of government control the same territory and citizens. It is a system of government that allows two or more entities to share control over the same geographic region (Collins, 2016.). The word *federal* comes from the Latin term *foedus,* meaning 'to trust'. A Country operating federal political system has both central and other smaller political units, usually called states, provinces, or territories. These smaller political units surrender some of their political powers to the central government, relying on it to act for the common good. Musgrave (1959) introduced the concept of fiscal federalism. He believed that the federal or central government should be responsible for the economic stabilization and income redistribution while the allocation of resources should be the responsibility of the state and local governments. Musgrave distinguished three functions of the public sector, which he grouped into Allocative function, Distributive, and Stabilization.

The Concept of Economic Growth

A number of people often use economic growth and economic development interchangeably as if they mean the same thing. This is an error

as Economic growth differs from economic development. Economic growth is the sustainable increase in the total output of goods and services produced in an economy over time. It is a positive change in the level of production of goods and services by a country over a certain period. Technological innovations and positive external forces usually lead to economic growth. Economic growth increases the capacity of an economy to produce goods and services (Investopedia). Economic growth according to Todaro and Smith (2006), is the steady process by which the productive capacity of the economy is increased over time to bring about increase in the levels of national output and income. Economic growth therefore occurs whenever people take resources and efficiently rearrange them in ways that make them more productive overtime. It is the continuous improvement in the capacity to satisfy the demand for goods and services; resulting from increased production scale, and improved productivity i.e. innovations in products and processes. In brief, economic growth brings new products, more outputs and wider options for consumers. According to Kindleberger (1965), "Economic growth means more output and changes in the technical and institutional arrangement by which it is produced and distributed. Growth may well involve not only more output derived from greater amounts of inputs but also greater efficiency, i.e., an increase in output per unit of input.

Friedman(2012), defined growth as an expansion of the system in one or more dimensions out of a change in its structure, while development is an innovative process leading to the structural transformation of social system. Thus, economic growth is related to a quantitative sustained increase in the country's per capita output or income accompanied by expansion in its labour force, consumption, capital, and volume of trade. Economic development, on the other hand, is a wider concept than economic growth. It is a growth plus qualitative changes in economic wants, goods incentives, institutions, productivity, and knowledge or the "upward movement of the entire social system" (Mydral, 2012). Development describes the underlying determinants of growth such as technological and structural changes. Economic growth is a necessary but not sufficient condition for economic development. An economic growth may not translate to development. In other words, an economy may experience growth with prevalence of poverty, unemployment, and inequalities. Todaro (2006) defined Economic

development as an increase in living standards, improvement in self-esteem, needs and freedom from oppression as well as a greater choice. The most accurate method of measuring development is the Human Development Index. It takes into account the literacy rates and life expectancy, which, affects productivity and could lead to further economic growth and creation of more opportunities. Economic development also implies an increase in the per capita income of every citizen.

Theories on Fiscal Federalism

The theories of Fiscal Federalism are trace able to the works of Kenneth Arrow, Richard Musgrave and Paul Samuelson. Samuelson's work on the theory of public goods in 1954, Musgrave's work on public finance in 1959, and Arrow's discourse on the roles of the public and private sectors 1970 all offered a framework for analysing the role of the state in the economy. The theory was later referred to as "Decentralization Theorem".

The framework identified some vital roles for the central government, which are:

i. Correcting market failure,
ii. Equitable income distribution
iii. Macroeconomic stabilization at full employment and
iv. Stable prices (Musgrave, 1959).

"The government was expected to step in where the market mechanism failed and to maximize social welfare due to various types of public goods characteristics". (Ozo-Eson, 2005). The theory, which was later tagged "Decentralization Theorem" by Oates (1999) focused on the situation where different levels of government will provide public goods "whose special patterns of benefits were encompassed by the geographical scope of their jurisdictions" (Oates, 1999: 5). Such situation came to be known as "perfect mapping" or "fiscal equivalence". Arowolo, (2011), properly explained the roles of government at different levels. In his words:

> "It was also observed that there was hardly any level of government that could produce a perfect mapping for all public goods due to variance in consumption along different levels of government. Thus, it was recognised that there would be local public goods with inter-jurisdictional spill-overs."

For example, the benefits, which are enjoyed by road users, may go beyond users in the local jurisdiction within which the road is confined. The local

authority because of this, may decide to ignore the need for such a good and not provide for it. To avoid this, the theory then resorts to a situation whereby the central government is required to provide matching grants or adequate loans to the lower level government in order to internalize the full benefits. Based on the preceding paragraph, he continued by stating, "The role of government in maximizing social welfare through public goods provision came to be assigned to the lower tiers of government. The other two roles of income distribution and stabilisation were, however regarded as suitable for the central government. From the foregoing, one can summarize the role assignment following from the basic theory of fiscal federalism thus; the central government is to ensure equitable income distribution, maintain macroeconomic stability, and provide public goods that are national in character. Other lower levels of government are to focus on the provision of local public goods with the central government providing targeted grants in cases where there are jurisdictional spill-overs associated with local public goods. Once the assignment of roles has been taken care of, the next thing is to determine the appropriate taxing framework. In addressing this, attention is paid to the need to avoid distortions resulting from decentralized taxation of mobile tax bases. Gordon (1983) emphasized that the extensive application of non-benefit taxes on mobile factors at decentralized levels of government could result in distortions in the location of economic activity.

Ozo-Eson, (2005), observed that following from the assignment of functions, taxes that matched more effectively the assigned functions were also assigned to the relevant tier or level of government. For example, progressive income tax is suited to the functions of income redistribution and macro-economic stabilisation and is therefore, assigned to the central government. On the other hand, property taxes and user fees were deemed more appropriate for the local governments. Benefit taxes are also prescribed for decentralized governments based on the conclusion that such taxes promote economic efficiency when dealing with mobile economic units, be they individuals or firms. The final element of this basic theory that is worthy of note is the need for fiscal equalization. This is in the form of lump sum transfers from the central government to decentralized governments. The arguments for equalization were mainly two. The first, which is on efficiency grounds saw equalization as a way of correcting for distorted migration

patterns. The second is to provide assistance to poorer regions or jurisdictions. Equalization has been important in a number of federations. For example, Canada has an elaborate equalization scheme built into her inter-governmental fiscal arrangements (Weingast, 1995). It should be pointed out however, that recent literatures emphasize the importance of reliance on local revenues for financing local budgets. Arowolo (2011) drawns attention to the dangers of decentralized levels of government relying too heavily on intergovernmental transfers to finance their budgets.

THEORIES ON ECONOMIC GROWTH

The Malthusian Theory

Thomas Robert Malthus, famous for his theory on population, recognized the importance of distinct and systematic theories of growth. He contributed to economic development in a section of his book *"Principles of Political Economy",* titled "The *Progress of Wealth".* Malthus saw the concept of economic development as a dynamic one. He did not view it as something that automatically takes place when certain factors are fixed. Rather, his perception of development was a process involving peak and slump levels in economic activities with no constant trend of upward movement. Malthus was concerned with the "progress of wealth" of a country. By progress of wealth, he meant economic development, which could be achieved by increasing the wealth of a country. The wealth of a country could be analysed based on the quality of products obtained by its labour, and partly upon the valuation of these products. Although, according to him, "the wealth of a country does not always increase in proportion to increase in value, because an increase in value may sometimes take place under an actual diminution of commodities."

While explaining the role of production and distribution in economic growth, Malthus regarded production and distribution as "the two grand elements of wealth". If they are combined in the right proportions, they can increase the wealth of a country in a short time. But if they are taken separately or combined in unsuitable proportions, it may take many thousands of years to cause an increase in wealth. So Malthus emphasized on maximum production and optimum allocation of resources for increasing the wealth of a country during the short run. According to him, the source of capital accumulation is higher profits, which come from the savings of

capitalists because workers are too poor to save. Malthus suggested the concept of "optimum propensity to save". By this, Malthus meant that savings should be directed towards earning more profit that is, a conversion of revenue into capital. He concluded that savings pushed to excess would destroy the motive of production and probably restrict expansion of the scale of production.

The Harrod–Domar Model

Both Harrod and Domar are interested in discovering the rate of income growth necessary for a smooth and uninterrupted working of the economy. Though their models differ in details, yet, they arrive at similar conclusions. Harrod and Domar assigned a key role to investment in the process of economic growth. They laid emphasis on the dual character of investment. Firstly, it creates income, and secondly, it augments the productive capacity of the economy by increasing its capital stock. The former may be regarded as the "demand effect" and the latter as the "supply effect" of investment. Hence, so long as net investment is taking place, real income and output will continue to expand. However, for maintaining a full employment equilibrium level of income from year to year, it is necessary that both real income and output should expand at the same rate at which the productive capacity of the capital stock is expanding. Otherwise, any divergence between the two will lead to excess or idle capacity, thus forcing entrepreneurs to curtail their investment expenditures. Ultimately, it will adversely affect the economy by lowering incomes and employment in the subsequent periods and moving the economy off the equilibrium path of steady growth. Thus, if full employment is to be maintained in the long run, net investment should expand continuously. This further requires continuous growth in real income and at a rate sufficient enough to ensure full capacity use of a growing stock of capital. This required rate of income growth rate may be called the "warranted rate of growth" or the "full capacity growth rate". The Harrod–Domar model describes the economic mechanism by which more investment leads to more growth. It states that for a country to develop and grow, it must divert part of its resources from current consumption needs and invest them in capital formation. Diversion of resources from current consumption is called saving. Hence, the government should focus more on planning for capital expenditure and direct its resources/savings towards efficient establishment of capital structures that will boost its growth and

development. While saving is not the only determinant of growth, the Harrod–Domar model suggests that it is an important ingredient for growth. Its argument is that every economy must save a certain proportion of its national income if only to replace worn-out of capital goods. The model shows mathematically that growth is directly related to saving and indirectly related to capital-output ratio. Suppose national income is defined as Y, growth as G, capital output ratio as K, saving as S, and investment as I, and average saving ratio as s, and incremental capital-output ratio as k, then a simple model of economic growth can be constructed as follows:

$S=sY$ ……..1
i.e. saving (S) is some proportion of (s) of national income (Y)

$I=\Delta k$……..2
I.e. investment (I) is defined as the change(Δ) in capital stock k

$G=\frac{\Delta y}{y}$……..3
i.e. growth is defined as change in National income (ΔY) divided by the value of the National income.

Since the total stock, K bears a direct relationship to total national income, or output Y, as expressed by the capital-output ratio k, then, it follows that:
$\frac{K}{Y}= k$ ……..4
Or $\frac{\Delta K}{\Delta Y} =k$

Finally, since total national savings (S), must equal total investment, (I) this equality can be written as:
$S=I$ ……5

But from Equation (1) above, recall that S = sY and from Equations (2) and (3), it is known that
$I = \Delta K = k \Delta Y$

It therefore follows that the identity of S=I in Equation (6) can be written as
$S=sY=k\Delta Y = \Delta k = I$ ……..6

Or simply as
$sY=k\Delta Y$……7

$\frac{\Delta Y}{Y} = G = \frac{s}{k}$ 8

Now by dividing both sides of Equation (7) by Y and later by K, the growth Model ΔY/Y is derived, which represents the rate of change of national income or rate of GNP (i.e., It is the percentage change in GNP). Equation (8), which is a simplified version of the famous Harrod –Domar equation in the theory of economic growth, implies that the rate of growth of GNP (ΔY/Y) is determined jointly by the national saving ratio, S, and national capital/output ratio, k. More specifically, it says that the growth rate of national income will be directly or positively be related to saving ratio (i.e. the more an economy is able to save and invest out of given GNP, the greater the growth of that GNP) and inversely or negatively; relate to the economy's capital/output ratio (i.e., the higher the K, the lower will be the rate of GNP growth). The economy logic of equation (8) is very simple. In order to grow, an economy must save and, therefore invest a certain proportion of their GNP. The more an economy can save, the more it can grow because the rate of growth depends on how productive the savings is. That is, how well such savings can be invested to result in growth.

The Traditional Neoclassical Growth Theory

Neoclassical growth theory up to the late 80s is known as Traditional Growth theory. It is a summary of neoclassical growth theory up to the 1980s and is primarily based on Solow's Neoclassical Growth model. Solow's growth model was an extension of Harrod-Domar growth model and like the Harrod-Domar model; it stressed the importance of savings. Solow's model was considered to be an improvement over Harrod-Domar model, because it showed how the liberalization of national markets could draw additional domestic and foreign investment and thus increase the rate of capital accumulation. Solow extended Harrod-Domar model in two ways. First, he considered labour as a second factor of production. Second, he introduced a third independent variable, technology. Most importantly, unlike the fixed coefficient, constant returns to scale assumption of the Harrod-Domar model, Solow's model exhibited diminishing returns to labour and capital separately and constant returns to both factors jointly. Technological progress became the residual factor in Solow's model, explaining long term growth. Its level was assumed to be determined exogenously and independent of all other factors. Production Function in Solow's model:

$Y=Ae^{\mu t}K^{\alpha} L^{1-\alpha}$

Where, Y = GDP, K = stock of human and physical capital, L = unskilled worker, A = constant, representing the base level of technology, $e^{\mu t}$ = constant exogenous rate at which technology grows. α is the elasticity of output with respect to capital and assumed to be less than one. The above formation of Solow's growth model yields diminishing returns to capital and labour. i.e., $MP_K < AP_K$ and $MP_L < AP_L$. Traditional Growth theory, on the basis of Solow's growth model, explained that since in the developed countries, capital is relatively more abundant compared to the developing countries, according to the law of diminishing returns, capital would have a lower return in the developed countries compared to the developing countries. As a result capital would have a natural tendency to go towards the developing countries where the rate of return is higher. So from the developing country's context, the best strategy would be to open up the country to foreign capital and to remove all restrictions on inflow of foreign capital.

In accordance with the traditional neoclassical growth theory, output/economic growth results from factors, which include increases in labour quantity and quality (through population growth and education in which public fund is been expended upon), and improvement in technology. This proves the importance of revenue allocation formula and other factors and how they are crucial to rapid economic growth and development.

Review of Empirical Literature

Dare Arowolo (2011) wrote on "Fiscal Federalism in Nigeria: Theory and Dimensions". His work focused on the causes of dissatisfaction arising from the revenue allocation formula. The paper adopted analytical methods which relied on secondary data, and it also adopted primary data by interviewing prominent figures involved in the resource allocation process. Arowolo concluded that the hegemony of the federal government and its extended period and nature of interregnum rule in the military era are some of the factors that contribute to the constant conflicts associated with fiscal federalism in Nigeria. Saibu M.O. and Adedokun S.A. (2006) wrote on "Fiscal Federalism and the Growth of the Nigerian Economy. The paper examined the relative effects of the state and federal government share in expenditure and revenue on the economic growth in Nigeria, using annual

time series data from 1980 to 2004. The variables were examined using the Ordinary Least Square estimation technique. The result showed that there was significant difference in the effects of state government shares and federal government shares on economic growth. Specifically, while state government shares had positive albeit insignificant effects, the federal share had positive and significant effects on economic growth. In conclusion, Saibu and Adedokun stated that more fiscal power should be devolved to the state and an effective mechanism should be put in place to ensure that resources are efficiently utilized in all tiers of government without political prejudice. Sam O.et al conducted a research on Fiscal Federalism in Nigeria, using a cluster analysis of revenue allocation to states and local government areas, from 1999 to 2008. The results from cluster analysis showed that a small number of states constituting each of the clusters in terms of statutory allocation, VAT and net statutory allocation occupied the range of values for highest and lowest allocations. Specifically, the South-East zone was found to be the least beneficiary of statutory allocations. In the case of VAT, North-West zone benefited more than other zones while North-Central zone dominates the cluster of least beneficiary states. The story changed completely in the case of net statutory allocation. The oil producing states received the largest net statutory allocation above Lagos and Kano the most industrialized states in Nigeria basically because of the derivation fund enjoyed solely by them. Owolabi Usman (2011) wrote on Fiscal Federalism and Economic Growth Process in Nigeria, in which he applied the Ordinary Least Square estimation technique to analyze a series of secondary data. The results obtained from his regression analysis showed a direct relationship between the revenue allocation formula as proxies by the share of federal, state, and local government from the federation account and economic process in Nigeria. He concluded that macroeconomic stability can be maintained by controlling the rate of inflation within reasonable limit is required to promote economic growth and development.

Femi Omotosho (2010), wrote a work titled "Nigerian Fiscal Federalism and Revenue Allocation Formula for Sustainable Development in the Niger Delta". The study focused on the imbalance associated with the systems which have combined to affect the Nigerian federal system as a whole. The data used in the study was secondary, but the estimation technique used was not specified. The results showed that the lack of sustainable development in

the Niger Delta region is traceable to imbalances in the revenue allocation which the government gives to the region. Omotosho concluded by recommending the use of the derivation principle for sharing of revenue so as to promote sustainable development and reduce tension in the Niger Delta region. Aladesanmi Kayode (2010) wrote on Fiscal Federalism and Economic Growth in Nigeria. The study examines the relationship between fiscal federalism and economic growth in Nigeria using data on an annual basis from 1980 to 2005. The study employed co-integration technique to estimate the parameters in the model. The results showed that fiscal federalism and economic growth were positively related mostly at the federal level, least positive at the local government level, but inversely related at the state level. Aladesanmi concluded that both states and local governments did not have significant fiscal impact on the economic growth of their respective regions.

Research Design

The method adopted in this study involves multiple regressions, employing the Ordinary Least Square (OLS) technique and Augmented Dickey-Fuller Unit Root test. The research was based on time series analysis, and the specified model was analyzed using the Unit Root Test and the Ordinary Least Square Method. The data used in this research is secondary. It was sourced from a government publication (Central Bank of Nigeria Statistical Bulletin, 2013 edition). The data sourced included Real Gross Domestic Product (RGDP), Total revenue collected from the federation account at the federal, state, and local government levels, gross fixed capital formation, and increase in stocks.

Presentation of Result:

Unit Root Test

All variables were tested with intercepts and maximum lag of 4 at level, first difference, and second difference, and the results for each were as follows:

Augmented Dickey-Fuller Unit Root Test

Variables	ADF Test Statistic (ADF*)	5% critical value	Order of Integration
RGDP	-5.744401	-3.052169	I(2)
FGR	-3.921864	-3.052169	I(1)
SGR	-6.064724	-3.081002	I(2)
LGR	-4.861557	-3.040391	I(1)
INV	-6.454053	-3.065585	I(2)

Source: E-views Software

I(0) = level, I(1) = first difference, I(2) = second difference.

From the above decision rule,

RGDP becomes integrated at the second order. Hence, it is not stationary.

FGR becomes integrated at the first order. Hence, it is not stationary.

SGR becomes integrated at the second order. Hence, it is not stationary.

LGR becomes integrated at the first order. Hence, it is not stationary.

INV becomes integrated at the second order. Hence, it is not stationary.

Regression Results by Ordinary Least Square (OLS) Method

Dependent Variable: RGDP
Method: Least Squares
Sample: 1993 -2012
Included observations: 20

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	345.1672	6.524629	52.90220	0.0000
FGR	0.058308	0.017539	3.324449	0.0046
SGR	-0.071280	0.051611	-1.381086	0.1875
LGR	0.127880	0.122888	1.040622	0.3145
INV	0.042665	0.008267	5.161067	0.0001

R-squared = 0.992222, Adjusted R-squared = 0.990148, F-statistic = 478.3732, Durbin-Watson statistic = 1.955482.

Source: Authors' Computation

R^2

From the results, R^2 and the adjusted R^2 show that the variables fit very well into the model at levels of 0.992222 and 0.990148 respectively. This means that the total variation in RGDP explained by FGR, SGR, LGR, and INV is more than 99%. Unexplained variables (i.e. variables not included in the model) account for less than 1% of the remaining variation in RGDP in Nigeria during the period under review.

Durbin-Watson

If $0 < d^* < d_L$ .....There is positive autocorrelation
If $d_L < d^* < d_U$.....The results are inconclusive
If $d_U < d^* < 4-d_U$ .....There is absence of autocorrelation
If $4-d_U < d^* < 4-d_L$ .....The results are inconclusive
If $4-d_L < d^* < 4$ .....There is negative autocorrelation
With respect to the samples used, where number of samples (n) = 20 and number of explanatory variables excluding the constant intercept (k) = 4, d_L = 0.90, d_U = 1.83.From the analysis, d^* lies between $d_U$and 4- d_U, having a value of 1.955482. Hence, there is absence of autocorrelation in the model.

F-Statistic

H_0: $\beta_1 = \beta_2 = \beta_3 = \beta_4 = 0$. The explanatory variables do not have any significant impact on the dependent variable. Hence, the overall variables in the model are not significance.
H_1: $\beta_1 \neq \beta_2 \neq \beta_3 \neq \beta_4 \neq 0$. The explanatory variables have significant impact on the dependent variable. Hence, the overall variables in the model are significant.
The test is done at a 5% level of significance
$F_{0.05}$ at n – k degrees of freedom (where n = 20 and k = 4) = 3.63

The f-statistic, which jointly tests the significance of all parameters estimated in the model is statistically significant at 5% level, with a value of 478.3732 which is higher than the $F_{0.05}$ (3.63). Hence, H_0 is rejected and H_1 is accepted, meaning there is overall significance of all the parameters in the model.

A priori Conformity

Variable	Coefficient	A priori expectation	Conformity
FGR	0.058308	$\frac{\partial GDPR}{\partial FGR} = \beta_1 > 0$	Conforms
SGR	-0.071280	$\frac{\partial GDPR}{\partial SGR} = \beta_2 > 0$	Does not conform
LGR	0.127880	$\frac{\partial GDPR}{\partial LGR} = \beta_3 > 0$	Conforms
INV	0.042665	$\frac{\partial GDPR}{\partial GXP} = \beta_4 > 0$	Conforms

From the table, it is observed that all the variables, excluding SGR have a direct relationship with the dependent variable, RGDP. SGR on its own has a negative relationship with RGDP. Hence, if FGR, LGR, and INV increase or

fall, a corresponding effect will be felt on RGDP but if SGR increases or falls, it will have an opposite effect on RGDP. This inverse relationship corresponds with Aregbesola's statement. It shows that the state misuses the revenue it gets from the federation, making it a waste and a deduction from the country's income instead of investing it in areas that will add value to the national income.

CONCLUSION

From the research done, the research concludes that the state and local governments have no significant impact or contribution to the growth of the Nigerian economy or their respective regions. This means that despite the many adjustments made since inception of fiscal federalism in Nigeria, the state and local governments still face problems when performing their fiscal duties in their respective regions. Also, the negative relationship found in the state connotes that the states use their allocations in other areas that do not contribute to economic growth. One wonders what the state does with the allocations it receives. The problem may not necessarily be from the amount allocated to the states and local governments. Rather, the problem originates from the use of these allocations.

Policy Recommendations

In line with Saibu and Adedokun's suggestion, agencies should be put in place to monitor the use of revenue by each state, and ensure that such use is in line with the nation's objectives for growth and development and not frivolous activities. Sharing of revenue should also be diversified, so as to help develop areas and regions which do not contribute much to the national income i.e. horizontal allocations should not be fully based on proportion of revenue the region adds to the federation account, but the principle of basic needs and fiscal efficiency should be adopted. If the federal government shares are based primarily on what it gets from each state and local government, those states and local government areas will continue to grow and develop till they reach a certain stage, while the others will remain unproductive. Hence, revenue should be spread across different governments to give them equal chances for development.

In addition, the main beneficiaries of the nation's development (i.e. the public) should be given attention, and be allowed to advice to some extent

on the kind of areas that will be of greatest importance to them if the government invests in it. Ideas can be shared through public opinion polls and public hearings. This will avoid waste of resources and better management of facilities, due to their relative importance to the public. Finally, the lower tiers of government should not rely completely on the higher ones for its revenue. Each state and local government should be able to attain a level of self-sustenance when allocations are removed. For example, in 2012, the states' internal revenue stood at 548.1, which accounted for about 15 percent of the states' total revenue. The federation account allocations to the states summed up to 1,857.0, which made up about 52 percent of the states' total revenue. Value Added Tax (VAT), grants, stabilization funds, and others accounted for the remaining percentage of the states' revenue. This low contribution of the states themselves to their total revenue should be corrected.

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