FINANCING FEDERAL GOVERNMENT EXPENDITURE IN NIGERIA (1980 - 2003)

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CERTFICATION

This is to certify that the research thesis was carried out by KANU, SUCCESS IKECHI of the Department Of Financial Management Technology, Federal University Of Technology, under the supervision of Dr. L. E. Akujuobi and is hereby admitted as having partially satisfied the requirement for the award of the degree of Master of Science (M.Sc) in Financial Management Technology Of the University.

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(DEAN, POST GRADUATE SCHOOL) DATE

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EXTERNAL EXAMINER. DATE

DEDICATION

To my darling wife - Mrs. Obumneke Chineme – Ikechi Kanu.

She stood in the gap for me, provided an enabling environment and

Worked tirelessly for this work to come to fruition.

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Finally, I want to thank god for the journeying mercies He granted me in the course of this program-

KANU SUCCESS IKECHI

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ABSTRACT

This study seeks to assess the relationship between various sources of finances available to the Federal Government of Nigeria and her expenditure pattern. This study was carried out using secondary data collected from the Central Bank of Nigeria's Statistical Bulletins and her Annual Reports for the period 1980 to 2003. The contributions of the various sources of finance were compared with the total expenditure. From the findings of this study, strong and significant relationships exist between the various components of federal government financing and her total expenditure profile, except for one variable – external grants received by the federal government. While the capital expenditure of the federal government has been significantly financed through dedicated accounts / special funds, federal government independently generated revenue and external loans; her recurrent expenditure needs were financed by allocation from federation accounts, internal loans and dedicated accounts / special funds. The outcome of this study has shown that the federal government of Nigeria does not generate enough funds to finance her expenditure profile. This deficit, she augments through external and internal loans. Based on the findings, several recommendations were made, the major ones being that there is a need to diversify our economy and change the revenue structure of the federal government. This must become significantly based on domestic production activities in contrast to the ages long dependence on export of primary commodities (be they agricultural commodities or crude oil).

Again, the level and composition of public expenditure should form an integral part of the macro economic framework of reform measures.

Perhaps, this could be the best way forward!

CHAPTER ONE

1.1 BACKGROUND OF STUDY

Financing of federal government's expenditure in Nigeria falls within the purview of public revenue and expenditure. According to Anyafor (1996), public expenditure refers broadly to expenditure made by Local, State and national agencies as distinct from those of private individuals, organizations or firms.

Nnamocha (2001:128) described government or public expenditure as the expense of government for its own maintenance and on the society and the economy as a whole. It is becoming more difficult to split public expenditure into expenditure for government maintenance and expenditure for the benefit of the society and the economy. This is because the state is getting increasingly involved in economic activities and in transfer payments to other governments and countries.

This explains the growing role and significance of public expenditure. As a result, public expenditure has maintained upward trend over time in virtually all countries.
The definitions of public expenditure are mainly influenced by either a macro or micro perspective of what constitutes public expenditure. The macro perspective tends to perceive public expenditure as one aggregate in the national economic accounts that is likely to impact on the macro economy, including issues of inflation, unemployment and interest rates.

In contrast, the micro perspectives concentrate on individual expenditure program and the implication of changes in expenditure and policy outputs.
Successive Nigerian governments since the attainment of independence in 1960 have been geared towards promoting economic growth and development. This, she has been able to attempt through direct government expenditure and / or indirectly through policies aimed at stimulating private spending into various sectors of the Nigerian economy.

On the other hand, public revenue as a concept refers to the sources and structure of government revenue.

According to Nnamocha (2001:75), prior to 1984, Nigeria's major sources of public revenue could be grouped into tax and non-tax revenues. However, from 1984, a new reporting system for Nigeria's revenue profile was adopted. This consisted of oil revenue, non-oil revenues, internally generated revenue, and revenue profile from dedicated accounts, federal allocation and loans.

A valid relationship between public revenue and expenditure in the economic policy of any nation gives rise to economic growth and development. Economic development is generally defined as aspects of the life of the entire citizenry. Such improvements are generally manifested in greater number of useful jobs for employable persons, higher level of real income, better health condition, better housing facilities, high level of education, more and better government presence/ services.

From the foregoing therefore, the primary purpose of the government is to provide basic infrastructures, amenities and services that would lay foundation for enhancement of citizens' welfare. These also are necessary for economic growth and development to take place. A responsive government at whatever level therefore ensures that at least, greater populations of the citizenry are provided these necessities of development as much as possible.

In fact, for this economic development which is one of the cardinal objectives of the government to take place, there must be this basic framework through which the fluid of development flows.

Any country which lacks this important bedrock of development, always finds it difficult to experience any meaningful development.

Development as conceived is a multi-dimensional process involving changes in structure attitudes and institutions as well as the acceleration of economic growth, the reduction of inequality and eradication of absolute poverty (Nnadi, 1997). The result being that, individuals as well as social groups in the system move away from a condition where life is widely unsatisfactory to a state of life considered materially and spiritually better.

Therefore, growth and development whether in an urban or rural setting are consequent on the availability of infrastructure that provide essential utilities and services necessary to improve standard of living.

These utilities and services form the central catalyst that induce population growth which is the basic footing on which development activities stand as well as the principal ingredient for development.

In the first place, they offer prospects for better living through the provision of such services as electricity, pipe-borne water, health care services and more readily available modes of transportation and communication.

Secondly they also provide many prospects for employment and other forms of economic activities. When this happens, it can be said that the operating economies and other related facilities will emerge and improve.

Hence, one might rightly ascribe that for effective and meaningful development to be achieved in an area, it must be backed up with the provision of adequate infrastructural facilities.

Simply stated, public utilities are those goods and services declared to be wholly within the domain of government and whose provision and distribution are done though government agencies and facilities. These agencies or faculties are therefore service oriented (Adams Smith, 1767).

Services rendered are either delivered to the consumers through network system such as telephone lines, water pipes etc. Also other services can be obtained from facilities that have point systems as exemplified by post offices and fire services. Either way both systems require a particular type of access in order to obtain maximum efficiency of function. This maximum efficiency of function can only be provided by location convenience to mass transit lines and preferably close proximity to residential neighborhoods. The former needs a location which links it closely to consumers.

Government involvement is in the provision of certain goods and services. The essence of government is for the well being of the society and its direct involvement in provision of goods and services was made prominent during the period of classical economies.

The major tenets of the economies as popularized by Adam Smith (the founding father), include the promotion of competition and general maximization of welfare. He came up with three major functions that every government worth its name should perform in an independent state.

According to Adams Smith, the three major functions independent states must perform for its citizens are, one, protection of the society from violence and evasion of other independent society, a function which can be best performed by means of the military.
Secondly he believed in the administration of justice in order to protect as far as possible any member of society from oppression and any form of injustice. The third, is the erection of those public institutions and works which may be in the highest degrees advantageous to the society, however of such a nature of depth the profit could never repay the expense to any individual or small number of people could not erect or maintain.

Economic development is also manifested in the greater ability of people to draw on domestic resources to solve their problems. Economics development is more subjective than economic growth and can be measured by the gross domestic product (G D P).
A study of public revenue and expenditure in Nigeria is very relevant as the fiscal viability of any government is measured by the government's revenue ability to match its expenditure profile.

From 1980 to date, the federal government has recorded budget surplus only twice i.e. in (1995 and 1996).The trend has always been that of deficit budgeting. This has continued unabated even till 2005.

An investigation of federal governments expenditure profile shows that it has obeyed an increasing trend, which is in conformity with Wagner's law of rising public expenditure. Federal governments expenditure increased from ₦14.11 billion in 1980 to ₦ 60.26 billion in 1990. The figure increased from ₦ 701.05 billion in 2000 to ₦ 1225.95 billion in 2003.

If the trend of government expenditure continues, and this is very likely, then government revenue must be made to obey the same trend in order to avert or eliminate a continued budget deficit, which has become the order of the day.
An extensive review of this background information will form the bedrock of this research work.

Consequently, this study takes an in-depth look into the sources of financing available to the Federal Government of Nigeria, with a view to proffering adequate policy measures necessary to curb or at least, reduce the ever-increasing problem of deficit financing in the country.

1.2 STATEMENT OF THE PROBLEM

From 1970 to 2003, Nigeria as a nation has witnessed both the military and democratic forms of government. Each government harnessed the resources of the nation to execute its budget.

For instance, the Central Bank of Nigeria (Economic Revenue, various years), reports that between the years 1980 to 2005, Nigeria experienced budget surplus only in the years 1995 and 1996.Furthermore, this rising deficit budget has been accompanied with some attendant economic problems, such as underdevelopment, mounting debt burden, deficit financing and inadequate basic amenities.

Ironically, there has been an increase in government's expenditure pattern over time. The nation has witnessed a tremendous increase in our revenue base especially the accruals from oil exports. The trend in world oil market both in terms of increased output and price has prompted the increase in our revenue base.

Paradoxically, it does not appear that the increase in revenue is not at par with government's expenditure profile. It has certainly obeyed Wagner's law of increasing public expenditure.

From all indications, federal government is saddled with a lot of responsibilities. The natural question to ask is if the federal government is capable of pulling through in her constitutionally assigned roles / responsibilities.

This question has become necessary in view of repeated complaints by all tiers of government over inadequate sources of funds to carry out their functions and an ever-increasing trend of deficit financing in our nations polity.

Against the above background, there is an urgent need for a quick review of the total revenue base of the nation. This should be in line with her total expenditure profile.

Hence, there is the need for a proper empirical investigation of the problem of financing Federal Government expenditure with a view of determining the available financing options necessary to realise Federal Government budgeting responsibilities.

1.3 THE OBJECTIVES OF THE STUDY

The purpose of the study is to identify those variables that make up the major sources for funding of government's expenditure. Again, we will attempt to ascertain the relationship between government's sources of revenue and her expenditure pattern in Nigeria over time. In general objective of this study is to investigate if federal government has enough funding sources to discharge her enormous tasks and constitutional responsibilities.

Specifically, this study will however, consider the following objectives:

a) Analyze the composition and pattern of federal governments Revenue
b) Analyze the level of public expenditure in Nigeria.
c) Develop and estimate models to explain / determine the size of Nigeria's public expenditure over time and
d) Assess how the federal government has financed its capital expenditure. This is to see the extent to which loans, grants and dedicated are being used by the federal government.
e) Assess how the federal government has financed her recurrent expenditure. This is to ascertain the extent to which internally generated revenue and allocations from the federation account are being utilized by the federal government.
g) Lastly, draw up policy implications as well as make suggestions based on findings.

1.4 RESEARCH QUESTIONS

This research work is aimed at subjecting available data to further analysis in order to answer the following questions:

1. What are financing options available to the Federal Government towards meeting its budgetary demands?

2. What is the nature of relationship between the Federal Government financing sources and its total expenditure?

3. To what extent has the Federal Government financing sources been able to meet its capital expenditure?

4. To what extent have the Federal Government financing sources influenced the level of its recurrent expenditure provision?

All these and many more will be answered in course of this research work.

1.5 HYPOTHESES FORMULATION

The following hypotheses are therefore formulated for the study:

Ho_1: There is no significant relationship between Federal Government financing sources and expenditure.

Ho_2: Federal Government revenue sources are not significantly related to capital expenditure.

Ho_3: The level of Federal Government recurrent expenditure is not significantly affected by its revenue sources.

1.6 SIGNIFICANCE OF STUDY

There has been much commentary on the importance of the relationship between government financing, expenditure and economic development.

Invariably, must of this concern has focused on some of the background theories that government expenditure should fuel economic growth and hence should encouraged.

However, some other schools of thought have continued to query these growth-enhancing theories, citing the inefficiency of public management of funds and its attendant problem of "crowding out effect" of investments as why much government expenditure should be discouraged.

Regrettably, not much work appears to have been done empirically, to ascertain the Nigerian experience. Hence, this study will be of great importance to some categories of people in Nigeria.

First, policy makers, by this study, are presented with a veritable tool for policy formulation. Recalling that the work establishes the composition of Federal Government financing sources as well as its expenditure profile, it becomes easier to present a prediction model for financing Federal Government expenditure and therefore contribute economic development. This research work will be of huge importance to different groups of people. One group comprises of students. This research work will help them to clearly articulate and appreciate the concept of

a) Crowding out: in the early 70's and 80's, it was expenditure on defense and security that crowded out productive expenditure. However, since the early 90's, federal government budget and expenditure has over crowded that of the states and Local governments.
b) Fiscal federalism and reasons for agitation by some sections of the country on increased revenue and calls for control.

Another group is the political class. Be it at the federal, state or Local government Levels. They will find this work relevant in the sense that it contains useful hints and analysis of government's revenue and expenditure profile. A politician who is all out to impact positively on the lives of his people will seek to improve on their welfare and consequently be improving on the nation's gross domestic product. This work will enable any government in power to stamp her feet on the sand of time, with the provision of basic amenities and infrastructures. There is a need to embark only on meaningful and people oriented projects.

Political economists and technocrats are not left out. This study will generate keen interest and a possible argument on the relationship between public finance, expenditure and economic development. This work will throw more light on how/ where the economic barometers of our nation are tilting.

Again, concerned members of the society will find the work useful, as it will aid them in offering constructive criticisms to the government in power.

Lastly, this study is also expected to serve as a reference material for future and further works in the area of public finance, expenditure and economic development of Nigeria.

1.7 SCOPE AND LIMITATIONS OF THE STUDY

Financing of governments expenditure is a very broad area. This study as a matter of fact is limited only to the Nigerian economy. Again, due to the overbearing influence of the federal over the state and local government; focus / emphasis was placed on the federal tier of government.

The period of investigation for this work is delineated to the period: 1980 to 2003; a period of 24 (twenty four) years.

The researcher was faced with a number of constraints, which tried to impede the progress of the research work. They include the following;

TIME: Considering the fact that this research work is part of the requirements of an academic program, in addition to the fact that work on it is limited to a short period of time within a year in which the entire masters program should have been completed, it becomes obvious that one does not have all the time to make much contribution to the work.

LOW LITERATURE RATE: Inadequacy of indigenous literature on the subject matter of the research posed a big problem to the researcher. This is evident to the fact that, bulk of related literature referred to, in this study came mostly from foreign books.

FINANCE: inadequacy of funds formed the crux of the problem as the researcher could only reach some experts in the field of study. The researcher tried to access the internet but was unable to get access to some research works that relates to the research, this was as a result of the fact that access to such publications required paying money in foreign currency to the copy right owners through the internet before access can be granted. This was far beyond the reach of the researcher.

Again, the high cost of transportation to and from the Research Department of the central Bank of Nigeria, Garki Abuja and their currency centers in Owerri and Port Harcourt made extensive collation of resource materials quite expensive.

SECRECY OF INFORMATION: In Nigeria, to obtain valuable information for research purpose is usually very difficult because of either it's unavailability or inadequacy or both and restriction to its access. Most times, where data is obtained, it cannot be relied upon with absolute confidence because of the Inherent inaccuracies and distortions.

In spite of all these limitations, the researcher tried to get the best with the resources within his reach. However, the findings were not influenced by the above-mentioned limitations.

1.8 ORGANISATION OF THE STUDY

For the purpose of clarity and easy comprehension, it would be important to divide the research work into five-related chapters.

The first chapter is introduction of the research work, which encompasses the background of study, statement of problem, the objectives of the study, research hypothesis, scope, limitations and the significance of study.

The second chapter covers the review of literature. It involves the review of related past research works and the theoretical basis of the research topic and problems.

The third chapter is the research methodology. This covers the introduction, source of data, sample size, model development, test of hypothesis and the computer software used.

The fourth chapter involves data presentation, calculations, discussion of results, and model development for the relationships between financing of federal government's expenditure, test of hypothesis and discussions of result.

The fifth and final chapter is the summary, conclusion and recommendations of the study

CHAPTER TWO

REVIEW OF RELATED LITERATURE

2.0 INTRODUCTION

A study of financing federal government expenditure in Nigeria is important for several reasons. First, Nigeria's economy depend so much on accruals from a mono-product – oil. The dominance of oil in our economy is very risky, considering it's vagaries in the world oil market.

Secondly, the relative magnitude of government revenue, vis – a – vis it's expenditure profile has been on the increase.

Thirdly if the trend of government expenditure continues – and this is very likely – then government must make concerted efforts at diversifying her revenue base. Government revenue must be made to obey the same rise in trend. This is to avert or reduce / eliminate continued budget deficits.

Lastly, there is a need to ascertain if the expenditure pattern of the federal government is in tandem with her federally collected revenue.

A survey of most write – ups on this discuss portrays some common and interesting features .Most of such writings deal largely with the macro and micro influences on the financing of public expenditure.

Experience and knowledge gained from these writings coupled with the analysis of empirical data will form the basis of this research.

This literature review relied heavily on textbooks, manuals and some past-unpublished works relevant to the objectives of this study. It is sub – divided under the following headings:

(A). Theoretical frame work

- Wagner's law of increasing state activity
- Peacock and Wiseman's hypothesis of displacement effects.
- The critical limit hypothesis
- Musgraves theory of public expenditure
- The leviathan Hypothesis
- Other theories.

Canons, Effects and growth of public expenditure

Nigerian public expenditure: Profile and policies

(B) Sources of Government Revenue

- Taxation
- Export proceeds
- Dedicated Accounts
- Government borrowing and Deficit Financing
- Money creation
- Service Charges for governmental goods and services.
- Grants.

Nigeria's Revenue Structure and profile.

(C) Justification of public sector intervention in the provision of economic activities, infrastructural needs and general services.

- Historical Perspective
- Economic perspective
- Allocation functions
- Stabilization functions
- Distribution Activities.

The conventional wisdom on the assignment of functions and resources.

Federalism in Nigeria.

- Fiscal Federalism
- Principles of fiscal federalism
- Tax types and jurisdictions.

Revenues allocation scheme

- Principles upon which the scheme is based.
- Revenue allocation efforts in 1970's and early 1980's
- Vertical and Horizontal Allocations.
- Revenue allocation efforts since the establishment of Natural Revenue mobilization, allocation and fiscal commission (NRMA & FC).

2.2 THEORITICAL FRAMEWORK

Over the years, economists have examined the growth in the public sector very closely. They have developed some theories in an effort to explain this growth in the state sector. These theories have emphasized the explanation of increasing state expenditure. Such theories include:

(1) Wagner's law of increasing state activities
(2) Peacock and Wiseman's Hypothesis of Displacement effect
(3) Musgrave's theory of public expenditure growth.
(4) Critical limit hypothesis
(5) These theories are now discussed below.

2.2.1 WAGNERS LAW OF INCREASING STATE ACTIVITY

Writing in the 1880's; the German economist, Adolph Wagner advanced his "Law of rising public expenditure". He studied the German economy overtime and observed a correlative growth of national output and public expenditure in the economy. He expressed the view that there was an inherent tendency for the activities of the government to increase in size. Wagner observed in the relationship between the growth of an economy and the increasing activity of the state that there is an inherent tendency for the later to grow faster. He expresses the view that public expenditure increase at a faster rate than national output i.e. that the share of the public sector in the economy would increase as economic growth proceeds. This is the main thesis of Wagner: That the collective sector of an economy has an inherent tendency to increase in size and importance.

Wagners theory was supported by other writers like T.Nitti (   ).Nitti showed that the law also applies to various other countries like it does to Germany. Such inherent tendencies manifest themselves in the form of income elasticity of demand for public goods that is greater than unity, growth in population and economic growth and development, which must require improved infrastructural facilities, both social and economic.

The growth path in public expenditure is smooth and continuous over time as in the illustration below.

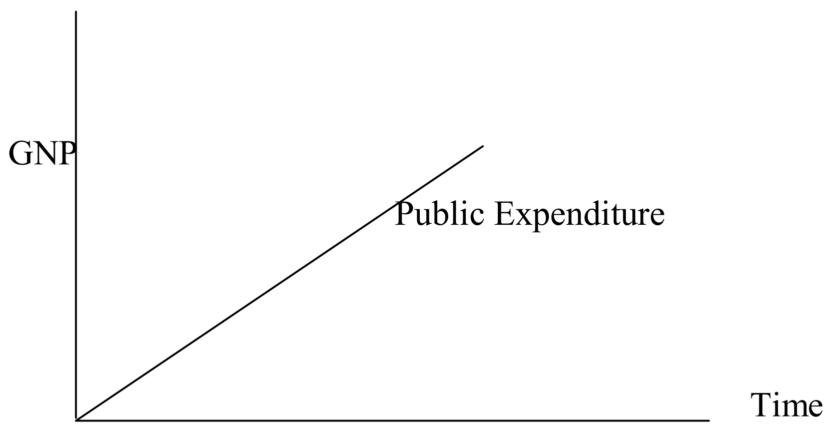

Fig 2.1 Law of increasing state activity

2.2.2 PEACOCK AND WISEMAN'S HYPOTHESIS OF DISPLACEMENT EFFECT

Allan Peacock and Jack Wiseman studied the growth of public expenditure in the UK for the period 1890 – 1955. They came up with an alternative hypothesis of the growth of public expenditure different from what Wagner proposed. Peacock and Wiseman's hypothesis is popularly referred to as Displacement effect hypothesis. They believed that the pattern of growth of public expenditure in Britain is less regular than and quite different from the corresponding pattern of growth in the size of the rational output as proposed by Wagner.

The core argument is that public expenditure does not increase in a smooth and continues manner but in a stepwise fashion. This line of reasoning is depicted in the illustration given below.

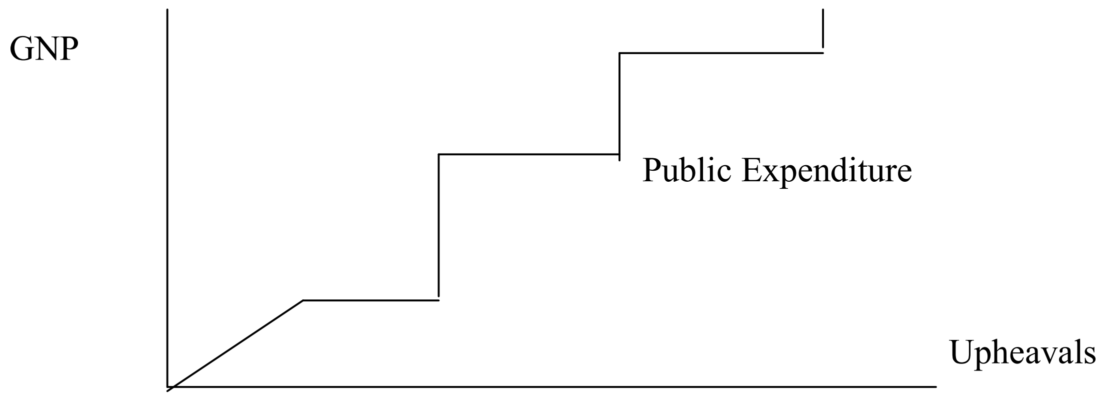

Fig 2.2 Displacement Effect Hypothesis

The chart of government expenditure normally exhibits peaks separated by plateaus. Peacock and Wiseman argued that countries experience upheavals of various types. During these upheavals there is need for increased public expenditure over and above the existing public revenue. This mounts a serious pressure on the government and the people to accept a higher level of sacrifice by withdrawing more resources from the private sector to the public sector. In doing so, public expenditure displaces private expenditure during the period of disturbance. Thus, there is a movement from a lower level of public expenditure and revenue to a higher level. And so government expenditure and revenue are displaced upwards. This is the main thrust and the essence of the displacement effect hypothesis. When the need for higher public expenditure is recognized and accepted, the government and the people will review the revenue position with a view to finding a solution. This usually involves an upward adjustment of the revenue to fiancé the increased expenditure.

It should be noted that public expenditure is usually financed by taxes. Over the years, people get used to a certain rate of tax and start to tolerate that rate. It is only in the face of crisis that the people will tolerate an increase in the tax rate. They now begin to tolerate the new higher rate imposed by the crisis. The new public expenditure and revenue get stabilized at that higher level. The constraint imposed by the tolerable level of taxation in government spending is removed by crisis that destroys established levels of taxation. As a result, tax rates and other methods of raising revenue hitherto unacceptable by the people, become acceptable during periods of crisis. This acceptance remains even after the crisis that gave rise to it is over. And so, although the government expenditure and tax rate may fall after the upheaval, it is unlikely to fall back to the pre – crisis level. The government can now do those things it has been wanting to do but could not do because of dearth of funds. In this way the public expenditure and revenue get stabilized at a new level till another disturbance, which may give rise to a displacement effect happens. The displacement effect hypothesis is based on the political theory of public expenditure determination, which says that:

- Government likes to spend more money
- Citizens do not like to pay more taxes
- Government needs to pay attention to the wishes of their citizens.

  Peacock and Wiseman showed that this divergence of the idea of citizens as to what is the desirable public expenditure from what is the reasonable burden of taxation offers a basis for explaining the growth in government expenditure over time.

  The government assumes a larger proportion of the total national (economic) activity in each disturbance. Also the central / federal government assumes a larger proportion of the total national economic activity than the other levels of government. This is refereed to as the concentration effect.

The hypothesis of peacock and Wiseman were developed from available data from the UK. The hypothesis is based on re – occurring abnormal situations that displace public expenditure and revenue upwards. In all fairness, it must also be noted that the public sector has an inherent tendency to increase in size on account of increase in activities both in quantity and quality and programmed systematic expansion.

2.2.3 THE CRITICAL LIMIT HYPOTHESIS

The main thrust of this hypothesis that when the share of the government sector exceeds a certain critical limit (percentage) of the whole economic activity in a country. Inflation triggers off even under balanced budgets. Colin Clark (1945) placed the limit at 25 percent. In his public finance and changes in the value of money" (Economic journal pp 871); he proposed the critical limit hypothesis regarding tax tolerance. Colin Clark contends that when the government's share of the aggregate economic activity reaches the critical limit of 25 percent, the income earners are affected by reduced incentives, which results in low productivity. This can be traced to the negative effect of high tax incidence on productivity. This leads to low output, which finally results to reduced supply: But the increased government activity increases demand significantly even if the budget is balanced. As a result of this excess demand, inflation begins to gather momentum. Critics have argued that the choice of 25 percent is arbitrary.

Bhatia (2000) thinks that it would have been more acceptable to assert that in a market economy, increasing state activity leads to mounting inflationary pressures. More so when some countries have exceeded the defined critical limit of 25 percent share of the government sector in total economic activity without significant inflationary pressure.

2.2.4 MUSGRAVES THEORY OF PUBLIC EXPENDITURE GROWTH

Musgrave (1989) thinks that the income elasticity of demand for public goods and services is the major determinant of public expenditure growth. He grouped consumers into three, based on per capita income as follows

(1) Those at low levels of per capita income typical of pre – industrial society in developing countries. At this level, demand for public goods and services tend to be generally low because nearly all income is devoted to satisfying primary needs. Public expenditure is therefore very low.

(2) As per capita income starts to rise above those low levels, the demand for public goods and services usually provided by the government, such as education, health, electricity, portable water, etc. begins to rise thereby compelling the government to provide more of them and so increasing expenditure on them. This explains the growth of public expenditure in the state at that level. This depicts the early stage of economic development.

(3) At very high levels of per capita income characteristic of developed economics, basic wants have been satisfied, and sometimes by the private sector. The rate of growth of the public sector then tends to fall.

Apart from increase in par capita income, other factors identified by musgrave as likely factors that could bring about increase in public expenditure growth are

(1) Technological change

(2) Population change

(3) Relative cost of public services and

(4) Urbanization

(5) Availability of tax handles

(6) Political and social factors

(7) Changing scope of transfers

These factors are briefly discussed below:

(1) Technical Change: Technological change in particular has a major bearing on the development of the expenditure share. As technology changes, so do the processes of production and the product mix, which it is efficient to produce. These changes in technology may be such that they increase or decrease the relative importance of goods whose benefits are largely external and which must therefore be provided by government.

(2) Population Change: Population change according to musgrave is another major determinant of the public expenditure share. Changes in the rate of population growth generate changes in age distribution and this trend is reflected in expenditures for the aged. An era of baby boom will result in higher school and college enrolment; thus placing a major burden on a nation, state or local finances. If the population trend continues, education needs will give way to demands for housing facilities; and as the population bulge moves up further in the age scale, the major fiscal problem fifty or sixty years hence may well be that of support for the aged.

(3) Relative Cost of Public Services: the more rapid rate of inflation in the price of inputs or goods purchased by the public sector resulted in an increase in expenditure – to – GNP ratio well ahead of that recorded by the deflated ratio. The nature of publicly provided goods and services may be such as to render these components of GNP less receptive to technological progress than is the case for private goods, thus raising their cost relatives to that of private goods.

(4) Urbanization: The process of urbanization and resulting congestion has increased the need for infrastructure and for public services. Needs arise which call for public provision and which are not present in a rural setting where economic units are more self-contained.

(5) Availability of Tax Handle: In any given economy, the ability to finance expenditure is a function of how much is in the state's coffers. In a typical low – income economy, it is much difficult to impose and collect taxes than in the advanced economy.

A feasible source of revenue collections is via import and exports. For low-income countries with high trade involvement.

These difficulties do not exist, or exist to a much smaller degree, in highly developed countries, where effective income, profit and sales taxation is feasible. The relative absence of adequate tax handles in low-income countries, to a large extent affect their expenditure pattern. Since there is not much money, the tendency is that public expenditure will be very low or minimal. For developed or robust economics the reverse is the case

(6) Political and Social Factors

Political and social changes are equally great determinants of expenditure growth. Over the past century, there have been vast changes in social philosophy as well as shifts in the balance of political power among the various sectors of a population. These have a deep effect not only on what individuals consider to be the desirable size of the public sector, but also on the force with which the views of various groups make themselves felt in the political decision process.

(7) **CHANGING SCOPE OF TRANSFERS**

Transfer programs such as welfare payments are distributional in nature. The need for redistribution depends on a prevailing state of distribution prior to adjustment. If income inequality decreases as per capita rises, less extensive redistribution measures are needed.

If the objective is to adjust family incomes so as to achieve a given relative income distribution, an increase in the average level of income leaves the need for redistribution unchanged. The situation differs if the objective is to set a tolerable minimum level determined in absolute terms; such as the cost of meeting minimum nutrition requirements. In this case, the need for redistribution falls as average income rises. But again, if the minimum level is defined as a function of average income, the need for redistribution once more remains unchanged as income rises.

All the factors discussed, suggest that there are good reasons for public expenditure to change over time. The desired mix of goods changes with rising income. More over there are exogenous factors such as technological and demographic changes, which have major bearing on what constitutes the proper level of government expenditure on public services. Though these factors do not add up to a clear presumption in favour of rising expenditure profile; there is a need, not to over look them while considering the expenditure profile of a state.

2.2.5 THE LEVIATHAN HYPOTHESIS

According to Aigbokhan (1997), the leviathan model is an explanation proposed by Brennan and Buchanan (1980), which considers government as a revenue – maximizing entity, whose ability and propensity to maximize tax – pricing revenue is only constrained by constitutional provision for decentralization of spending and taxing powers among sub – national government. The cardinal hypothesis postulated by Brennan and Buchanan (1980) is that the lesser the total government intrusion into the economy, ceteris paribus, the greater the extent to which taxes and expenditures are decentralized. As in Aigbokhan (1997), given the assumption that government expenditure is financed mainly from taxes and user charge, spending will be limited by the ability of the government to raise taxes. It may also be correct to say that the ability and willingness of tax – payer to pay will bear much on the expenditure behaviour of government. Another inference that can be made from the leviathan model is that "the more decentralized taxing and expenditure (spending) responsibilities are, the smaller the size of government would be." The Leviathan's hypothesis agrees with fiscal federalism theory that intergovernmental transfers, especially from top to down, influences public expenditure. The federal government transfers to state government is herein referred to as the strategic transfers (STC).

2.2.6 OTHER THEORIES

In a line of continua between the Wagner's law and the leviathan hypothesis are such other hypotheses; Differential productivity hypothesis offered by Baumol (1967), relative price hypothesis of Richard Bird (1980), developmental changes argument of Rastow (1971), etc.

Baumol (1967), for instance, explained the rise in government expenditure in terms of unbalanced growth between public and private sectors. Dividing the economy into progressive private sector and non – progressive public sector, he explained that productivity rises only in the private sector, where as wage rate rises in both, and as a result public expenditure would rise moreover, as public services are more labour intensive, and as employees in themselves have no motivation to improve productivity, the increase in public expenditure becomes acceleratory. On Rastows (1971) part, growth in public expenditure is better explained in terms of the changes in levels of development of the country's economy. For instance, less developed countries at their cradle of development require higher levels of investments in order to create necessary infrastructure for gainful economic break through. As such economies approach maturity of economic development, much of the further public expenditure would basically be prompted by repeated market failures. A fuller discussion of these theories can be found in Rosen, Agiobenebo (1998) and Onuchuku (2001).

2.2.7 COMMENTS ON THE THEORIES REVIEWED

A critical look at these theories would bring out some salient points of note. In the first instance it can be said that Wagner's theory sees government expenditure as one that increases at an arithmetic progression. On the other hand, Wiseman and peacocks hypothesis appears to subscribe to government expenditure to be increasing at a geometric progression (in Jerks and Step like Manner). One common point however, is that both are attempts to explain the growth of public expenditure over time. Secondly, from Wagner's view point, a list of factors that affect public expenditure would include: expansion in the nature and complexity of traditional governmental function, increase in the scope or coverage of state activities, the need to provide and expand the sphere of public good, increasing population, increasing flight of population to urban center, problems of cost – over – runs, higher cost providing public services occasioned by increase in size and nature public services, rising welfare and social security costs, budget deficits and debt – servicing requirements, targeted economic growth rates or levels, and development plan's targets.

To Wiseman and Peacock (1961), the major factor affecting public expenditure would include all major social and other disturbances in the economy. Contrary to Wagner's contention, Collins Clerk's critical – limit hypotheses see inflation as an effect of increasing public expenditure beyond the critical limit, rather than as a casual factor.

Musgrave (1989) believes that the income elasticity of demand for public goods and services is the major determinant of public expenditure growth.

These theories provide good foundation for empirical theories. There is a need, to investigate which of these factors that truly affect expenditure in a developing economy like Nigeria.

2.3 CANONS, EFFECTS AND GROWTH OF PUBLIC EXPENDITURE

Findlay and Dalton (   ) enunciated the basic canons or principles of public expenditure. These canons are discussed as follows:

2.3.1 THE CANON OF BENEFIT

The canon of Benefit is also known as the canon of maximum social advantage or benefit. According to this canon, public expenditure should be so incurred on various items that it provides maximum benefit to the society as a whole.

Nicholson (   ) says that the maximum social welfare is achieved when the public utility of marginal expenditure in each case is equal.

Shirras (   ) was of the opinion that no public expenditure should be incurred for the benefit of individual or society unless it satisfies three conditions. First, the amount expenditure should be small. Second, a claim for the amount should be enforced in a court of law third, the expenditure should be incurred in pursuance of a recognized policy or custom. This canon is fulfilled if these three conditions are satisfied.

2.3.2 THE CANON OF ECONOMY

By the canon of economy is meant that public expenditure should be incurred as to avoid the waste of public money. It should avoid all extravagance and useless expenditure. The word ‘economy’ can be interpreted both in the narrow and wide sense. In its narrow sense, it means that there is no extravagance in public expenditure. In it’s wide sense, it means that if a particular public expenditure is not incurred on a particular item or use, it will not lead to the maximum social welfare.

2.3.3 THE CANON OF SANCTION

This canon states that no public expenditure should be incurred without the sanction of proper authority. Any public officer cannot incur public expenditure because it will lead to misuse or malallocation of funds. There should be a competent authority to sanction all public expenditure which may allocate them according to the requirements of the country.

Shirras (   ) observes in this connection that no expenditure should be sanctioned by an authority which at a latter date is likely to involve expenditure beyond its power of sanction.

2.3.4 THE CANON OF ELASTICITY

By the canon of elasticity is meant that public expenditure should change according to the needs and requirements of the economy. It should be quite flexible so that it can be increased during depression and reduced during inflation. In other words, public expenditure should be sufficiently elastic.

2.3.5 THE CANON OF SURPLUS

The canon of surplus means that the public authority must earn it's living and pays its way like ordinary citizens. Balanced budget as in private expenditure should be the order of the day. The above definition by shirras points towards a balanced budget. The government revenue should be more than it's expenditure. But it again becomes a canon both of income and public expenditure. The state as an entity may not always behave like an individual. It has to spend sometimes more and at other times less than its revenue. This entirely depends on the prevailing economic conditions of the country.

2.3.6 THE CANON OF EQUITABLE DISTRIBUTION

According to this canon, public expenditure should be incurred in such a manner that it helps in reducing the inequalities of power, income and wealth. The pattern of public expenditure should such that the poor and weaker sections receive the maximum benefits in the form of free education, medical facility, old age pension, housing etc

2.3.7 CANON OF PRODUCTIVITY

This canon requires that public expenditure should help in increasing productivity. Such expenditure should increase such infrastructure facilities as roads, energy and power, communications etc.

2.3.8 THE CANON OF NEUTRALITY

The canon of neutrality implies that public expenditure should be incurred in such a manner that it neutralizes all adverse effects on production and distribution. Rather, it should have a healthy influence on both production and distribution in the country. It should encourage productivity and at the same time reduce inequalities of income and wealth. But it is not always possible that public expenditure should have neutral effects. At the most, the adverse effects of public expenditure can be minimized.

2.3.9 EFFECTS OF PUBLIC EXPENDITURE

According to Dalton (   ) public expenditure has far reaching effects on production, employment and distribution in a country. These effects are discussed below under the following sub headings:

- Effects of public expenditure on diversion of Resources
- Effects of public expenditure on Income Distribution
- Effects of public expenditure on Economic Stability
- Effects of public expenditure on Economic development

2.3.9.1 EFFECT OF PUBLIC EXPENDITURE ON PRODUCTION

According to Dalton ( ) production and employment in a country depend on three factors

(a) Ability of the people to work, save and invest

(b) Willingness to work, save and invest

(c) Diversion of economic resources as between different uses and localities

Public expenditure on social insurance benefits the: unemployed, sick, old in our mist and tends to increase the purchasing power of workers indirectly.

Public expenditure on basic facilities also tends to raise efficiency and ability to work. When the state provides basic facilities such as low – cost housing, mid – day meals to children, subsidized nutritional food suppliants, etc; the ability to save increases. This in turn raises the ability to work

Public expenditure on education, public health and economic overheads has direct welfare effects on the society. While expenditure on education and health are regarded as investment in human capital, expenditure on economic overhead tends to increase the supply of resources for production over a long period.

Public expenditure in the form of grants and subsidies to farmers, firms and industries is highly productive. When it comes in the form of credit and banking facilities; this also helps in increasing the productive capacity of the economy.

Public expenditure on provision of information via the electronic and print media helps private and public enterprises in getting their products publicized.

2.3.9.2 EFFECTS OF PUBLIC EXPENDITURE ON DIVERSION OF RESOURCES.

Public expenditure affects the pattern of production through the diversion of resources from existing uses to more productive uses. In fact, government expenditure in itself is a diversion of resources from private to public uses. Public expenditure induces people and governments to divert their resources to more productive ventures via the following means:

- Provision of basic infrastructures
- Diversion of resources from more developed places to less developed areas.
- Provision of loans and other credit facilities
- Diversion of resources towards the defense of nations sovereignty. Defense provides security to life and property and saves the nation from foreign invasion and domination. All expenditures on defense are not wasteful, but rather it is indirectly productive.

2.3.9.3 EFFECTS OF PUBLIC EXPENDITURE ON INCOME DISTRIBUTION

Public expenditure by increasing social welfare helps in reducing inequalities of income and wealth. According to Dalton, it is only progressive expenditure that tends to reduce inequality. It does this through income distribution. Again, there are two parts to income distribution. It could come through transfer or exhaustive expenditure.

2.3.9.4 EFFECTS OF PUBLIC EXPENDITURE ON ECONOMIC STABILITY

Increase in public expenditure tends to raise national income, employment, output and prices. An increase in public expenditure during deflation increases the aggregate demand for goods and services and leads to a large increase in income via the multiplier process. It has the effect of raising disposable income, thereby increasing consumption and investment expenditure of the people.

2.3.9.5 EFFECT OF PUBLIC EXPENDITURE ON ECONOMIC DEVELOPMENT

The effect of public expenditure on economic development lies in increasing the growth rate of the economy, providing more employment opportunities, raising incomes and standard of living, reducing inequalities of incomes and wealth, encouraging private initiative and enterprise and bringing about regional balance in the economy.

2.3.9.6 GROWTH OF PUBLIC EXPENDITURE

There has been a phenomenal increase in Nigerian public expenditure over the years. This can be attributed to several reasons; amongst which are:

(i) **ECONOMIC DEVELOPMENT AND DEMOCRATIC GOVERNANCE:** Modern governments are engaged in the development of their economies. This can only thrive in a democratic setting. Democracy as a form of government is quite expensive to run.

(ii) **EXPANSION OF STATE ACTIVITIES:** There is an intensive as well as extensive increase of State functions and activities. New duties are being continuously undertaken and old ones are being performed on a large scale.

(iii) **INTERNAL SECURITY:** Enforcement of law and order for maintaining peace and security has led to the expansion of legal and administrative systems and police. These have led to the increase in public expenditure.

(iv) **DEFENCE:** As Adam Smith said long ago "Defense is better than opulence". Every country has got to depend her sovereignty. Public expenditure, which is always on the increase, is very essential.

(v) **WELFARE ACTIVITIES:** Due to increase in welfare activities, public expenditure is on the increase too!

(vi) **POPULATION INCREASE AND URBANISATION:** With the over increasing growth in population; there is migration of population from rural to urban areas in search of employment. It requires huge public expenditure to provide the necessary amenities for the teaming population.

(vii) **PRICE RISE:** The rise in the cost of living has further increased government expenditure.

(viii) **PUBLIC DEBT:** States borrow to meet its rising obligation. This further raises public expenditure in the form of repayment of loans and interest charges.

The above reasons for increase in public expenditure over the years have been articulated and enunciated as testable theories of public sector growth. This is presented below.

2.4 NIGERIA'S PUBLIC EXPENDITURES: PROFILE & POLICIES

2.4.1 CONCEPTUAL ISSUES:

Public expenditure can simply be seen as the absorption of resources by the public sector. Here, the public sector, broadly defined is that portion of the national economy in which economic and non – economic activities are under the control and general direction of state (Federal, State and Local Government). In the Nigerian context, as an example, the public sector consists of the federal government, state governments and the Local government (Anyanwu 2002:94).

Thus, public expenditure involves all the expense, which the public sector incurs for her maintenance, for the benefit of the economy, external bodies and for other countries.

On the other hand, public expenditure programming is a comprehensive set of expenditure policy measure designed to achieve a given set of macroeconomic goals including the restoration of equilibrium between aggregate domestic demand and supply (Imf institute, 1993)

Public expenditure program while stressing the end product is designed to consider the pursuit of policy objectives of government in light of all economic cost of the programmes. Public expenditure program stresses the relationship between various outputs or programmes and the inputs necessary to produce them. This approach seeks to be all – inclusive, recognizing all contributions that the activity makes and all costs incurred, regardless of organizational structure (Due, 1968).

2.4.2 EXPENDITURE STRUCTURE AND CATEGORIZATION

Expenditure structure addresses the question of how the expenditure is or should be composed. Such an expenditure structure facilitates the accounting aspects of fiscal management, while lending itself to central control over decentralized expenditure. Such public expenditure refers to the absorption of resources involving all expenses which the public sector incurs for it's maintenance, for the benefit of the economy, external bodies and other countries (Anyanwu, 1994).

Public expenditure is usually categorized into recurrent and capital expenditure. These are further broken down into their compositions. For example, recurrent expenditure is composed of administration (general administration, defense, internal security); social and community services (education, health and others); and transfers (pubic debt charges or interests for both internal and external debts, pensions and gratuities, and others such as transfer to contingency fund, net depreciation on the revaluation of investments and extra budgetary expenditures.

Most governments and public sector organizations attempt to make a clear distinction between items of recurrent nature and items of a capital nature. In spite of this, there is no single definition of capital expenditure that is acceptable in every circumstance. In general the approval that is adopted is to isolate capital expenditure from recurrent expenditure that concerns the period of benefit. The benefits flowing from recurrent expenditure tend to be limited to the year in which the expenditure is incurred where as the benefits that result from capital expenditure extend beyond the year of payment

The recurrent expenditure serves the following purpose:

- Determining income and expenditure
- Assist in Policy making and planning
- Authorizing future expenditure providing the basis for controlling income and expenditure
- Setting a standard for evaluating performances
- Motivating managers and employees.
- Coordinating the activities of multipurpose organizations and developments.

On the other hand, a capital expenditure is a plan for acquiring and maintaining long-term assets. It is also a means of financing these activities. Typically, the capital expenditure includes one or more of the following:

(a) New facilities and major additions

(b) Major renovation and repairs to existing facilities.

2.4.3 ROLE OF PUBLIC EXPENDITURE

Public expenditure is used for allocation, stabilization and distribution. It also shapes the course of development, affects adjustment and growth by influencing the rates of consumption, saving and investment in both physical and human capital.

Public expenditure could rightly be:

- The type of public expenditure coverage
- Size or coverage of public sector and it's composition and
- The relevant time horizon.

2.5 SOURCES OF GOVERNMENTS REVENUE

Bhatia (2000: 35) likened a government in power to any economic unit, which needs funds to finance its activities. Invariably, there are various sources of funding governmental activities.

These sources may include:

(1) Taxation

(2) Government borrowing and deficit financing

(3) Money creation

(4) Public debt

(5) Export proceeds

(6) Dedicated Accounts

(7) Grants

(8) Service charges for governmental goods and services.

These sources of funds to government are discussed below.

2.5.1 TAXATION

A tax is a compulsory levy payable by an economic unit to the government without any corresponding entitlement to receive a definite and direct quid proquo from the government (Bhatia 2000: 37).

Tax can be seen as the price individuals pay for the public goods and services provided by the state and enjoyed by individuals. In other words, it is the market price of government goods and services. Thus, people pay taxes for funding governmental goods and services. If the payment for these goods and services is left for voluntary donation, people will not pay for them. They may even conceal their preference for these goods.

Taxation has proved to be a major source of government revenue. The cost of providing goods and services to the public is a major determinant of the tax pattern of any government. Since taxation plays such a major role in financing government's expenditure, there is then the need to take more than a cursory look at this subject matter.

2.5.1.1 PRINCIPLES OF TAXATION

For a tax system to achieve certain objectives, it must choose and adhere to certain principles, which are termed as its characteristics. Adam Smith is best remembered for what has been known as his cannons of taxation. He identified the following canons or principles of taxation.

(i) **Canon of Equality:** He proposed that the amount payable by taxpayers should be equal, by which he meat proportional to income. He intended that tax burden must be felt equally. The rich and the poor are expected to make equal sacrifice in taxation.

(ii) **Canon of Certainty:** The rate of tax and how to calculate it should be certain. Hence, both the taxpayer and officials should be able to work out the tax due with certainty. The taxpayer should know for certain how much they should pay.

(iii) **Canon of Convenience**: There should be convenience of payment. The timing and method of paying taxes should be convenient to payers.

(iv) **Canon of Economy** The tax must be cheap to collect. The cost of collecting the tax must be small relative to the tax revenue. Taxes should not be imposed if their cost of collection is excessive.

Theses canons of taxation have a sound philosophy behind then and exhibit an insight into the practical aspect of tax administration and it's effect.

In view of developments in economic philosophy and problems of modern state, later writers like Bhatia (2000) have come up with a few additional principles. These includes:

(v) **Canon of Productivity:** According to this principle, the tax administration / system should be able to yield enough revenue for the treasury and the government should not need to resort to deficit financing

(vi) **Canon of Buoyancy:** The tax revenue should have an inherent tendency to increase along with an increase in national income, even if the rates and coverage of taxes are not revised.

(vii) **Canon of Flexibility:** It should be possible for the authorities without undue delay, to its coverage and rates, to suit the changing requirements of the economy and of the treasury. (Bhatia : 2000)

(viii) **Canon of Simplicity:** The tax system should not be complicated. It should be easy to understand, administer and interpret.

(ix) **Canon of Diversity:** Tax revenue should come from diversified sources. It is risky for a state to depend upon too few a source of public revenue. This could breed a state of uncertainty for the treasury

2.5.1.2 THE BASE OF A TAX

The base of a tax is the legal description of it's object, with reference to which the tax is payable. For example the base of an excise duty is production, packaging or processing of a specific good; the base of an income – tax is the income of the assesee. A tax base may have a time dimension e.g. income tax is usually on an annual basis.

A tax base may increase or decrease for example, as production of excise goods increase, the base of the excise duties also grow (Bhatia: 2000)

2.5.1.3 TAX STRUCTURE

This refers to the composition of the tax system. Taxes could be classified into

(1) Direct and Indirect tax system and

(2) From the point of view of a relationship between tax rate and the tax base.

2.5.1.4 DIRECT TAXATION

Direct taxes are levied on income of people (both private and corporate individuals) or on wealth as distinct from taxes levied on goods and services.

The person or company on whom a direct tax is imposed bears the burden of the tax. It may not be possible to shift it to other person. Direct taxes are more closely associated with ability to pay and to that extent are generally regarded as being more equitable than indirect taxes.

Examples of direct taxes includes:

Poll tax, personal income tax, company tax, petroleum profit tax, capital gains tax and surtax. These are briefly discussed below:

(i) **Poll Tax:** Poll tax is a tax of certain amount per head of the population. Lumpsum poll tax is usually imposed on people whose income is not more than a certain minimum. It is usually not graduated.

A direct poll tax comes with some measure of graduation. The purpose is to tax people a little more as their income increases.

(ii) Personal Income Tax: This is a tax on all types of personal income, which may include rent, interest, wages and salaries and profit for a defined period. It is usually levied on people with defined income up to a certain specified maximum amount. Taxpayers are granted tax fee allowances according to their peculiar circumstances. Income tax management act (ITMA) of 1961, modified in 1975 and represented in personal income decree no 104 of 1993 clearly defines the rules and regulations guarding personal income tax.

(iii) **Company Tax:** Companies are legal persons in the eye of the law. And so, they pay tax like other citizens. Usually, company tax was based on profit. In which case company pay a certain percentage of their profit as tax. Today companies are obliged to pay a certain amount even if they do not make profit.

(iv) **Petroleum Profit Tax:** This tax is based on the petroleum profit tax act of Nigeria (1959). The tax is on companies dealing on mineral oil and natural gas in Nigeria. This has turned out to be a major source of government revenue in Nigeria.

(v) **Capital gains Tax:** This is a tax imposed on the increase in value of a capital asset over time (i.e. between the time the asset was bought and when it is sold).

The basic advantages of direct tax includes:

(1) Direct taxes are equitable and it constitutes a major source of government revenue.

(2) Little cost are incurred in collecting direct taxes and it makes citizens responsible and alive to their civic responsibilities.

(3) Taxes are fiscal policy instruments for controlling the economy.

The disadvantage of indirect tax is that it acts as a disincentive to work and savings as it reduces company profit.

Again, direct taxation may mean that only people in the organized sector pay tax; while people in distributive trade will evade taxes.

2.5.1.5 INDIRECT TAXES

These are taxes on goods and services. They are different from taxes on income and property, which are direct taxes. Indirect taxes could be specific or advalorem i.e. according to value of the commodity. Example of indirect taxes includes: Custom duties, import duties, Excise duties, sales tax, value added tax, export duties etc.

(i) **Custom Duties:** This is tax imposed on imported goods. Originally, they were imposed to cover expenditure on docks and harbours and the cost of defending shipping against pirates, but today, custom duty is a major source of government revenue.

(ii) **Export Duties:** This is the tax placed on goods that are exported. The government is not so stringent on collecting export duties in the new dispensation. The essence is to encourage exporting of goods in order to earn foreign exchange.

(iii) **Excise Duty:** This is tax on home produced good for home consumption. Excise duty is usually imposed either to raise revenue or to check the consumption of the commodities on which they are imposed.

(iv) **Value – added Tax:** This is a tax levied on the value added at each of the processes carried out by a business. Vat is a tax on net value added by each firm.

The advantages of indirect taxes include:

(1) It is administratively easy to collect and the amount is so small that buyers can ignore the fact that they are being taxed.

(2) People cannot evade paying indirect tax and it is a sure source of increased government revenue.

(3) They are used to discourage the production and consumption of harmful goods.

Limitations of Indirect Taxes:

(1) It is regressive and may be discriminatory

(2) It possesses on inherent inability to reach concentration of income and wealth, just like the direct tax.

2.5.1.6 TAX STRUCTURE (LL)

Taxes may also be classified in terms of relating the tax base to the tax rate. In this way, 3 forms of taxation are recognized as follows:

Progressive

Regressive and

Proportional tax system.

A tax is progressive if the tax rate increases as the tax base increases. A tax system is regressive if the tax rate increases as the tax base decreases. In other words, there is an inverse relationship between the tax rate and the tax base.

A proportional tax system is one in which the tax varies in proportion to income.

2.5.1.7 CHARACTERISTICS OF A GOOD TAX SYSTEM

According to Bhatia (2000: 43), the characteristics or feature of a good tax system could be formulated from various objectives, principles or canons of a tax system.

Formulation of characteristics of a good system by considering its effect does not imply that the non – tax items or the public expenditure can be ignored. Any choice is bound to harbour several conflicts and contradictions, necessitating an adjustment. It is implicitly assumed that taxation forms a major portion of the public revenue and that the expenditure side of the budget is being administered in an optimum manner, or at least it is not working against the objectives of the tax system.

Secondly, a tax system has many dimensions. We could look at it form the point of volume composition, rates, coverage, timings of collection, mode of collection and so on in order to grasp its effects in their totality. It is rather difficult to evolve a tax system, which is the best or ideal in every respect.

Thirdly, in theory many tax proposals may appear very convincing, but it may not be possible to implement them. It is assumed that a government has an absolute right over the property of all its subjects, but in practice, it is not a right, which can be exercised fully and without limit. Some taxes, though theoretically sound, may involve a heavy cost of collection.

Fourthly, the attitude of the tax – payers is an important variable in determining the contents of a good tax system. Normally each taxpayer desires to be free from a tax burden but does not mind if the tax burden is borne by others. If this is a not so, he feel discriminated against. It is essential that a good tax system should appear equitable to the tax- payers.

Fifthly, it is a well – known fact that changes in a tax system can be brought about only slowly and in stages. Even if it is decided to have an entirely new tax system, the authorities cannot suddenly disrupt the existing one. They have to gear their tax machinery to the new system. A good tax system recognizes that the taxpayer has some basic rights. He is expected to pay his taxes but not to under go harassment. With this end in view, tax laws should be simple in language and the tax liability should be determinable with certainty. The mode and timings of payment should suit the convenience of the taxpayer to the extent possible. At the same time, a tax system should be equitable as between different taxpayers. It should be progressive so as to levy an equitable burden on all.

Lastly, in the process of economic growth, a developing country is likely to face the problem of inflation. A good tax system should help in counteracting the inflationary forces. It should be designed to discourage unnecessary consumption and boost up production along desired lines.

2.6 EXPORT PROCEEDS

According to Anyanwu (2000: 59) a structural analysis of Nigeria's export shows that between 1960 and 1970, non – oil exports comprising mainly agricultural product dominated total exports, accounting, on the average for over 80% of total exports.

However, from 1970 onwards, crude oil exports started to exceed 50% of total exports, receiving a major boost during the oil crisis of 1973 – 74. Oil exports in 1980. This resulting dramatic increase in oil earnings made Nigeria to delude itself by confusing wealth with income, hence the euphoria and the oil wealth syndrome (Anyanwu 1990).

The rapid monetization of her oil earnings led to a spending spree, leading to high import consumption, huge budget deficits, excess money supply and external debt overhang. Nigeria found herself in a situation where high but temporary oil revenue has adversely affected the non – oil traded goods sector, thus delaying the learning by doing experience that would improve its comparative advantage in the production of manufactured goods. It is a phenomenon of de – industrialization and de – agriculturization characterized by relative shrinkage of domestic manufacturing industries and local agricultural production and a relative expansion of service industries. Thus, Nigeria is facing serious problem in building up a diversified export base since a large chunk of the oil revenue is spent on non – traded goods.

2.7 DEDICATED ACOUNTS

Some accounts are specifically dedicated to the federal government of Nigeria. Such account heads are targeted towards specific programs as enunciated by the federal government. Revenues accruing to such accounts go straight into the coffers of the federal government. In recent times, such funds have accounted for a quantum leap in the source of funding the expense profile of the federal government.

The dedicated accounts include:

(i) The petroleum Trust fund (1994 – 1999)

(ii) The Education Tax fund

(iii) The AFEM Surplus Account

(iv) NNCP joint ventures payment account

(v) The external service fund

(vi) The national Priority Project Funds.

These account heads are briefly discussed below

2.7.1 THE PETROLEUM TRUST FUND

This fund was created late in 1994 as an institutional attempt to douse public opposition to the sharp increase in the prices of petroleum product e.g. from N3 to N11 in the case of petrol. The additional revenue from these increases accrued principally to the PTF and was "invested in social and infrastructural projects for the benefit of the Nigerian people". Given the political and social crises, which Nigeria was experiencing when it was created, the PTF was a laudable exercise in political and social engineering. The concrete performances of the fund was commended by its beneficiaries. This was not a popular view as most people from the southern Nigeria complained of the lopsided nature of the projects undertaken by the PTF. The fund which was headed by a former Head of State; Gen. Muhammadu Buhari, was accused of concentrating the developmental efforts in the North at the expense / chagrin of the south; especially the south – south geographical spread where petroleum products are being extracted from (Anyanwu:).

All these not withstanding; it is pertinent to mention here that the PTF was a budgetary aberration and a violation of the constitutionally specified revenue allocation system. In budgetary terms, the PTF was in effect a scheme of earmarked revenue. Proper budgeting is against earmarking because it curtails scrutiny, and transparency. In addition, the PTF implied the creation of a parallel authority on capital expenditure matters alongside the regular authorities.

In revenue allocation terms, the money in the fund ought to go into the federation account first. Consequently; one can equivocally say that the PTF short changed the three tiers of government of their due share of the federation account (Anyanwu : 2000)

The PTF was an instrument for perpetrating long standing inequalities in the distribution of Nigerian resources. Clearly, only a military administration could have got away with a creation such as the PTF. Perhaps, this could help explain why the Obasanjo led civilian administration in 1999, scrapped the petroleum trust fund.

2.7.2 AUTONOMOUS FOREIGN EXCHANGE MARKET.

As part of the deregulation of the foreign exchange market, the federal government established the autonomous foreign exchange market (AFEM) at which all the banks are active participants.

The central Bank of Nigeria intervened regularly at the market on short notice with a view of achieving desired policy objectives

The Afem operates exchange rates, which are mutually agreed between buyers and sellers of foreign currencies. Forward foreign exchange contracts are allowed subject to some guidelines. Open positions for individual banks for both prudential and operational reasons are determined by the central bank. The Afem regulations require no initial advance deposits for the Naira counterpart of the foreign exchange demanded by banks, but the accounts of the banks are debited with the Naira value of sales before forex is released to their correspondent banks.

Surplus amount reserved for this exchange rate pricing mechanism eventually turned out to be a major source of funding for federal government expenditure profile. The surplus amounts recorded could be attributable to the gradual but eventual sliding of our Naira against internationally acclaimed currencies.

2.7.3 EDUCATION TAX FUND

The education tax decree was enacted in 1993, and was amended by decree No. 40 of 1998.

This tax is at a rate of 2 percent charge on the assessable profit of a company registered in Nigeria. The assessable profit of a company is ascertained in a manner specified in the companies' income tax act or the petroleum profit tax act.

The education tax is payable within 60 days after the board has been served notice of the assessment on a company.

The funds so realized from this tax are paid into the coffers of the federal government. Proceeds from education tax are channeled into our educational system.

Our education sector overtime had experiences a decline / near neglect in the maintenance and erection of new physical structure. This fund has enabled the federal government refurbish most of the ram shackled structures in our citadels of learning, starting from the primary to tertiary levels of education.

2.7.4 NNPC JOINT VENTURE PAYMENT ACCOUNT

The oil sector is a veritable source of finance to the federal government.
The Nigerian National Petroluem Company (NNPC) actively represents her in this sector. Most of the oil exploration and exploitation activities involve a lot of money

In most cases a counter part funding arrangement is put in place between the NNPC and other operators. Thus, the government has to make provision for the joint venture payments. In the same vein, proceeds / accruals from such investment has really helped to oil the pace of development in the Nigerian economy.

2.7.5 EXTERNAL SEVICES FUNDS

As the name suggests, this fund is specifically set aside for the servicing of Nigerian's external debt burden. The activities of the External / foreign affairs ministry is an exclusive preserve of the federal government. Thus, this account is an exclusive preserve of the federal government. The amount earmarked for this service is always set aside, prior to making allocations to the three tiers of government.

2.7.6 NATIONAL PRIORITY PROJECT FUNDS

The federal government sets this fund aside; the essence is targeted towards issues of national interest or priority. Such projects could come in the form of provision of portable waters, eradication of Guinea worm, fighting of endemic disease such as the Acquired Immune deficiency syndrome (Aids), etc.

Undermining the seeming advantages of setting up these dedicated accounts, the truth remains that they are schemes for earmarked revenue. They violate / negate the revenue allocation formula between the 3 tiers of government.

2.7.7 SPECIAL ACCOUNTS / FIRST CHARGES.

Prior to 1995, the FGN had been earmarking a portion of the revenue for various special projects. This was achieved through the creation of off – shore "dedicated oil accounts. The funds in these accounts are controlled by the FGN but are neither meant to fund cash call obligations nor are they deposited into the federation account. These funds and the associated expenditures have not been recorded in the budget or the final accounts as shown by the Auditor General of the federation. The use of these accounts continued unabated even when it was announced in the 1994 budget speech that they would be closed. Although the federal government has not published much data regarding the use of the oil dedicated accounts. It is known that there were, and many still be, at least six of such accounts. These includes:

- NNPC projects
- The LNG export project
- A loan recovery fund
- Development of solid minerals funds
- Fund for establishment of strategic reserve for crude oil
- A special projects fund

While the first four funds were retained by NNPC, the ministry of petroleum and mineral resources controlled the fifth, while the sixth was controlled by the presidency and managed by the central Bank of Nigeria.

Not much is publicly known about the details of the special projects, but there is evidence that these ranged from large projects such as construction in Abuja, an aluminum smelting plant, power and steel to smaller projects such as roads, dams and even miscellaneous expenses for public officials.

In 1995, it was announced that the dedicated account would be closed and replace by dollar – denominated first charger on federally collected revenues the first charges, including a claim for external debt service, were published as part of the 1995 budget speech but few details were provided about the individual programs and projects to be so funded. Thus, there has been only limited progress in transparency while the policy of ear – marking revenues for special projects, prior to revenue sharing has been preserved.

Aside from the dedicated accounts, other miscellaneous activities and varied diversion of funds prior to revenue sharing is still very much in place. These transactions are carried out with a high level of secrecy. The NNPC cannot claim to be ignorant of these activities.

2.7.8 **DEFICIT FINANCING**

There are various forms of deficit financing; these include borrowing from abroad, which may result in debt overhang that Nigeria currently faces. Domestic borrowing as well as money creation may finance another part.

Dinh and Giugale (1991) examined the budget deficit financing by printing money and financial repression in Egypt and opined that, if the budget deficit cannot be adjusted fast enough, pressure on domestic process will build up quickly. Also, if the budget deficit cannot be adjusted fast enough to reduce the need for the inflation tax, the inflation rate will accelerate rapidly. The study connoted that the budget deficit must be at one way or the other because so long as it remains huge and cannot be financed by any other means, the inflation tax is still necessary.

Despite the complexity of the relationship between deficits and inflation, most economists would agree that larger money financed of budget deficits would lead to higher rates of inflation. In addition, the stylized facts show that hyperinflation occurred in countries where budget deficits were significantly larger. According to Yeager (1981) and sergeant (1982), on hyperinflation episodes in the central European countries during the 1920's, substantial reduction in the budget deficit, monetary reform and a fixed exchange rate were crucial for the successful stabilization policies in those countries. Fiscal restraint, which in most cases meant outright elimination of the fiscal deficit, was probably the most important of these policy measures. According to kiguel (1986), the positive links between deficits and inflation varnishes under perfect foresight, large money financed budget deficits could only lead to hyperinflation. These deficits can never the source of hyperinflation.

In particular, it was argued that in models in which the money market continuously clears, there is an inflationary finance of the deficit and agents have rational expectations, that budget deficits cannot be the source of hyperinflation

(Bruno and Fischer, 1985). This result appears to be particularly disturbing since the available evidence suggests that budget deficits have had a major effect on the beginning and ending of hyperinflationary processes. On the other hand, it was argued that significant reductions in the deficits (which in some cases might require a balance budget) would always eventually succeed in reducing the rate of inflation. More over, in the presence of fiscal lags, a reduction in the rate of inflation could by itself contribute to a reduction in the deficit and act as an additional stabilizing element (Kiguel, 1986).
Lal (1984), opined that a major reason for a big build up of debt by many third world countries (including Nigeria) was the need to finance rising public expenditure and the associated incipient fiscal deficits. The debt crisis arose because the rise in interest rates and hence the cost of public debt service exposed the underlying fiscal weaknesses which the earlier build up of debt by many third world borrowers had masked.

As the rise in interest rates was in part the result of the actual and expected structural fiscal deficits in industrial countries, the current and continuing debt crisis can thus be seen as flowing essentially from a global fiscal crisis, that is a crisis of the public sectors in both developed and developing countries.
Wijmbergen (1984) used a model to demonstrate the effects of deficit spending in different employment regimes. He found that the reason for employment, if any exists is a crucial determination of the effects of fiscal policy. Further, lack of effective demand is causing unemployment; deficit spending is shown to lead to more output and employment. Perhaps, this may explain why Nigeria as a nation is indulging in an ever-increasing deficit financing in her fiscal policy decisions.

Government borrowing essentially involves transferring purchasing power to government from individuals and organizations or other governments voluntarily on the condition that it will be repaid at an agreed future date. It could be internal or external, as has been highlighted before now. The effect of borrowing will depend on the level of employment of other resources in the economy and also on what the nation / individual could have used the money for. The effect also will depend on whether the loan is external or internal.

Government borrowing as a source of revenue has eaten deep into the act of governance in most of the developing economies. Borrowing from international bodies like he international monetary fund (IMF) with the attendant repayment schedule has brought with it excessive debt burden on the developing countries of the world.

2.8 PUBLIC DEBT

The act of borrowing creates Debt.

Debt therefore refers to the resources of money in use in an organization, which is not contributed by its owners and does not in any other way belong to them. (Oyejide, et al 1985:9)

Debt is a liability represented by a financial instrument or other formal equivalent.

When a government borrows, the debt is a public debt. The government through borrowing in the domestic and international markets respectively incurs internal and external debts.

Public debt is seen as all claims against the government held by the private sector of the economy, or by foreigners, whether interest – bearing or not (and including bank held debt and government currency, if any); less any claims held by the government against the private sector and foreigners (Anyanwu 1993).

It is the obligation of a public debtor including the national government, a political subdivision and autonomous public bodies (Klein; 1994).

Public debt can be internal or external; gross or net, marketable or non – marketable, short term, medium – term or long term; interest bearing or non-interest bearing; and / or project or jumbo loans (Anyanwu 1993).

2.8.1 IS THERE A NEED FOR PUBLIC DEBT?

The classical principles of loan finance rationalizes loans to provide intergeneration equity, pay – as – you – use, capital formation, old age insurance, self liquidating projects, adjusting distribution and reduction of tax friction.

Borrowing may be considered as a second best alternative to money creation during periods of unemployment. In this way, it is seen as an instrument of managing the economy.

Foreign loans, in particular, are seen as a means of filling domestic savings gap especially in the face of dwindling government revenues from domestic sources. It is particularly so in the face fluctuation in the prices of primary commodity exports and hence dwindling foreign exchange earnings.

External borrowing is also seen as enabling a developing country increase its rate of real investment just as it is seen as an engine of growth. In this sense, it increases per capita GNP or its component measures. Thus, debt acts as a source of capital formation.

Public internal borrowing acts as an anti – inflationary measure by mobilizing surplus money in people's hand.

Foreign Loans help to supplement domestic resources, by supplementing domestic resources, external loans, if used productively helps to accelerate the pace of economic development.

It is pertinent to mention here, that the bulk of Nigeria's public external debt consists of high cost medium term international capital market loans at floating interest rates with fixed margins above. Indebtedness to the Paris and London clubs dominate Nigeria's external loans.

2.8.2 JUSTIFICATION FOR THE USE OF EXTERNAL BORROWING IN THE FINANCING OF GOVERNMENT PROJECTS BY DEVELOPING COUNTRIES

There has been sustained debate on the justification for external borrowing for developing countries, especially in view of negative effects of debts on their economies and the experience of virtually all debtor countries of the third world. Eaton and Gersovits (1981) sought to justify debt in their study. They articulated four primary motives for external borrowing as:

(i) To smoothen consumption

(ii) To invest (if domestic marginal product of capital exceed the world's cost of funds.

(iii) To facilitate transaction and

(iv) To ease the transition to a new economic environment

Aikhomu (1988) complied further some reasons for resorting to external borrowing. According to him, external loans are required.

(v) To supplement domestic savings which make possible a higher rate of capital formation. As a corollary, we can borrow externally to execute viable projects;

(vi) To build up a country's external reserve position and hence strengthen the liquidity position of the country

(vii) To absorb major external shocks (In external resource of flows) in order to avoid wasteful deflation and stagnation and

(viii) To serve as financial intermediation in countries with weak financial markets.

The two points of view above shows that on its own, debt is very beneficial and advantageous for the process of economic development in less developed countries (LDC) that mostly have weak financial markets and low level of capital formation. The non-application of these loans to regenerative ventures and the interplay of other negative macro – economic aggregates have tended to make the issue of debt unviable and unattractive. Nigeria, for instance, experienced severe shocks between 1983 and 1996 as a result of its debt problem. This however, does not vitiate the need for external financing for the growth process. The basic problem is how to ensure that the debt burden correlates with the resources base of a country to enhance development. There is also the issue of ensuring that debt over hang does not affect economic growth negatively, especially on the long run.

2.8.3 CAUSES OF THE DEBT PROBLEM

(1) **Proximate Cause**

It is note worthy that external borrowing in Nigeria dates to 1958 when the sum of $28 million was contracted by the federal government for the Nigerian Railway construction project (CBN Research Series 1993).

Between 1958 and 1977, the country did not resort to much external borrowing even in the face of the needs and imperatives of development planning and financing, which was the case immediately after independence in 1960 and the civil war of 1967 – 1970. The first major external borrowing took place in 1978 when the federal government contracted a "Jumbo" Loan package of 12 billion (Abubakar 1990). This loan package was an attempt to meet shortfalls in the resource gap of the country. Prior to this borrowing, the revenue from oil export provided enough resources for the development process. With oil boom, there was a total neglect of other sectors of the economy, especially agriculture. The decline of agricultural production resulted in reverse in the non – oil export trade and food production necessitating the massive importation of good to meet the short falls. Also increasingly, there were shortages of raw materials for the productive process. These variables had negative impacts on the balance of payments.

However the effects of the above were not evident until the petroleum sector experienced reverses in 1980 / 1981. This

Situation reflected in a general decline in real GDP between 1981 and 1984. The real GDP declined from 5.1 percent in 1980 to 2.0 percent in 1981, - 31.7 percent in 1981-1983 and – 6.7 in 1984. The decline in oil receipts led to payment arrears and problems in obtaining new lines of credit.

(2) **REMOTE CASUES**

The remote causes of the debt overhang are essentially structural in nature, arising from the peripheral nature of the Nigerian economy in the world's economic relations. Essentially, the disarticulations of production and consumption profiles in Nigeria were singular factors, which had a profound effect on the debt crises. This is a product of the contradictions in the development planning process. According to Olukoshi (1988) the contradictions arises from the fact that the country stands as a peripheral appendage in the international capitalist economy, to supply natural economic resources to western countries and to serve as a market for the advanced countries surplus manufactures. The above scenario could be said to be a situation where Nigeria produces what it does not consume and consume what it does produce. The pattern of production over the years centered on import substitution and assembly of processes imported from abroad. This orientation led to conspicuous consumption amongst the citizenry, especially the elite group and resulted in massive importation of all sorts of luxury and irrelevant goods. Thus a high level of dumping was noticeable in the Nigerian economy. Conversely, the prices of the countries export products, which are essentially primary products, are regulated by the western countries. As a result, the resource inflows are also regulated and depended on these western powers.

Adedeji (1989) contends that the continued fragmentation of the African product and factor markets have exacerbated the lopsided nature of development, openness and external dependence of Africa and deepened it's economic crisis. This affects foreign resource inflows necessary for the development process.

The issue of over dependence on western economies is another factor that affected the debt crisis. The Nigerian economy has since independence been highly dependent on the economies of developed countries for productive capital, financial resources, technical and expatriate skills, food and even the export market for its products.

According to Nwoke (1988) the cyclical crisis of the advanced countries are consistently and systematically transmitted to the country as the derivative crisis of global capitalist reproduction while the country is persistently denied autonomous development dynamism, as it becomes a buffer for resolving the crisis of the advanced economies of western Europe. A classical example of the nature of dependence of Nigeria to external economies was the devaluation of the US dollar about the same period. This was because the Naira exchange rate was pegged to the dollar and the depreciations suffered by the dollar were translated to the Nigerian economy. This scenario consistently promoted balance of payment disequilibria and eventually the debt overhang problem.

Also the escalation of interest rates in western countries affected the debt stock since this creates debt – servicing problems. As interests rate rise in these countries, the debt stock also increases proportionately.
Capital flight has been recognized as a major source of the debt crisis. This is because of the destabilizing effects on the balance of payments.

Essentially, we can say that the pattern of capital accumulation in Nigeria has not sustained the demands of economic development. According to Nwoke (1990), the international credit system is controlled exclusively by the western countries, while Nigeria hangs on the periphery of the world's monetary relations. This affects the debt crisis negatively. Long term funds needed for economic development are politicized, while the conditions for obtaining it are very stringent for third world countries. According to Nwoke, since Nigeria could not have access to investment capital, nor could it create sufficient internal funds for its needs, the country became a pawn in the politics of international finance, which further aggravated the development process and debit crisis. Generally, adequate capital resources are essential for an emerging economy to sustain its development potentials and acquire level of technology for the growth process.

To a large extent, the terms on which developing countries obtained foreign capital and technology reflect the peculiar relationships between the developed and developing countries. This relationship has worked against the developing countries, largely due to the structure of their economies. Nigeria is no exception in this regard. One key variable that has sustained the imbalance in economic relations and the uneven flow of capital resources is the imbalance in trade relationships between the developing and developed countries.

The need for foreign capital in the development process is more pronounced in Nigeria due to low domestic capital formation. Various factors are responsible for this. First is the low level of savings arising from low-income levels? Secondly, the presence of weak financial markets and financial intermediaries also militate against resource mobilization. Thirdly, the fact of political instability and unstable macro – economic policies, which increase the risk of holding domestic financial assets necessary for capital formation, thus encouraging capital flight. Also, the distress syndrome which financial intermediaries were faced with in the immediate past in Nigeria also affected the level of public confidence and thus the level of resource mobilization. This affects capital formation negatively. This is in addition to the limited instruments necessary for resource mobilization and the inefficient regulatory framework.

The factors above, coupled with the need for capital – intensive technology; led to the over – increasing demand for foreign capital resources which has been receding especially since the beginning of the debt crisis in 1982. One important issue that has affected the debt burden is the issue of the over valued exchange rates. This sustained resource outflows, another point of view contends that other aggregates outside the exchange rate encourage and sustained the persistent net resource out flows in Nigeria. All the views however agree that exchange rates introduce externalities into the money supply and thus affect capital formation, investments and resource generation of the country generally.

Nigeria is also unable to exercise control over the production and distribution of her primary exports to the same degree that the advanced countries have over their own manufactured goods. Thus, the goods sent to Nigeria are usually over priced, especially those that are project tied. In some cases, the products are so priced to encourage dumping. All these constrain favorable balance of trade and a healthy balance of payments. Thus, we have a situation where the distribution of value added from international trade is weighted against Nigeria.

Another cause of the debt problem is the fraudulent and unpatriotic actions of the citizens. Through the system of over invoicing, fraudulent practices and collusion with oversea partners / suppliers, large sums of money are siphoned out of the economy to western economies. This is the genesis of the capital flight in Nigeria. It is also a well – known fact that the leaders (political and business) use all conceivable means to siphon. Money away from the country to overseas bank. Essentially, holding a slice of power – especially positions where the treasury is easily accessible, would invariably mean joining the "rat race" to transfer money abroad for the rainy day.

The faulty development plans, poor industrial and domestic economic policies pursued since independence also exacerbated the debt crisis. The various governments managed the economy on ad hoc basis and although development plans exists, no conscious attempts were made to pursue long-term development objectives. Moreover, no proper coordination exists between the various targets prescribed. A case in point is the various industrial policies pursued since independence. At a point the emphasis was import substitution. The industrial sector consisted merely of assembly plants (Adejugbe, 1987). The implication of this was that industries had very little backward linkage in the economy, since the bulk of the inputs were imported. The various industrial policies only served as a drain on the foreign exchange position of the country resulting in balance of payments disequilibria, especially since all components and inputs – raw materials, machinery, spare parts. Technology and technical acknowledgment were imported from the western countries.

The mismanagement of resources as is prevalent in the establishment of public enterprises in Nigeria, was also a major source of leakage in the economic system. The establishment of unproductive projects affects effective resource use and capital building. Thus fiscal deficits were very often accumulated a result.

External debts usually impose a burden on the present and future generations of any country. To ensure that debt does not threaten political stability, the burden of debt service should not leave the debtor in a state of long-term economic stagnation. Sadly, this has been the experience of most of the debtor countries in sub – Saharan Africa, - Nigeria is not an exception to the issue of debt burden. Debt burden arises principally because the country must pay interest and principal on the debt without necessarily receiving corresponding benefits in return (spencer, 1975). Most of such debts are never used in purchasing capital goods for regenerative or investment purposes or creation of jobs for citizens, such that the resultant current output is at least large enough to aver the interest and principal payments on the debt.

2.9 MONEY CRETATION

This is a possible avenue of financing governmental activities. A sovereign government can finance its activities by money creation. This involves printing more money and crediting it to government accounts, from where the government can make drawings.

Money. Creation does not seem to involve sacrifice or giving up resources by anybody. This appears to be an easy way out; but it does have an impact on the economy if such an economy is not at a level of full employment of its resources. Money creation calls for caution and a prudent management of such an economy by it's government as this could lead to a process of hyper – inflationary trend.

2.10 CHARGES FOR GOVERNMENTAL GOODS AND SERVICES

Some of the goods and services provided by the government have the character of private goods. And so it is possible to charge for them specifically. This is referred to as user pricing which simply means charging users for the public services provided to them. This can be likened to the supply of such goods by the market pricing system. It is also possible that may not be split into units consumed e.g. tollgate fees. These are called user charges i.e. levies, the incidence and payment of which are related to the use of a particular public service. The revenue from the service may or may not be used to maintain the service origin. They may not pay the full cost of the services provided.

2.11 GOVERNMENTAL GRANTS.

According to George F. Break (1965: 105), the basic economic justification for federal functional grants – in – aid is provided by the widespread and ever increasing, spillover of benefits from some of the most important state and local expenditure programs.

Intergovernmental grants, sometimes called grants – in – aid are transfers of funds from one government to another, most often from a higher – level government in the federal system to a set of lower – level governments. These grants are of many different types and are intended to improve the operations of a federal system of government finance.

Traditionally four potential roles for intergovernmental grants in a federal fiscal system are identified. Grants may be used to correct for externalities that arises from the structure of sub national governments and thus can improve the efficiency of fiscal decisions; for explicit redistribution of resources among regions or localities; to substitute one tax structure for another and as a macro economic stabilizing mechanism for sub national government sector.

2.11.1 TYPES OF GRANTS

Inter governmental grants usually are characterized by four factors: whether use of the grant is intended for a specific service or may be used generally; whether grants are automatically allocated by a formula or require an application associated with a specific project; whether the grant funds must be matched by recipient government funds, and whether the potential size of grants is limited.

Records have shown that specific or categorical; grants are the dominant type, both by number and amount of funds, offered by the federal and state governments.

A grant is a lump sum, or non-matching, grant if the amount does not change as a recipient government changes its taxes or expenditure. The amount of the grant cannot be altered by fiscal decisions of the recipient governments

Matching grants on the other hand, do require recipient government taxes or expenditures, with the size of the grant depending on the amount of those taxes or expenditure. Typically, a specific matching aid program offers to match each dollar of recipient tax or expenditure on that specific service with R grant dollars, intended to be spent on that service “R” is called the matching rate.

General grants are those issued without use restriction. General grants are rare among federal government grants, but are more common among state grants. These grants, which are sometimes said to provide general fiscal assistance, almost always are allocated by formula. If the formula includes factors outside of the direct control of the government, such as population or per capita income. The grant is a pure lump sum to the government.

On the other hand, if the formula includes factors controlled by the recipient government, such as tax collections or tax effort, then the amount of the grant can be altered by recipient government decisions.

2.11.2 INTERGOVERNMENTAL GRANT POLICY

Economic theory and evidence about the effects of alternative types of intergovernmental grants lead to three major conclusions about grant policy.

First, open – ended categorical matching grants are the best device if the objective is to increase recipient government expenditure on a specific function. A matching grant with a matching rate equal to the non resident share of benefits will offset the effects of inter jurisdictional externalities by reducing the local tax price. The lower price will induce the increase in expenditures necessary for efficiency.

Although other grants could be used to increase expenditure, an open – ended matching grant will induce the desired expenditure response with the smallest possible grant; matching grants provide the largest expenditure effect.

Second, general lump sum is a better mechanism than matching grants to redistribute resources among sub national jurisdiction. There is no economic reason for such grants to go to all jurisdictions; of course they should be targeted to low. Income or high cost jurisdictions.

Last, categorical lump sums and close – ended matching grants should generally be avoided. Close – ended matching grants become lump – sum once the maximum grant is reached and categorical restrictions do not alter grant effects unless the grant is large compared to recipient government expenditures in the category. If the objective is to increase expenditure or to induce recipients' governments to begin spending on a specific function, open ended matching grants are preferred.

2.12 NIGERIA'S REVENUE STRUCTURE AND PROFILE

The dictionary of banking and finance terms by John Clarke defined revenue as money received from transaction or sales or money received by government in the form of taxation.

For an economy to experience an upward thrust; there must necessarily be a form of government intervention. Government intervention on the free working of an economic system entails the divertion of some resources from the private to the public sector. Fiscal policy instruments are veritable tools for diversion of resources from private to the public sector.

In Nigeria, major fiscal policy instruments include changes in taxation rates on (personal income, company income, petroleum profits, capital gains, import duties, export duties and excise duties, as well as mining rents, royalties and NNPC earnings) and government expenditure (recurrent and capital). These taxes, along with interests repayments, and licensing fees constitute government's revenue. (Anyanwu: 2002)

Such taxes are imposed, not only to generate revenue but also to provide incentive and / or disincentives in certain specific socio – economic activities. Tariff rates are also varied not only to regulate the external sector of the economy but also to encourage domestic production as well as to protect domestic (Particularly infant) industries.

Prior to 1984; Nigeria's revenue structure stood as follows:

(1) Direct Taxes: personal income tax, company income tax, petroleum profit tax and other taxes (stamp duties, penalties etc).

(2) Indirect Taxes: Import duties, export duties, excise duties

(3) Other tax revenues.

(4) Non – tax revenue which include:

- Mining (Rents, Royalties, and NNPC sales).
- Interests and repayments
- Miscellaneous: Licenses, fees, earnings, sales, rent on government properly, reimbursement etc.

However. From 1984, a new reporting system for Nigeria's revenue was adopted as follows:

(1) Oil revenue: from export sales and autonomous foreign exchange market (afem surplus account)

(2) Non oil revenue:

- Company income tax
- Customs and excise duties
- Value – added tax (VAT) – from (1994).
- Federal government independent revenue from interest payments, rents on government properties, personal income tax of armed forces, police, external affairs and federal capital territory

(3) Afem surplus account (from 1995).

The aforementioned entries give the federally – collected revenue which is allocated to the following sub heads: Federation account, federation stabilization account, vat pool account, petroleum trust fund (PTF), joint venture control (JVC), payment accounts, external debt service funds, National priority projects. Funds and Nigerian National petroleum corporation (NNPC).

In the same vein, the federal government retained revenue is made up of revenue from the following sources: federation account, VAT, federal government independent revenue, PTF, National priority projects, Afem surplus intervention fund, external debt service funds and others.

2.13 ANALYSIS OF THE LEVEL, COMPOSITION, PATERN AND TREND OF FERDERAL REVENUE

The federal level of government controls all the major sources of revenue – import duties, excise duties, mining rents and royalties; petroleum profit tax and company income tax. An important aftermath of such concentration of revenue powers at the federal level of government is the over – dependence of states and local governments on the federation account.

In 1980, totally collected revenue stood at N15.20 billion. Of this amount, oil revenue accounted for the sum of N12 .40 billion which represents 81.58% of the total amount. This trend continued with oil revenue accounting for N2074.30 billion in 2003 as against totally collected revenue of N2575.10 billion.

One would as a matter of fact conclude that Nigerian's revenue source have always been heavily skewed, concentrated as they were on just one or two taxes over the past three decades. Though the locus of concentration has changed over time from foreign trade taxation especially import duties to oil based taxes, but the heavily skewed nature remains unabated. In 1980, oil revenue accounted for 81.58% of federal governments revenue, in 1985 oil revenue stood at N10, 923.7 million or 74.4% of total federal government revenue. This fell to 60.9% in 1995 but with absolute amount rising to N279, 902.3 million. In 1995 non-oil revenue contributed only 21.8% of federal governments revenue. Among the non - oil sources, customs and excise duties and VAT remain the dominant contributor. In 1995, this gave 37.2% of the federal non-oil revenue with "VAT" contributing about 20.3%. In year 2003; oil revenue was N2074.30 billion or 80.55% of the totally collected federal government revenue, while non – oil accounted for 19.45% or N500 . 8 billion of the said revenue profile.

The relative and cyclical decline in the revenue yield from import duty has been compensated by the petroleum profit tax. However, in 1985, there was a sharp fall in petroleum profit tax. When it's enabling law was amended to "net in" the earnings of NNPC and rent and royalties. The impact of this amendment contributed further to the rise in the relative share of oil revenue.

2.14 .1 JUSTIFICATION OF PUBLIC SECTOR INTERVENTION IN THE PROVISION OF ECONOMIC ACTIVITIES, INFRASTRUCTURAL NEEDS AND GENERAL SERVICES

Under normal circumstances, because of its efficiency, the private sector, through market mechanism is the obvious choice for the provision of economic and welfare activities. However, even in the most democratic of all nations, substantial public sector still exists. The reasons are both historic and economic.

2.14.2 HISTORICAL PERSPECTIVE

Historically, the work of Adam Smith (Wealth of Nations, written in 1776) stated four justifiable areas of government allocation activities and they are:-

(i) The duty of protecting the society from violence and invasion by other independent societies – National defense.

(ii) The duty of protecting every member of society from the injustice or oppression of every other member of the society – the obligation of establishing an administration of justice which provides law and order within the society, so that the market economy may function.

(iii) The duty of establishing and maintaining highly beneficial public institutions and public works which are of such a nature that the profit they could earn would never repay the expense to any individual or small number of individuals to provide them. Therefore, funds for their provision may never be adequate.

(iv) The duty of meeting the expenses necessary for support of the sovereignty which varies depending on the political structure (Smith 1913)

It would, therefore, be seen that even though Adam Smith has been seen as an apostle of minimal governmental activity, he never supported outright ban of public sector activities.

2.14.3 ECONOMIC PERSPECTIVE

The economic or modern case for public sector intervention will be considered using a three-pronged approach. They are the allocation, stabilization, and distribution activities.

Herber (1979) and musgrave (1982) outlined the following reasons for intervention based on allocation function.

2.14.4 ALLOCATION FUNCTIONS

2.14.4.1 DECREASING COST OF PRODUCTION AND IMPERFECT MARKET STRUCTURE

Under conditions of imperfect market structure, a significant allocational problem crops up if marginal cost equals average revenue at a point of output where the average cost of production is decreasing. Under this condition, the best profitable point of production for the firm – marginal cost equal to marginal revenue – does not coincide with the optimal social allocation point for the society – marginal cost equal to average revenue (price). This leads to serious misallocation or reduced output and the situation calls for intervention.

2.14.4.2 ZERO MARGINAL COST.

Under this situation, the social optimum output would be at a point where the price of the good is zero. This is an extreme variation of the decreasing cost condition, which would require that the good be provided, free of charge; since additional individuals can consume it without any increase in production costs. In this case, it will amount to inefficiency if any price should be charged for the good. However, it is known that this is not possible. An example that readily comes to mind in this regard is in the provision of radio and television services.

2.14.4.3 <u>THE CONCEPT OF JOINT (COLLECTIVE) CONSUMPTION WITH NON EXCLUSION.</u>

The allocative argument here is that consumers may not pay for goods with joint or collective consumption and non – exclusive characteristics voluntarily. This is unlike private goods where non – payers may be excluded from consumption. In this case, free – rider problem may make it impossible for the goods to be produced privately. Therefore, the public sector comes in to finance the production such goods through compulsory means such as taxation.

2.14.4.4 <u>SPECIAL SUPPLY CAUSES OF MARKET FAILURES IN RESOURCE ALLOCATION</u>

There are also other causes in resource allocation activities, which can lead to an economic role for government, and they include:

(i) There may be lack of adequate market knowledge by producers, which may prevent them from attaining sufficient output levels of an important economic good. The government is expected to come in here to supply the missing information

(ii) Immobility of productive resources may not allow for the attainment of efficient resource allocation. So, government steps in to encourage free movement of resources to areas of need. An example is the allowance of deductions for moving expenses in United States federal personal income tax law when job locations are changed. This is worthy of emulation by Nigerian government.

2.14.4.5 REJECTION OF MARKET FAILURES APPROACH: THEORY OF SECOND BEST

Some scholars of public finance have seen the approach of justifying public sector intervention on market failure as being both anti – state and pro – state. For instance, kittick (1983) sees the Pareto optimality on which most of state justification is based as unattainable especially in developing economies. He is therefore, of the opinion that the second – best option, which is achievable and close to the theoretical optimum point is better pursued.

Protagonist of second – best theory justifies the existence of the public sector as every government in power manipulates events to achieve the desired objectives. This, it does by fine – tuning policies and re – fine tuning until the desired objectives are achieved.

2.14.4.6 MODERN CASE FOR PUBLIC SECTOR STABILIZATION ACTIVITIES

2.14.4.7 STAGFLATION:- The pioneering work of Keynes (1936) proved that market economics do not automatically attain an optimal full employment, non – inflationary aggregate economic equilibrium. Although Keynes agreed that such an equilibrium may be possible, more likely situations would be two "sub – optimal equilibrium", with deflationary gap or inflationary gap. It is well known that given substantial market structural imperfections, there exists market inability to simultaneously attain, the objectives of both full employment and price stability. The greater the degree to which one goal is achieved, the lesser the degree to which other would be attained. This situation further helps in the resultant condition of stagflation (musgrave and musgrave: 1982). The state therefore intervenes with policies capable of swaying the situation to what is desired during a particular period.

2.14.4.8 THE PROBLEM OF INADEQUATE ECONOMIC GROWTH

The forces that achieve economic growth require a significant dose of both economic and non – economic variables. Quantitative expansion of productive resources, particularly capital and qualitative improvements of these resources are essential to the maintenance of a satisfactory and sustainable growth rate.

If an economy is to grow steadily, it must have a continually rising level of production capacity and this does not come automatically. In line with this, fischer (1993) finds that a stable macro economic environment is conducive to sustained growth.

Thus, to facilitate economic development and sustained growth, there is invariably a need for government intervention in economic activities.

2.14.4.9 PROBLEMS WITH BALANCE OF INTERNATIONAL PAYMENTS

Balance of international payments of a country also plays a role in justifying the existence of public sector. This is particularly true in an open economy, which deals significantly in international product and resource markets. Moreover, Herber (1979) is of the opinion that when monetary exchange rates between nations are less than fully flexible, an expanding domestic economy, especially if accompanied by price inflation, can lead to an expansion of imports and a contraction of exports. This situation calls for action by government, since it cannot be automatically corrected.

2.14.4.10 FISCAL POLICY INSTRUMENTS FOR STABILIZATION

Fiscal policy instruments may be grouped into two – the automatic fiscal stabilizers and the discretional fiscal stabilizers. While the automatic fiscal stabilizers are built into the budgetary structure as automatic response of a counter – cyclical nature, discretionary fiscal stabilizers consists of ad hoc discretionary policy strategies directed towards a current, aggregate, malfunction in the economy.

The instrument of fiscal policy whether automatic or discretional are implemented through budgetary procedures of taxation and expenditure. In Nigeria, such ad hoc policies or discretional measures involve changes in tax rates or tax bases, adoption or deletion of a tax and deliberate changes in government spending. They are rationally directed towards the improvement of the aggregate performance of the economy in terms of such important objectives as full employment and price stability.

2.15 JUSTIFICATION FOR GOVERNMENT INTERVENTION IN DISTRIBUTION ACTIVITIES.

2.15.1 SOCIETAL DESIRE:

Taking into consideration the societal concept of distributive justice, it may be taken for granted that a society should assist those who are incapable of helping themselves. It therefore, follows that society has already made a decision that some redistribution of income and / or wealth is desirable under this situation, the government cannot be neutral but should act since a decision to help a needy section of the population entails redistribution from a "better off" to a worse off (Hockley 1922)

2.15.2 NEED FOR AT LEAST MINIMUM ENJOYMENT OF SERVICES / GOODS.

The need to give the citizenry a minimum level of comfort calls for government redistribution activities.

It may need to be pointed out that needs are satisfied equally only when income is spread unequally. In this case, economic welfare can be increased by government provision or redistribution. In line with this, Dalton (1959) writes

Income consists of the means of economic welfare, and great inequality in incomes in any community implies great inequality in the economic welfare attained by different individuals. But this is not all. For it implies also considerable waste of potential economic welfare. Put broadly and in the language of common sense, the case against large inequalities of income is that the less urgent needs of the rich are satisfied, while the more urgent needs of the poor are left unsatisfied. The rich are more than amply fed, while the poor go hungry. This is merely an application of the economists law of diminishing marginal utility, which states that, other things being equal as the quantity of any commodity or more generally, of purchasing power, increases, its marginal utility diminishes.

2.15.3 DISTRIBUTION AS A SOCIAL GOOD

Distribution calls for government intervention when it is seen as a social good. If a donor derives welfare not from adding to the well being of a particular recipient but (proceeding in a more intellectual fashion from reducing the overall degree of inequality in society at large. In this situation, the potential donor would see very little use in individual giving. The problem appears similar to provision of social goods, X will find it worthwhile to contribute only if “Y” and “Z” do the same and since each may act as a free rider, taxes (government intervention) are needed just as they are with social goods (musgrave and musgrave; 1982).

2.15.4 DISTRIBUTION AS MERIT GOOD

Issue of merit good is another area that justifies the intervention of public sector. It would be recalled that in any economy, some goods, which are necessary, are considered as “meritorious” while some are considered as undesirous. For instance, while education is considered as a merit good and subsidized by various governments, alcoholic drinks are considered undesireous and taxed. It is necessary to point out that the issue of merit goods cuts across private and public sector, as goods which are private in nature (such as low cost housing, may be considered as merit goods, just as some social goods may be considered as de – merit goods.

If the purpose of such and in the provision of goods like low – cost housing were merely redistributional, the objective would have been better achieved by cash grants, so that the individual decides on what to buy. However, by making the grant in kind, the governments own preferences are imposed on the individual. This is in conformity with the wishes of a majority who can be found for contributing to, say the housing consumption of the poor, but not for adding to their income, which may be spent on frivolous and undesirable things. Such restrictions, even though, may be seen as interference with the recipient's choice, but are better viewed as conditional clarity of federal (but not imposed) by the donor. It may be pointed out, however that such provisions are not restricted to only goods consumed by the poor, as some goods enjoyed by the wealthy sometimes have similar subsidies.

The formulation of providing or helping to provide a specified basket of goods e.g. essential items of food, clothing and shelter is known as categorical equity and links the merit – good approach to that of distributive justice. This concept which involves all the problems of merit – good concept, along with it helps to explain the prevalence of public policies aimed at in – kind support of low – income house holds or at subsidizing products bought by them (musgave and musgave: 1982).

2.15.5 EFFICIENCY COST AND DISTRIBUTION

In formulating and implementing distribution policies, efforts should be made to see that this is done with minimum efficiency cost. If the hard working citizen sees distribution policies as punishment for hard work, there is a tendency for him to work less. In the same vein, a lazy citizen that sees that government guarantees his three square meals may love to enjoy his leisure and may not make effort to work. This is one of the reasons against unemployment benefits in developing countries. In Nigeria, the fabulous pension allowances of soldiers, which sometimes are up to 100% of their monthly salaries, may be part of the reasons why we have many retired generals who are less than fifty years. Many see early retirement with such benefits very tempting to resist.

2.15.6 THE CONVENTIONAL WISDOM ON THE ASSIGNEMENT OF FUNCTIONS AND RESOURCES

The three major functions often assigned to the public sector (i.e. government) are allocation, distribution and stabilization. Under government's allocation functions, it determines those functions that would be performed by the private sector and therefore, those that would be publicly provided as well as determines which tier of government will provide each good that is to be publicly provided. Under its distribution function, it redistributes incomes and resources to promote national unity and equity while under its stabilization roles; it is expected to ensure economic and monetary stability.

The governmental wisdom in the theory of public goods and public choice is that both the redistribution and stabilization functions be performed by the central government as those functions would be performed by the central government as these functions would be inefficiently performed by local governments because of the divergence between national benefits and local benefits, divergence between national costs and local costs and free – rider problems (musgrave and musgrave; 1989, layard and walters, 1978, etc). In respect of public goods provision, the conventional wisdom is that the central government should provide national public goods whose spatial incidence of benefits covers the entire country e.g. defense, foreign affairs etc. similarly a state / region / local government should provide local public goods whose spatial incidence of benefits is limited to a state/region/local government area covers the entire country e.g. defense, foreign affairs, etc. Similarly a state / region / Local government should provide local public goods whose spatial incidence of benefits is limited to a state / region / local government area and conform to a unique taste / preference pattern. However, when the provision of a local public good enjoys substantial economies of scale or / and when the provision and consumption of a local public good produces substantial externalities, the cause of efficiency may be promoted if such is provided by central government (musgrave and musgrave, 1989; Tiebout, 1956 etc).

As it relates to revenue collection and sharing, the conventional wisdom suggests that in order to reap both the benefits of central and decentralized revenue collection, revenue collection should not be over centralized. This would require that revenue collection powers be shared between the different tiers of government in a manner that ensures that revenue collection powers are closely aligned with expenditure functions (Tanzi, 1995 etc.). This is because while centralized collection of revenues would promote efficiency in the central government's performance of its "distribution", stabilization and the provision of national public goods functions, results in substantial economies of scale in tax administration and promotes uniform taxation across the country, decentralized collection is known to promote efficiency in the provision of local public goods, promote accountability and responsibility as well as real fiscal autonomy of lower tiers of governance (Tan31, 1995; Gboyega 1994; etc). When some inevitable imbalances exist, revenue sharing function of the central government should be exercised in such a manner that would ensure equitable provision of merit goods, promotion of national unity and equity (e.g. through grants). It is against these prescriptions of the conventional wisdom that fiscal federalism experience of a country is to be judged.

2.16 FEDERALISM IN NIGERIA

Nigeria became a single political entity when under lord luggard; the southern and Northern British protectorates were amalgamated in 1914. Though the Clifford constitution brought some constitutional reforms, it was not until 1946 that the Richard constitution sowed the first seed of federalism in Nigeria but even then, Nigeria was still a unitary colony. The McPherson constitution of 1951 further strengthened the elements of federalism contained in the Richard constitution by creating some resemblance of federalism in the administration of Nigeria to the extent that the period between 1951 and 1953 is often referred to as a period of quasi federalism in Nigeria. In 1954, the Littleton constitution granted a large measure of regional autonomy and this could be said to be when full federalism arrived on the Nigerian political scene (Nwosu; et al, 1998).

Since 1954 till date, Nigeria has been governed as a federal state except in the periods of military rule when it experienced nominal federalism. Similarly too, as constitutional development produced political federalism, fiscal federalism was a bye product.

2.17 FISCAL FEDERALISM

Fiscal federalism refers to a decentralized system in a federation, (Nnamocha, 1997) it is intergovernmental fiscal relations as enshrined in a federal constitution providing for the functional responsibilities to be performed by the financial resource that can be raised and shared for provision of collective goods and services. It recognizes that the role of the state in economic management may have to be performed by two or more governments and not one central government as in a unitary system of government. Fiscal federalism specifies the functions to be performed by each tier of government and provides for the financial resources to be used in carrying out the functions.

2.17.1 PRINCIPLES OF FICAL FEDERALISM

In fiscal federalism, certain ground rules are necessary for there to be good relationship among the various levels and units of governments making up a federation. Such rules called principles are out lined by musgrave and polinsky (1970) as follows: -

(1) The principle of Diversity: The federal system should leave scope for variety and differences in fiscal arrangements pertaining to various

states and localities. Communities may differ in their preferences for public services and should not be forced into uniform pattern.

(2) **The principle of equivalence:** Cognizance must be taken of the fact that the spatial scope of various public services differs. The benefits of some are nation wide, such as defense, those of others are region – wide such as flood control and those of still others are local, such as street lights. Similarly the burden incidence of some taxes can be confined to a particular area more readily than that of others. For fiscal arrangements to be truly efficient, each type of service would be voted on and paid for by the residents of the area, which benefits.

(3) **The Principle of Centralized Redistribution:** The redistributive function of fiscal policy (i.e. progressive taxation and transfers) should be centralized at the federal level. Otherwise, redistribution becomes ineffective and location decisions are distorted.

(4) **The Principle of Locational Neutrality:** regional fiscal differences tend to interfere with the location of economic activity. Some degree of interference is an inevitable cost of fiscal federation, but it should be minimized. Differential taxes which (in the absence of offsetting differential benefits) distort location decisions should be avoided.

(5) **The Principles of Centralized Stabilization:** The use of the fiscal instruments for purposes of macro (stabilization, growth) policy has to be at the national level. It was further stated that because of inadequacies and imperfections in any federalism, the following supplementary criteria are also relevant.

(6) **Correction of Spillovers:** Benefit spillovers between jurisdictions lead to inefficient expenditure decisions. This calls for correction by higher levels of government.

(7) **Minimum Provision for essential public services:** The national government should ensure that each citizens, no matter in which state or

locality he resides, is provided with a minimum level of certain essential public services, such as safety, health, welfare and schooling.

(8) **Equalization of Fiscal Position:** While redistribution is primarily an inter – individual matter, the existence of sharp regional differences in the balance between fiscal capacity and need among governments cannot be disregarded entirely. Some degree of fiscal equalization among governments is called for so that minimum service levels can be secured with more or less comparable tax efforts.

2.17.2 **FISCAL FEDERALISM: THE NIGERIAN EXPERIENCE** We will examine the Nigerian experience with fiscal federalism under the following four major sub headings: Expenditure assignment, tax types and jurisdictions, rights to revenue and revenue sharing, and lastly the revenue allocation formula.

EXPENDITURE ASIGNMENT

Since Nigeria became independent in 1960, the assignment of government functions among tiers of government, have not changed significantly except for few exceptions during the military regimes. In the different constitutions, Nigeria has operated; the exclusive list contains the functions reserved for the federal government only. On the concurrent list, both the federal and the state governments could function, however, when there is a conflict, the federal government shall prevail. The functions reserved for the states are found in the residual lists, which are functions not assigned to local government and neither contained in the Exclusive, nor concurrent lists. The table below presents a summary of the assigned expenditure responsibilities among the tiers of government in Nigeria as of 2002.

ASSIGNMENT OF EXPENDITURE RESPONSIBILITIES IN NIGERIA, 1999

Level of Government	Expenditure category for which it is responsible

Federal only -------	Defense, foreign affairs international trade including export. Currency, banking, borrowing, exchange control. Use of water resources, shipping federal trunk roads, elections ,Aviation, Railways, Postal service price control, police & other security services Regulation of labour, interstate commerce, Telecommunications, immigration. Mines and minerals, nuclear energy, citizenship and naturalization, rights, social security, insurance, Business Registration, National statistical system (census, births, death) Guidelines and basis for minimum education.
Federal – State (Shared) -----------	Health, social welfare, culture, Education (post primary / technology), Antiquities, Monuments, archives, statistics stamp duties, commerce, industry, Electricity (Generation, transmission, distribution) Research surveys.
State Only -	Residual power i.e. subject neither assigned to federal nor local government level.
Local Government -	Economic planning and development, Health services land use control and regulation of advertisements, pets, small business, markets, public conveniences, social welfare, sewage, Refuse Disposal registration of births, death, marriages. Primary, adult and vocational education Development of agriculture and natural resources.

Source: Nigerian 1999 constitution.

As could be seen from the above table, matters of national interest e.g. defense, foreign affairs, currency, Aviation, price control etc are assigned to the federal government only. Also, local matters e.g. marriages; markets, refuse, etc are assigned to local governments. Though Economic Planning and development is assigned to local governments, this function, over the years, has been performed by federal and state governments. Overall, this structure of assignment of responsibilities appears to be in tandem with the patterns in most federal states in the world today.

2.17.3 TAX TYPES AND JURISDICTIONS

The table below presents a summary of tax jurisdictions of different tiers of government in Nigeria indicating the source of power to collect the tax (Law), who has the duty to collect it (Administration and collection and who has right to the revenue so collected. One cannot help concluding that the type of taxes levied in Nigeria have remained virtually unchanged over the years.

NIGERIAS MAJOR TAX JURISDICTIONS AND RIGHT REVENUE FOR SOME SELSCTED YEARS.

Types of Tax			Right to Revenue
	1952	1993	1999
(1) Import duties	Federal	Federal	Federation A/C
(2) Excise duties	Federal	Federal	Federation A/C
(3) Excise duties	Federal	Federal	Federation A/C
(4) Mining Rents & Royalties	Federal	Federal	Federation A/C
(5) Petroleum profit tax	Federal	Federal	Federation A/C
(6) Companies Income tax	Federal	Federal	Federation A/C
(7) Capital gains tax	Regions	States	States
(8) Personal Income tax	Regions	States	States
(9) Personal Income tax (p)	Federal	Federal	Federal
(10) License fees in TV & radio	Regions	Local	Local
(11) Stamp duties	Regions	States	States
(12) Capital Transfer tax (CTT)	Regions	States	States

(13) Vat (sales tax b/41994)	Regions	Fed/States	Fed/States
(14) Pools Betting	Regions	States	States
(15) Motor vehicle & Drivers lance	Regions	States	States
(16) Entertainment tax	Regions	States	States
(17) Land registration & survey	Regions	States	States
(18) Property taxes	Regions	States	States/LGA
(19) Market & trading License.	Regions	LGA	Local

Source: constitution of the federal republic of Nigeria.

A summary of who has right to different types of taxes for some selected (as depicted in the above table) indicates that while the tax types have remained virtually unchanged since independence, a number of changes had occurred with respect to who has right to revenues. The most significant is probably is that of mining rents and royalties. Before 1959, regional governments have rights to 100 percent of mining rents and royalties but with production and exportation of oil in 1958, and following Raisman commission recommendations in 1959, this was to be distributes as follows:

Mineral Region (50%)

Federal (20%)

Distributable Pool Account (30%)

Another change that is significant is that in 1994, sales tax, to which states (or regions) hitherto had 100% right was replaced by value Added Tax (VAT and which is to be federally collected. Today, federal government has right to 35% of this revenue. In virtually all cases, the changes have been in the favor of the federal government and at the expense of the states.

Lastly, while responsibilities for the administration and collection of major different types of taxes would seem, on the surface to an optimal distribution; a closer look will reveal that the federal government's mix will always ensure a lion share of totally collected Nigerian revenue.

2.17.4 RIGHT TO REVENUE AND REVENUE SHARING AMONG TIERS OF GOVERNMENT

Since 1946 when the first seed of federalism was sown in Nigeria, all major constitutional changes and / or changes in administration have been associated with attempts to modify or change the revenue sharing rights of the different tiers of government (Ovwasa, 1995). This was usually preceded by the appointment of fiscal commissions. In all, about 9 fiscal commissions were appointed to examine Nigerian revenue sharing arrangement between 1948 and 1988; these include Philipson (1948), Hicks. (1952), chick (1954) Raisman (1959, Binns (1964), Dina (1968, Aboyade (1977), Okigbo (1979) and Danjuma (1988) commissions (OVWASA, 1995). The recommendations of these commissions had often influenced the revenue sharing formula adopted at the respective periods in the main, they determine the tiers of government that have rights to revenue collected.

2.17.5 VERTICAL ALLOCATION OF FEDERALLY COLLECTED REVENUES

Like the arrangement for tax collection, the arrangement for sharing federally collected revenue is some what skewed in favour of the federal government. First the federal government retains some of the federally collected revenues as its independent revenues.

2.18 REVIEW OF PAST REVENUE ALLOCATION SHEME

Richards's constitution of 1946 granted internal autonomy to the regions and consequent sharing of responsibility between the federal and regional government, provided the need for the first attempt at the revenue allocation exercise in Nigeria. There were the following six revenue allocation commissions between 1946 and 1969, which were on adhoc basis.

(1) Phillipson commission (1949)

(2) Chicks – Phillipson commission (1951)

(3) Chicks commission (1953)

(4) Raisman commission (1958)

(5) Binnus commission (1964)

(6) Dina committee (1969)

Decree on revenue allocations were also issued in 1967, 1970, 1971 and 1975. Since emphasis is more on the recent past, suffice it, just to mention the achievements of these efforts. National revenue Allocation, mobilization and fiscal commission (1991) listed them as:

(a) The establishment of regional / state government autonomy over certain revenue sources (e.g. personal income tax)

(b) The establishment of federal government exclusive control of some revenue sources (e.g. armed forces income tax)

(c) The creation of a distributable pool account into which other revenue including import and export taxes, mining rents and royalties etc) were paid and which was subsequently distributed between the federal and regions / state governments.

(d) The development of revenue allocation principles, such as derivation, population, even development etc. On the basis of which fund in the Distributable pool account were shared among regions / states.

2.18.1 <u>SOME OF THE PRINCIPLES ON WHICH REVENUE ALLOCATION IS BASED IN NIGERIA: -</u> This refers to the yardstick used to determine what goes to whom in sharing the revenue. In Nigeria, to be able to decide what percentage of the revenue should go to the federal, states and local governments and also to decide what each state government gets, the following principles have been used at various times by various commissions.

(1) **<u>DERIVATION:</u>** Regions / states should receive allocation in proportion to revenue collected from them.

(2) **EVEN DEVELOPMENT:** To ensure even development and uniform progress, poorer states are to be given more revenue.

(3) **NEED:** Revenue to be shared according to the need of a state

(4) **NATIONAL INTEREST:** Allocation based on things that are of high social importance, things that unite the country e.g. education and police in the 1951 constitution

(5) **INDEPENDENT REVENUE EFFORTS:** Allocation is based on how much of the revenue due to the state; she (the state) was able to collect.

(6) **CONTINUITY OF GOVERNMENT ACTION:** Revenue to be shared in such a way that subsequent allocation should not give a government less than what it got in the previous allocation

(7) **FINANCIAL ALLOCATION COMPARED TO RESPONSIBILITY:** Allocation being based on the responsibility of the level of government

(8) **EQUALITY OF STATES:** All states are treated as equals because each is required to perform certain minimum functions.

(9) **POPULATION:** Allocating Revenue in proportion to the population of the state / local government area.

(10) **NATIONAL MINIMUM STANDARD:** Revenue being allocated in recognition that all states must provide minimum level of certain services e.g. education. Hence states below the standard will receive more allocation to enable them measure up to the National minimum standard.

(11) **EQUALITY OF ACCESS TO DEVELOPMENT OPPORTUNITIES** Allocating revenue in such a way that those below certain level of development will be given more allocation such that all states will have equal access to development.

(12) **ABSORPTIVE CAPACITY:** revenue allocation is being based on the ability of the state to absorb the allocation. By this criterion economically advanced states will receive more because they can absorb the increase revenue with ease.

(13) **TAX EFFORT:** This gives more to states that make more effort to collect taxes due to them.

(14) **FISCAL EFFICIENCY:** Allocation according to how efficient a state has been in tax matters and government revenue.

(15) **LAND AREA:** Revenue allocation is in proportion to the area of land occupied by the states.

(16) **SCHOOL ENROLMENT:** Allocation is based on the number of pupils in the state / Local Government area.

(17) **PUPIL OF SCHOOL AGE NOT IN SCHOOL:** By this, higher allocation is given to states with more pupils of school age that are not in school to help such / LGA to send such pupils to school. Some of the problems associated with the above listed principles include:

- What does each principle mean precisely?
- How do you quantify the principles or translate it into operational terms.
- What problems is one likely to run into when trying to quantify the principle? And
- At what stage in the revenue allocation system is a principle used or asked for and why?

2.19 REVENUE ALLOCATION EFFORTS IN 1970'S AND 1980'S

Between 19977 and 1984, more comprehensive revenue allocation schemes were embarked upon and they include

(a) Aboyade Committee (1977)

(b) Okigbo Commission (1980)

(c) Allocation of revenue Act 1981 and

(d) Allocation of Revenue Amendment Decree (1984)

THE ABOYADE COMMITTEE REPORT.

As part of their transition to civil rule program, the Obasanjo led federal military government appointed the Aboyede technical committee on revenue allocation in 1977. In line with its terms of reference, the committees reviewed inter –

governmental tax jurisdiction and revenue allocation arrangement with a view to injecting better efficiency and economy in fiscal federalism.

In line with the fiscal efficiency and economy, the committee recommended the delineation of functions among the three tiers of government. National revenue mobilization, allocation and fiscal commission (1991) presented the following as the functions recommended by the committee.

Federal Government

(a) Defense and security
(b) External Affairs
(c) Inter state and international
(d) Roads.
(e) Port Facilities
(f) Railways
(g) Airport and Facilities
(h) Power supplies
(i) Communication
(j) Heavy industries
(k) Higher education.

State Government

(a) Secondary education
(b) Urban water supply
(c) Housing
(d) Health
(e) Lighter infrastructure and industries
(f) Agriculture
(g) Town and country planning

Local Government

(a) Sewage Disposal

(b) Maintenance of feeder roads

(c) Primary education

(d) Market stalls

(e) Rural health

(f) Crafts and small – scale industries

The following tax jurisdiction for the different tiers of government were also recommended

Federal Government

(a) Import Duties

(b) Export Duties

(c) Excise Duties

(d) Mining Rents and Royalties

(e) Petroleum profits tax

(f) Companies Income Tax

(g) Capital gains tax (legal basis only)

(h) Personal Income tax (armed forces, External affairs officers and federal capital territory)

(i) Sales and purchase Tax (legal basis)

(j) Stamp Duties (legal basis only)

State Government

(a) Sale or purchase taxes (except on commodities so designated by federal government) Administration and Retention

(b) Football pools and other batting taxes

(c) Estate Duties

(d) Gift tax

(e) Land tax (other than Agricultural Land)

(f) Land Registration (legal basis only)

(g) Capital gains tax (Admin and Retention)

(h) Personal income tax (Admin and Retention)

(i) Company tax (Admin. Only)

(j) Stamp Duties (Admin and Retention)

Local Government

(a) Property tax

(b) Market and trading licenses and fee

(c) Motor park tax

(d) Entertainment tax

(e) Motor vehicle tax and Drivers license fees

(f) Land Registration (Admin and Retention)

(g) License fees on TV and Radio (Admin and Retention)

In line with economy and efficiency principles in tax administration, the Aboyade committee was more concerned with setting up more effective administrative and fiscal controls than had ever been experiences in the fiscal history of Nigeria. It recommended that all federally – collected revenue be paid into the consolidated federation account (except the personal income tax of Armed forces, External Affairs Officers and FCT). The committee further recommended that such revenue be shared among the federal, states and local governments using the following percentages: -

Federal government	57
State government	30
Local government	10
Special Grants	3
	100

In addition to the share of local governments stated above, each state was supposed to pass through to its constituent local governments 10% of its total revenue receipts for sharing among them. The special grants were meant for special problems requiring attention, national emergencies, oil pollution and disasters. For sharing of revenue among the states from the state joint account, the following principles were advocated: -

(a) Equality and access to development opportunities

(b) National minimum standards for national integration

(c) Absorptive capacity

(d) Independent revenue and minimum tax effort.

(e) Fiscal efficiency

The committee finally recommended the establishment of a joint fiscal and planning commission periodic non – adhoc reviews of the federal fiscal system.

On the horizontal allocation; the committee recommended that the 30% meant for the states be shared with the following criteria.

Equality of access to development opportunities:	25
National minimum standards for National Integration:	22
Absorptive capacity:	20
Independent Revenue Tax effort:	18
Fiscal Efficiency:	15
	100

The committee report was however, rejected because it was said to be too technical to be understood and operated.

OKIGBO REPORT (1980)

On assumption of office, the shagari administration appointed an eight man presidential commission to harmonize the deliberations at the representations to the constituent assembly by the three tiers of government; on the need to ensure that each tier of government had adequate revenues to discharge it's constituent functions. Revenue allocation formula was to be examined and recommendations made.

Using the levels of expenditure by each tier of government (both recurrent and capital) as basis for allocating revenue among the three tiers of government.

The table below shows a summary of what the commission recommended and what the government in 1981 accepted and the amendment by decree in 1984.

VERTICAL ALLOCATION: THE OKIGBO GOVERNMENTS WHITE PAPER: 1981 ACT ANDN 1984 DECREE.

	Okigbo	GWP	1981 Act	1984 Amendment
i Federal Government	53 .0	55.0	55.0	55.0
Ii State Government	30. 0	30.0	30.5	32 .5 (a)
Local government	10 .0	2.0	10.0	10.0
Development of F.C.T	2.5	2.5	-	-
Mineral producing States; Derivation	-	2.0	2.0	2.0 (6)
Development of mineral Prod. Areas	2.0	1.5	1.5	1.5 (c)
Ecological general problem	1.0	1.0	1.0	1.0
Revenue Equalization	1.5	-	-	-

NOTE: GWP = Government white paper

(a) What is shared among states is 32.5% of the federation account, less 2% of the mineral revenue component of the 32.5% of the federation account.

(b) This 2% is not of the federation account but of the mineral component of the 32.5% of the federation account

(c) This 1.5% of the revenue accruing to the federation derived from the mineral producing areas (source: NRMA and FC report volume11, 1989, P 81)

Again the table below shows what Okigbo commission for horizontal allocation recommended. It is of interest and importance to note that what was recommended was wholly accepted by the government white paper, the 1981 act and the 1984 decree.

Horizontal Allocation

The Okigbo's GWP. 1981 Act and 1984 Decree-

		%	GWP	1991 Act	1994 Amendment
I	Minimum responsibilities of government	40. 00	40 .0	40 .0	40. 0
Ii	Population	40.0	40.0	40.0	40.0
Iii	Social development. Factor - Primary School.	11.25 3.75	11.25 3.75	11.25 3.75	11.25 3.75
	Enrolment of which - Direct enrolment – Investment enrolment				
Iv	Internal Revenue effects	5.0	5.0	5.0	5.0
		100	100	100	100

Source: NRMASFC Report Volume11, 1989, p82

2.19.1 THE 1984 ALLOCATION OF REVENUE DECREE N0. 36.

The Buhari administration that ousted the government of Shagari promulgated allocation of revenue Decree no. 36 in 1984. The decree, which introduced some minor amendments, provided for the distribution of the federation account as follows:

	Percent
Federal Government	55.0
State Government	32.5
Ecological problems	10.0
Mineral producing area	1.5
	100.0

2.19.2 **REVENUE ALLOCATION EFFORT, SINCE THE ESTABLISHMENT OF NATIONAL REVENUE MOBILIZATION, ALLOCATION AND FISCAL COMMISSION (NRMA & FC).**

The above commission was established on September 6th 1988. It immediately started work on a new allocation formula that would meet the test of time. Below are the vertical and horizontal allocations: The commission's recommendation and Government's approval.

	VERTICAL ALLOCATION	COMMS. RECOMMENDATION	AFIRC APPROVAL
I	Fed. Government 47 %	47%	50%
Ii	State Government 30 %	30%	30%
Iii	Local Government 15 %	15%	15%
iv	Special funds 8 %	8%	5%
a.	FCT	1% (Federation Acct.)	1%
b.	Stabilization	2.5% (Federation Acct.)	0.5%
c.	Savings	2.0% (Federation Acct.)	0
d.	Derivation	2.0%(Federation Acct.)	.1
e.	Oil producing	1.5% (Federation Acct.)	1.5
f.	Non oil producing	0.5% (Federation Acct.)	0
g.	General Ecology	0.5%(Federation Acct.)	1

Table 2.3

Horizontal Allocation: Commission's Recommendation And Government Approval

Table 2.4

Commissions Recommendation		AFRC Approval	
i.	Equality of states: 40 %	I	40 %
ii.	Population: 30 %	ii	30 %
iii.	Social Development factor: 10 %	iii	10 %
a.	Education	a	Education
b.	Health	b	Health
c.	Water	c	Water
d.	Landmass	d	Landmass & Terrain
iv.	Internal Revenue effort: 22	iv	Int. Rev. Effort.10

Source NRMA & FC Report 1989.

Following the dissolution of the National primary education commission in 1991 and the transfer vide decree 3 of 1991 of management and funding of primary education to local governments with effect January 1991, the commission recommended that 5% of the federation account be set aside for the funding of primary education through an independent and autonomous body. Even though this was not accepted as recommended, it led to a slight change in the revenue allocation formula in 1992- the first change since the 1989 formula. This led to increase in the share of local governments from the federation account from 15% to 20% and reduction of states share from 30% to 25 %.

The federal government in June 1992 revised the formula further, leading to a future reduction of the states share of the federation account from 25% to 24% and the doubling of the general ecology fund and the development of mineral producing areas fund from 1% to 2% and 1.5% to 3% respectively.

2.19.3 <u>REVENUE ALLOCATION AND AMELIORATION OF VERTICAL AND HORIZONTAL IMBALANCES</u>.

Prior to 1975, when revenue allocation formula was introduced, many sections of the country complained about the lopsidedness of revenue sharing. The main evil then, it was agreed, was the principle of derivation principally in use. But by 1975, when the principle of derivation was reduced to only 20% of in-shore mining, people believed that the horizontal imbalance had been reduced. Another major improvement was that distributable pool Account (DPA) became the major channel of revenue allocation. In addition, DPA become more generously composed and more equitable shared.

In line with earlier recommendation, the federal government established the National Revenue mobilization, allocation and fiscal commission in 1989 for, among other functions, the regular and unpublicized reviews of the revenue allocation formula. The first fruit of this effort was the revenue allocation formula that became operational with effect from January 1990. With this formula, the problem of vertical imbalance was much ameliorated.

The following critical and weights attached for sharing helped in the improvement of the revenue sharing scheme.

(a). Equality of States: This was used based on the fact that certain basic needs must be provided by a state irrespective of its size.

(b). Population: Based on the need to take politics out off population and thus minimize the manipulation of census figures, the commission recommended a reduction of the weight given to population from 40 percent to 30 percent.

©. Social Development factor: The proxy for measuring social – development factor was for the first time increased beyond primary enrolment. In addition to primary school / secondary / commercial school enrolment, number of state hospital beds, water and rainfall were added and given 10 percent. Within this, education, health and water had 40 percent, 30 percent and 30 percent respectively.

(d). Landmass and Terrain:

10 percent for landmass and terrain for sharing revenue horizontally was divided equally between landmass and Terrain. That of terrain was shared as follows:

i). Wet lands 2.0

ii). Plains 1.0

iii). Highlands 1.5

Internal revenue effort criteria was used as a means of encouraging the states and local governments to help in baking the national cake instead of thinking only of how to share it.

As a way of improving the revenue sharing formula, what was recommended and adopted was an approach based on incremental concept. The percentage increase of internally – generated revenue in a given period over the proceeding period was used as a measure of internal revenue effort for the period. The weight approved by government for this criterion was 10 percent.

Furthermore, as a way of improving the vertical imbalance between the local governments in a state on one hand and the state government on the other hand, each state government was supposed to pay to it's local government 10% of its internally – generated revenue. However, many state governments have not been keeping to this statutory requirement.

So, the problem of vertical and horizontal fiscal imbalance would continue to exist. What is appropriate is that as soon as such glaring imbalance is noticed, efforts should be made to ameliorate it through prompt manipulation of the existing revenue sharing scheme. The national revenue mobilization and fiscal commission was set up to do exactly that.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 INTRODUCTION

This paper uses time series data for the period1980 – 2003 using regression techniques to analyze and establish relationship between various sources of federal government revenue and her expenditure profile.

3.2 SOURCES OF DATA

The nature of the research work prompted the use of secondary data. The essence of using secondary is because of the nature of the study data, which essentially involve the use of published works. The data were collected from.

(a) Central Bank of Nigeria Statistical Bulletin (Various Issues

(b) Central Bank of Nigeria: Annual reports and statement of account (1980 - 2000)

(c) Several business journals and the

(d) Websites.

3.3 SAMPLE SIZE

A twenty-four year data of Nigeria's revenue and expenditure profile (1980 - 2003) were used. The data size is considered representative enough. Thus recommendations proffered from the outcome of the study should be adequate in scope to tackle identified problems.

3.4 MODEL DEVELOPMENT

Regression analysis is used in developing a model of relationship between sources of revenue and the mode of expenditure.

There are a total of eight (8) Hypothesis involved. Six (6) of them will be regressed against total expenditure of Federal Government, While hypothesis 7 and 8 will involve a regression analysis between the components of Federal Governments financing and the capita/recurrent expenditure pattern of the Federal Government respectively.

This model is expressed as:

$Y_1 = b_o + b_1x_1 + b_2 X_2 + \ldots b_k X_k + e_1$ .... Equation 3.1

Where

Y_1 = Expenditure pattern

b_o = The intercept

X_1 = source of revenue/type I

X_2 = source of revenue/type II

X_n = source of revenue/type "n"

$b_1, b_2, \ldots b_k$ = Slope or coefficient of independent variable (X– revenue type/source)

e_1 = error term

For the multiple regressions; the equations for the computations of the estimates are as follows

$$b = \frac{\sum X_1 Y \sum X_2^2 - \sum X2\, Y \sum X_1 X_2}{\sum X_1^2 \sum X_2^2 - (\sum X_1 X_2)} \quad \ldots\ldots\ldots\ldots \text{Equation} \quad (3.2)$$

$$\hat{b}_2 = \frac{\sum X_2 Y \sum X_1^2 - \sum X_1 Y \sum X_1 X_2}{\sum X_1^2 \sum X_2^2 - (\sum X_1 X_2)^2} \quad \ldots\ldots\ldots\ldots \text{Equation} \quad (3.3)$$

$$\hat{b}_0 = \hat{y} - (b_1 X_1 + b_2 X_2) \quad \ldots\ldots\ldots\ldots \text{Equation} \quad (3.4)$$

Where $Y = y - \hat{y}$, $X = X_1 - X_1$ and $X_2 = X_2 - X_2$ .... Equation (3.5)

Computing the deviations of these data, we have

$$\sum Y^2 = \sum Y^2 - {}^1/n\, (\underline{\sum Y})^2 \quad \ldots\ldots\ldots\ldots \text{Equation} \quad (3.6)$$

$$\sum X_1^2 = \sum X_1^2 - {}^1/n\, (\underline{\sum X_1}^2) \quad \ldots\ldots\ldots\ldots \text{Equation} \quad (3.7)$$

$$\sum X_2^2 = \sum X_2^2 - {}^1/n\,(\underline{\sum X_2})^{2.} \quad \text{.........................Equation} \quad (3.8)$$

$$\sum X_1X_2 = \sum X_1X_2 - {}^1/n\,(\sum X_1 \sum X_2) \quad \text{......................... Equation} \quad (3.9)$$

$$\sum X_1Y = \sum X_1Y - {}^1/n\,(\sum X_1 \sum Y) \quad \text{.......................... Equation} \quad (3.10)$$

$$\sum X_2Y = \sum X_2Y - {}^1/n\,(\sum X_2 \sum Y) \quad \text{..............................} \quad \text{Equation } (3.11)$$

The correlation coefficient (R) which measures the magnitude of the relationship between the dependent variable Y and independent variable (X) is determined using

$$R = \frac{N\sum X_1Y_1 - (\sum X_1)(\sum X_2)}{\sqrt{(N\sum X_1^2) - \sum X_1)\,(N\sum Y_1^2 - (\sum X_1)^2}} \quad \text{..................... ... Equation } (3.12)$$

Also the coefficient of determination (R^2) which measures the extent of the variation in the dependent variation (Y) that is being explained by the variation in the independent variation (X) is given by

$$R^2 = \frac{SSR}{SST} \quad \text{......... Equation} \quad (3.13)$$

Where SSR (sum of square due to regression) is given by:

$$SSR = b\left[\sum X_1Y_1 - \frac{\sum X_1Y_1}{N}\right] \quad \text{............ Equation } (3.14)$$

And

SST (total sum of square) is given as

$$SST = \sum Y_1^2 - \frac{(\sum Y_1)^2}{N} \quad \text{............................ . Equation} \quad (3.15)$$

However, the sum of squares due to error is given by:

$$SSE = SST - SSR \quad \text{Equation. ....}(3.16)$$

3.5 **TEST OF HYPOTHESIS**

The Hypothesis stated in chapter one are restated as follows:

(1) H_0: Federal Government does not depend on internally generated revenue in the funding of its expenditure in Nigeria.

(2) $H_{0:}$ There is no significant relationship between Federal Government expenditure profile and the Federation account.

(3) H_0 Federal Government does not depend on external loans in the funding of its expenditure in Nigeria.

(4) H_0: Federal Government does not depend on internal loans in the funding of its expenditure in Nigeria.

(5) H_0: There is no significant relationship between federal governments expenditure profile and the dedicated accounts.

(6) H_0: There is no significant relationship between Government expenditure and the amount of grants she receives

(7) H_0: The capital expenditure of the federal government has not been significantly financed through loans, grants and dedicated accounts.

(8) H_0: The recurrent expenditure needs of federal Government has not been significantly financed through internally generated revenue accruing to the Federal Government and allocation from Federation account.

The above stated hypotheses are tested using the outputs of the multiple regression analysis, which is the F – test.

The F – test statistics is calculated using the formula:

$$F^*_{cal} = \frac{MSR}{MSE} \qquad \text{…… …Equation (3.17)}$$

Where MSR (mean square due to regression) is given as:

$$\frac{\mathbf{SSR}}{K} \qquad \text{……..…Equation (3.18)}$$

Where k is the number of independent variable. On the other hand MSE (mean square due to error) is given by

$$\frac{SSE}{n-k-1} \quad \text{………… …Equation (3.19)}$$

Where "n" equals the number of observations or the sample size. All the above parameters are summarized in a table of Analysis of variance as follows:

ANOVA TABLE

Source of variation	**Sum of squares (SS)**	**Degree of Freedom (DF)**	**Mean square (MS)**	**F-Ratio**
Regression Error	$SSR = \sum Y^2R^2$ $SSE = \sum Y^2\ (1-R)^2$	K n-k-1	$MSR = \frac{SSR}{K}$ $MSE = \frac{SSE}{n-k-1}$	$F^* = \frac{MSR}{\mathbf{MSE}}$
Total	$SST\ = \sum Y^2$	n-1		

Courtesy Nworuh, (2001)

$$\text{Where } R^2 = \frac{b_1 \sum X_1Y + b_2 \sum X_2}{\sum X^2} \quad \text{……… Equation (3.20)}$$

Where

SSR = Sum of Squares of Regression

SSE = Sum of Squares of Error

SST = Sum of Squares of Total variation (Y)

K = Number of independent variables $(X_1, X_2)_2$

N = Number of Observations.

In the multiple regression, we are interested in testing whether or not there is a significant relationship between dependent variables (Y) (expenditure) and the independent variables X_1, X_2 .... (X_n)

3.6 DECISION RULE FOR TESTING HYPOTHESIS

A stated hypothesis is accepted or rejected based on the following decision rules.

Accept the null hypothesis (H_0) if $F^* < F_{1-\alpha;}$ k, n-k-1 degree of freedom, otherwise the null hypothesis (Ho) is rejected.

$F_{1-\alpha\leq}$, k, n-k-1 is the critical value obtained from the standard F-distribution table and α=the chosen level of significance, which for the purpose of this study is 0.01.

3.7 COMPUTER SOFTWARE USED

In carrying out the multiple regression analysis that are presented in the next chapter, the software; statistical package for social science research (s.p.s.s.ver.11) is used.

CHAPTER FOUR

4.1 INTRODUCTION

This chapter intends to analyze and interpret the various parameters involved in the financing of federal government expenditure pattern Nigeria.

4.2 FINANCING OF FEDERAL GOVERNMENTS EXPENDITUE PROFILE (1980 – 2003)

The table below highlights federal government of Nigerian's financing of her total expenditure profile (1980 – 2003).

YEAR	FED GOVT INDPT. REV	ALLOCAION FROM FED ACCT	INTERNAL LOANS	EXTERNAL LOANS	GRANTS	DEDICATED /SPECIAL ACCOUNTS	RECURRENT EXPENDITURE	CAPITAL EXPENDITURE	TOTAL EXPENDITURE
1980	487.5	1250.8	387.1	255.3	0	1333.8	4805.2	10163.4	14968.5
1981	1997.3	5514.3	4200.8	464.4	0	-763.1	4846.7	6567	11413.7
1982	732.8	5086.3	3402	263.5	0	2438.6	5506	6417.2	11923.2
1983	710.1	5561.9	7057	1106.9	0	-4799.4	4750.8	4885.7	9636.5
1984	580.9	6686.3	2928.2	1184.5	0	-1452.3	5827.5	4100.1	9927.6
1985	838.9	9062.5	571.2	1045.9	0	1422.6	7576.4	5464.7	13041.1
1986	433.7	6311.6	475.5	708.1	0	8294.8	7696.9	8526.8	16223.7
1987	407.6	14551.4	6465.6	832.7	0	-238.6	15646.2	6372.5	22018.7
1988	540.5	15046.4	15046.4	1918.7	0	1882.1	19409.4	8340.1	27744.5
1989	938	18752.1	18752.1	5719	0	21417	25994.2	15034.1	41028.3
1990	1724	23575	23575	980.6	0	27896	36219.6	24048.6	60268.2
1991	3040.4	27788.8	27788.8	2972.6	0	670.2	38243.5	28340.9	66584.4
1992	4903.1	382240	38240	11859.6	0	14797.2	53034.1	39763.3	92797.4
1993	5626.5	51797.7	51797.1	16963.5	0	25705.2	136727.1	54501.8	191228.9
1994	3888.2	53661	53661	8390.8	0	34705.6	89974.9	70918.3	160893.2
1995	20761	325144	325144	22455.4	0	-126694.5	127629.8	121138.3	248768.1
1996	3407	81056	81056	7825.4	2000	274978.6	124491.3	212726.3	337217.6
1997	8339.9	101000	101000	13382.6	2000	311875.3	158563.5	269651	428215.2
1998	11431.6	124573	124573	16605.6	0	217719.5	178097.8	309015.6	487113.4
1999	20076.5	218874.5	218874.5	21040.8	0	423632.3	449662.4	498027.6	947690
2000	38061.8	502294.4	508844.4	11.9	0	56914	461608.5	239450.9	701059.4
2001	44405.2	530657.6	530657.6	0	0	324239.2	579329.1	438696.5	1018026
2002	68134.5	859014.9	859014.9	0	0	-58020.3	696777.7	321378.1	1018155.8
2003	54164.4	917104.4	917104.4	0	0	91005.1	984277.6	241688.3	1225965.9
TOTAL	**295731.4**	**3953860**	**1147096.5**	**112268.6**	**4000**	**1648957.9**	**4216696.2**	**2945217.8**	**7161914**

TABLE 4.1

Data picked from the above table is used in establishing relationships amongst the various variables. The information so generated is presented in our next table below.

4.3 RELATIONSHIP BETWEEN SOURCES OF FINANCE ANDEXPENDITURE PROFILE OF FEDERAL GOVT AS COMPUTED FROM TABLE 4.1

1.	FED. GOVT INDEPENDENT REVENUE = 295731.4 X 100 = TOTAL EXPENDITURE 7161914	4.13%
2.	ALLC FROM FED. ACCOUNT = 3953860 x 100 = TOTAL EXPENDITURE 7161914 1	55.21%
3.	INTERNAL LOANS = 112268.6 X 100 = TOTAL EXPENDITURE 7161914	16.02%
4.	EXTERNAL LOANS = 112268.6 X 100 = TOTAL EXPENDITURE 7161914	1.57%
5.	GRANTS = 4000 X 100 = TOTAL EXPENDITURE 7161914	0.05%
6.	DED. ACCOUNTS/SPECIAL FUNDS = 1648957.9 X 100 = TOTAL EXPENDITURE 7161914	23.02%
7.	(EXT. + INT.) loans + grants = 1263365.1 x 100 = TOTAL EXPENDITURE 7161914	17.64%
8.	PERCENTAGE OF LOANS, GRANTS AND DEDICATED ACCOUNTS/SPECIAL FUNDS TO CAPITAL EXPENDITURE (INTERNAL + EXTERNAL) LOANS + GRANTS + DEDICATED ACCOUNTS / CAPITAL EXPENDITURE = 2912323 / 2945217.8 X 100	98.8%
9.	PERCENTAGE OF INTERNALLY GENERATED REVENUE BY FEDERAL GOVERNMENT AND ALLOCATION FROM FEDERATION ACCOUNTS TO RECURRENT EXPENDITURE (INTERNALLY GENERATED + ALLOC FRM FED. ACCT.) RECURRENT EXPENDITURE =	

	4249591.4 / 4216696.2 X 100	
10.	PERCENTAGE OF ACCRUALS INTO FED. GOVTS. COFFERS THAT ARE DEVOID OF LOANS TO TOTAL EXPENDITURE (ALLC. FRM. FED. ACT + D. ACTS + FED GOV.INDPT REV = TOTAL EXPENDITURE 5898549.5 / 716194 X 100	82.36%

TABLE 4.2

Based on the established relationship; we hereby present answers to earlier stated hypothesis

4.4 MODEL DEVELOPMENT FOR THE RELATIONSHIP EXISTING BETWEEEN THE VARIOUS COMPONENTS OF FINANCING AND TOTAL EXPENDITUURE.

The output of the multiple regression and correlation analysis is as follows.

Regression of sources of financing on total expenditure

Model Summary[b]

Model	R	R square	Adjusted R square	Std Error of the Estimate	Durbin-Watson
1	1,000[9]	1.000	1.000	2196.6783	1.994

a. Predictors: (constant), x6, x2, x4, x5, x3, x1

b. Dependent variable Y

ANOVA

Model	Sum of squares	**df**	Mean square		Sig.
Regression	3.508E + 12	6	5.847E+11	121171	.000[9]
Residual	82031724.9	17	4825395.580		
	3.508E + 12	23			

a. Predictors: (constant), x6, x2, x4, x5, x3, x1
b. Dependent variable Y.

Model	Unstandardized coefficients B	Standardized coefficients Std Error	Beta	T	Sig
(constant)	165.268	619.28		.267	. 793
x1	.652	.121	.032	5.406	. 000
x2	1.029	.007	.707	138.0	. 000
x3	.979	.018	.180	53.027	. 000
x4	1.241	.087	.026	14.269	. 000
x5	- . 771	1.639	-.001	-. 470	. 644
x6	.999	.007	.348	142.4	. 000

a. Dependent variable: Y

Based on the above output, we develop the following model of relationship existing between the various components of financing and total expenditure profile of the federal government of Nigeria (1980 – 2003)

$Y = 165.27 + 0.65 x_1 + 1.029 x_2 + 0.98x_3 + 1.24 x_4 - 0.77 x_5 + 0.99 x_6$

Where

Y = Total Expenditure

X1 = Federal Government independent revenue

X2 = Allocation from Federation Account

X3 = Internal Loans

X4 = External Loans

X5 = Grants

X6 = Dedicated accounts / special funds.

This model shows that a positive change (increase) in federal government's independent revenue, allocation from federation account, internal and external loans and dedicated accounts / special funds elicits a corresponding change in total expenditure.

Amongst the variables considered, only (Grants) witnessed a negative change (Decrease) in its relationship with total expenditure.

The correlation coefficient (R) is 1.00. This signifies a perfect positive relationship between components of government financing and her total expenditure profile. The R – square value is 1.000, which is the coefficient of determination. Thus, the explained variation completely explains the regression function (Nworuh, 2001: 155)

4.5 <u>TEST OF HYPOTHESIS</u>

Using the output of regression analysis above and the decision rule stated in chapter three, we carry out tests of outlined hypotheses.

4.5.1 <u>HYPOTHESIS ONE (1)</u>

Ho: Federal government does not depend on internal sources / independent revenue in the funding of its expenditure in Nigeria.

This hypothesis is tested using the above multiple regression output.

$T_{cal} = 5.39 > t_{table}\ 0.01 = 2.878$

A $t_{calculated}$ value of 5.39, when compared with the critical value from t – distribution table of $t_{0.01}$ of 2.878 shows that the t – value is grater than the t_1 - <; (k, n –k – 1). We therefore reject the null hypothesis and accept the alternative hypothesis.

In addition to the above test; result of table 4.2.1 reveals that federal governments independent revenue accounts for 4.13% of her total expenditure

We, therefore conclude that federal government depends on her independently sourced revenue in the funding of its expenditure in Nigeria.

4.5.2 HYPOTHESIS TWO (2)

Ho: federal government does not depend on dedicated accounts / special funds in the funding of its expenditure in Nigeria.

The hypothesis is tested using the output from our above multiple regression analysis, where $t_{calculated} = 142.71 > t_{table}\ 0.01 = 2.878$

We therefore reject the null hypothesis and accept the alternative hypothesis.

In addition to the above test, result of table 4.2.6 reveals that dedicated accounts / special funds accounts for 23.02% of federal governments expenditure pattern in Nigeria for the period under review.

We conclude that federal government depends on dedicated accounts / special funds in the funding of it's expenditure in Nigeria.

4.5.3 HYPOTHESIS THREE (3)

Ho: There is no significant relationship between federal government expenditure profile and the allocation from federation account.

This hypothesis is tested using the output of our above multiple regression analysis, where $t_{calculated} = 147 > t_{table}\ 0.01\ (\ ) = 2.878$

Going by this output; we reject the null hypothesis and accept the alternative hypothesis.

Furthermore, result of table 4.2.2 reveals that allocations from federation account amounted to the sum of N395 3860 million. This accounts for

55.21% of federal governments expenditure profile for the period under review.

We conclude that there is a significant relationship between federal government's expenditure profile and the allocation from federation account.

4.5.4 HYPOTHESIS FOUR (4)

Ho: Federal government does not depend on external loans in the funding of its expenditure in Nigeria.

This hypothesis is tested using the output of the above multiple regression analysis where

$T_{calculated} = 14.26 > t_{table}\ (0.01) = 2.878$

With this result, we reject the null hypothesis and accept the alternative hypothesis.

In addition to the above test, result of table 4.1.4 reveals that external loans accounts for 1.57% of federal governments expenditure profile for the period under review. We conclude that there is a significant relationship between federal governments expenditure profile and the value of external loans she obtains. As a matter of fact, federal government depends on external loans in the funding of its expenditure in Nigeria.

4.5.5 HYPOTHESIS FIVE (5)

Ho: Federal government does not depend on internal loans in the funding of its expenditure in Nigeria.

This hypothesis is tested using the output of our above multiple regression analysis, where $t_{calculated} = 54.39 > t_{table}\ 0.01 = 2.878$. With the above result; we reject the null hypothesis and accept the alternative hypothesis.

In addition to the above test, result of table 4.2.3 shows that total internal loans obtained by federal government amounts to N1147096.5 million.

This accounts for 16.02% of federal governments expenditure profile for the period under review.

We conclude that federal government depends on internal loans in the funding of its expenditure in Nigeria.

4.5.6 HYPOTHESIS SIX (6)

Ho: There is no significant relationship between federal governments expenditure and the amount of external grants, she obtains.

This hypothesis is tested using the output of our multiple regression analysis, where

$T_{calculated} = -0.47 < t_{table}\ 0.01 = 2.878$

With this result, we accept the null hypothesis and reject the alternative hypothesis.

To further, corroborate result of the above test, table 4.2.5 shows that external grants accounted for 0.05 % of federal governments expenditure profile for the period under review. This is quite insignicant!

We conclude that there is no significant relationship between federal governments expenditure profile and the amount of external grants that she receives.

The above tests, their results and the decisions taken are summarized in table 4.3 below.

4.6 T – TEST FOR MULTIPLE REGRESSION CONEFICIENT FOR THE VARIOUS VARIABLES.

EXPLANATORY VARIABLES	FED. GOVT INDEPENDENT REVENUE	ALLC. FROM FEDERATION A/C	INTERNAL LOANS	EXTERNAL LOANS	GRANTS	DEDICATED ACCT. FUNDS
REGRESSION COEFICIENT / PARAMETERS	0.652	1.029	0..979	1.241	0.771	0.999
STANDARD EFFORS	0.121	0.007	0.018	0.087	1.639	0.007
T – RATIO CALCULATED	5.39	147 .0	54.39	14.26	- 0.47	142..71

T – RATIO TABLE @ S% LEVEL OF SIGNIFICANCE Z – TAILED TEST	2.101	2.101	2.101	2.101	2.101	2.101
T – RATIO TABLE @ S% LEVEL OF SIGNIFICANCE Z – TAILED TEST **DECISION**	2.878	2.878	2.878	2.878	2.878	2.878
	SIGNIFICANT	**SIGNIFICANT**	**SIGNIFICANT**	**SIGNIFICANT**	**NOT SIGNIFICANT**	**SIGNIFICANT**

TABLE 4.3

4.7 MODEL DEVELOPMENT FOR THE RELATIONSHIP EXISTING BETWEEN VARIOUS COMPONENTS OF FINANCING AND CAPITAL EXPENDITURE PROFILE

The output of the multiple regression analysis is as follows: Regression of sources of financing on capital expenditure

Model Summary[b]

Model	R	R SQUARE	**ADJUSTED R** SQUARE	STD ERROR OF THE ESTIMATE	DURBIN-WATSON
1	990	. 981	.974	24775.3777	2.367

a. Predictors: (constant), x_6, x_2, x_4, $x_{5,}$ x_3, x_1
b. Dependent variable: Y2.

ANOVA

Model	Sum of Squares	Of	Mean square	F	Sig	
Regression	5.274E+11	6	8.790E+10	143.2	$.000_a$	
Residual	1.043E+10	17	613819190			
Total	5.378E+11	23				

a. Predictors (ANSTANT), x_6, x_2, x_4, x_5, x_3, x_1

b. Dependent variable y_2

Coefficients a

Model	Unstandardised Coefficients		Standardized coefficients	T	sig
	B	Std.Error	Beta		
1 (constant)	-714 205	7008.195		-.102	.920
x_1	10.038	1.665	1.261	6.028	.000
x_3	_. 389	1.116	-.682	-3.365	.004
x_3	6515E-02	.191	.031	.340	.738
x_4	3.622	.768	.190	4.716	.000
x_5	-4.280	18.232	-.01	-.235	.817
x_6	.647	.079	.576	8.204	.000

The above result shows that the various source of financing exhibited 99% correlation with capital expenditure of the deferral government. Also 98.1% changes in capital expenditure level are explained by changes in the components of financing put together.

Based on the output of multiple regression analysis, we develop the following model of relationship existing between components of financing and federal governments capital expenditure.

$Y2 = -\ 714.21 + 10.04\ x_1\ -\ 0.39\ x_2 + 0.065\ x_3\ +\ 3.62\ x_4\ -\ 4.3\ x_5\ +\ 0{,}65\ x_6$ ....

Equation 4

Where

x_1 = Federal government independent revenue

x_2 = Allocation from federal account

x_3 = Internal loans

x_4 = External loans

x_5 = Grants

x_6 = Dedicated Accounts/special funds

y_2 = Capital expenditure

Equation 4. Shows that x_1, x_3, x_4, and x_6, (federal independent revenue, internal loans, External Loans and Dedicated accounts) respectively, have direct relationship with capital expenditure while x2, and x_5 i.e. (allocation from federation accounts and grants) respectively indicate an inverse relationship with capital expenditure.

4.8 HYPOTHESIS TESTING

Hypothesis eight (8)

H0: The federal governments capital expenditure has not been significantly financed through internal and external loans, grants and Dedicated accounts/ special funds.

In testing the above hypothesis, the components of financing were tested for significance using the t – statistics.

Explanatory	Federal government independent revenue	Allocation from federation account	Internal loans	External loans	Grants	Dedicated Accounts/special funds
t-calculated	6.03	-3.37	0.34	4.72	-0.24	8.20
t-table	2.878	2.878	2.878	2.878	2.878	2.878

Components x1, x_4, and x_6 i.e. federal government independent revenue, External Loans and dedicated accounts/ special funds were found to be significant at 0.01 level of significant; since the calculated value of 6.03, 4.72 and 8.2 respectively were found to be greater than their corresponding tabulated value of 2.818.

Components x_3, and x_5, i.e. (internal loans and grants with their calculated values at 0.34 and –0.24 respectively, were found to be less than the tabulated value of 2.818 Thus, they are not significant.

To further corroborate the outcome of the above test, the percentage contributions of dedicated accounts/special funds and external loans accounts for about 60 of capital expenditure in Nigeria for the period under review.

We therefore conclude that

1) Federal government's capital expenditure has been significantly financed through federal government independent revenue, dedicated accounts/special funds and external loans.
2) Federal government's capital expenditure has not been significantly financed through internal loans and grants.

4.8.1 **.MODEL DEVELOPMENT FOR THE RELATIONSHIP EXISTING BETWEEN INTERNALLY GENERATED REVENUE, ALLOCATION FROM FEDERATION ACCOUNT AND RECURRENT EXPENDITURE PROFILE OF THE FEDERAL GOVERNMENT.**

MODEL SUMMARY B

Model	R	R square	Adjusted R square	Std error of the estimate	Durbin-Watson
1	.997[a]	.993	.991	24775.3539	2.367

ANOVA [b]

Model	Sum of squares	df	Mean square	F	Sig
1					
Regression	1.576E+12	6	2.627E +11	428.054	1000[a]
Residual	1.043E + 10	17	6138188160		
Total	1.581E + 12	23			

a: predictors: (constant), x_6, x_2, x_4, x_5, x_3, x_1

b: Dependent Variable: y_1

Coefficients

Model	Unstandardized Coefficients		Standardized coefficients	T	Sig
	B	Std. Error	Beta		
(Constant)	-714 194	7008.189		-.102	.920
x_1	-9.038	1.665	-.661	-5.427	.000
x_3	1.389	.116	1.419	12.021	.000
x_3	.935	.191	.256	4.886	.000
x_4	-2.622	.768	-.080	-3.414	.003
x_5	5.280	18.232	.011	.290	.776
x_6	.353	.079	.183	4.479	.000

a: Dependent variable: y_1

The above result shows that the various sources of financing exhibited 99.79. Correlation with recurrent expenditure of the federal government.

Also 99.3% changes in recurrent expenditure level are explained by changes in the components of financing put together.

Based on the output of multiple regression analysis, we develop the following model of relationship existing between components of financing and federal governments, recurrent expenditure.

$y_1 = 714.19 - 9.04\ x_1\ = 1.39\ x_2\ + 0.94\ x_3 - 2.62\ x_4 + 5.28\ x_5 + 0.35\ x_6$……..Eq 4

Equation 4. Shows that $x_{2,}$ $x_{3,}$ x_5 and x_1 (i.e. Allocation from federation accounts, internal Loans, Grants and Dedicated accounts/special funds respectively, have direct relationship with recurrent expenditure while x_1 and x_4 (i.e. Federally sourced independent revenue and external loans indicated an inverse relationship with recurrent expenditure.

HYPOTHESIS TESTING

4.9 HYPOTHESIS NINE (9)

Ho: The recurrent expenditure needs of the federal government have not been significantly financed through federal governments internally generated revenue and allocation from federation account.

Explanatory variables	Federal government internally generated revenue	Allocation from federation account
T – calculated	- 5.43	12.02
T – table	2.878	2.878

In testing the above hypothesis, the components of financing were tested for significance using the t – statistics. Components $x_{2,}$ x_3 and x_6 (i.e. Allocation from federation accounts, internal loans and Dedicated accounts/special funds were found to be significant at 0.01 level of significance since the calculated values of 12.02, 4.89 and 4.48 respectively were found to be higher than the tabulated vale of 2,878.

We therefore conclude that.

(1) The recurrent expenditure needs of the federal government have not been significantly financed through federal government's independent and internally generated revenue.

(2) The recurrent expenditure needs of the federal government have been significantly financed through allocations from federation account, internal loans and dedicated accounts.

4.10 DISCUSSION OF RESULT OF HYPOTHESIS TESTING

In this study. One was able to establish the following facts:

(1) A strong and significant relationship exists between the various components of government financing and her total expenditure profile; except for one variable – external grant received by the federal government.

An attempt at ranking the contributions of various components Into federal government expenditure profile provides the following expressions

Source of financing	Level of significance	Percentage	Ranking
Allocation from federation account	T cal = 147.0 T table = 2.88	52.21%	1st
Dedicated account/special funds	T cal = 147.0 Ttable = 2.88	23.02%	2nd
Internal loans	T cal = 54.39 T table = 2.88	16.02%	3rd
Federal government independent revenue	T cal = 5.4 T table 2.88	4.13%	4th
External loans	T cal = 14.26 T table = 2.88	1.57%	5th
Grants	T cal = 0.47 T table = 2.88	0.05%	6th

The above table reveals that the allocations from, federation account maintained a 55.21% lead. This is followed by inputs from dedicated accounts/special funds at 23.02%.

Revenue sourced from internal loans stood at 16.02% for the period under review and is ranked 3rd while independent revenue generated by federal government occupied the 4th position with an input of 4.13%. External loans maintained a 1.57% contribution and is ranked 5th. At the rear are proceeds from external grants received by the federal government. This accounted for 0.05% of total expenditure profile of federal government of Nigeria for the period under review. This variable has proved not to be a reliable/ significant source of finance for execution of federal government's expenditure.

(2) Federal governments capital expenditure has been significantly financed through external loans, federal government independent revenue and dedicated accounts/special funds. Internal loans and grants received did not make appreciable impact in the execution of capital expenditure.

This result is consistent with already established belief that external loans and earmarked special funds should go into capital projects, which will enhanced productivity and ensure a better future.

(3) The recurrent expenditure needs of the federal government have been significantly financed through allocations from federation accounts, internal loans, and dedicated accounts. Federal government's independent/internally generated revenue did not make an appreciable impact on the execution of recurrent expenditure.

The use of allocation from federation account in the funding of recurrent expenditure seems to be in order. Again inflows from dedicated account/special funds split partly into capital and recurrent expenditure appears to be in order too. But, the usage of internal loans in the execution of recurrent expenditure is inconsistent with already established beliefs.

(4) Furthermore, accruals into federal government coffers that are devoid of loans and grants amounts to N5898549.3 million. This could not have been enough to accomplish the total expenditure profile of N7161914.0 million.

Without Loans (internal and external) and other external inflows, the federal government of Nigeria would not be said to have enough funds to execute her projects. In other words, federal government of Nigeria does not generate enough internal revenue.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

This concluding chapter of this study presents the summary, conclusion and recommendations made there of, based on the findings of the study.

5.1 SUMMARY

On the basis of the results of analysis carried out in chapter four, the researcher in concluding, summarizes his findings on the individual sources of finance for federal government expenditure in Nigeria.

5.1.1 FEDERAL GOVERNMENT INDEPENDENT REVENUE

From the study, the researcher found out that this source of finance contributed 4.13% towards the total expenditure profile of federal government, for the period under review. The t-calculated was higher that the t-tabulated. Though it was affirmed that federal government depends on this variable in funding its expenditure; the dependency ratio is quite low.

5.1.2 **ALLOCATION FROM FEDERATION ACCOUNT**

The percentage contribution of this component stood at 52.21%, indicating that this source of financing is the major source for financing of federal government expenditure in Nigeria. It's t-calculated was far higher than the t-tabulated; hence it has been confirmed that there is a significant relationship between federal government's expenditure and the allocation from federation account.

5.1.3 **DEDICATED ACCOUNTS / SPECIAL FUNDS**

This extra – budgetary fund contributed 23.02% of funds towards federal government expenditure profile. Value of it's t-calculated was greater than t-tabulated thus, it was proved that federal government depended on dedicated accounts / special funds in the funding of her expenditure profile.

5.1.4 EXTERNAL LOANS

The percentage contribution of this component stood at 1.57%. It was thus confirmed that the federal government depends too, on external loans in the funding of its expenditure.

5.1.5 INTERNAL LOANS

The researcher found out that this source of finance contributed 16.02% to total expenditure profile of federal government for the period under review. It's t-calculated was greater than t-tabulated. It was adjudged that federal government depends on internal loans in funding its expenditure.

5.1.6 GRANTS

The percentage contribution of this component stood at 0.05%. Value of its t-calculated was less than that of the t-tabulated; this indicates that there is no significant relationship between grants received by federal government and her expenditure profile.

5.1.7 FUNDS AVAILABLE TO FEDERAL GOVERNMENT

The percentage contribution of accruals into federal government accounts, (devoid of loans) to total expenditure stood at 82.36%. This simply means that the federal government would not be said to have enough funds to execute her projects, as she had to borrow the outstanding balance of 17.64% to make up for the deficit. Put in another way, the federal government may need to prune down her expense profile to be in tandem with her limited resources.

5.1.8 FINANCING OF CAPITAL EXPENDITURE

The researcher found that the capital expenditure of federal government has been significantly financed through external loans, federal government independent revenue and dedicated accounts / special funds. This result is in consonance with already established belief.

5.1.9 FINANCING OF RECURRENT EXPENDITURE

The recurrent expenditure needs of the federal government has been significantly financed through allocations from federation account, internal loans, and dedicated accounts / special funds.

The usage of internal loans in the execution of recurrent expenditure is inconsistent with already established beliefs. Federal government independent revenue, ought to come to rescue.

5.2 CONCLUSION

On the basis of the above-summarized findings, we finally conclude this work by making the following recommendations.

5.3 RECOMMENDATIONS

Since the act of governance is an on-going process, funds will always be the needed to run a government. It is clear from the forgoing analysis of federal governments revenue and expenditure pattern in Nigeria, that changes must occur in the revenue structure in order to significantly enhance the effectiveness of fiscal policy instruments and to achieve set goals and objectives. This, the federal government can do by:

(1). Working on her potentially exportable commodities. There is a need to look inwards, for the production / processing of commodities that are needed elsewhere in the larger world. The new initiative on cassava production for export is a move in the right direction.

(2). Changing the revenue structure to concentrate more on domestic value added production activities in order to ensure robustness and sustainability. From the viewpoint of real economic growth, it is not just distinguishing between oil and non-oil revenue.

(3). Making projections for a long-term stability of the Nigeria federation. The inter tier distribution of jurisdiction over revenue sources urgently requires major adjustment in favor of the states and local governments in order to moderate the dominance of the revenue structure by the federal government.

(4). Reducing her over dependence on allocation from federation account. The federal government is as guilty as the other tiers of government on this phenomenon. She should intensify efforts at independent generation of revenue on matters that falls within her exclusive preserve.

(5). Effecting a change on it's revenue structure. This must become significantly based on domestic production activities, in contrast to the ages long dependence on export of primary commodities (Be they agricultural commodities or crude oil).

Other changes that need to be put in place includes:

(6). The nation stands to gain if the federal government can eliminate oil revenue leakages. Accounting for proceeds from oil revenue should be thorough and validly transparent.

(7). In the interim, increased production of petroleum product is recommended, since the wealth of the nation is hinged on this mono product. This is subject to production quota from the oil cartel - OPEC. Exploration and exploitation of new oil blocks should be encouraged too.

(8). Our value added tax base needs to be broadened. Again, the efficiency of its collection should be worked upon.

(9). Our present oil windfall and revenues from divestments from public institutions should be used in repaying our debt obligations to creditors and to clear outstanding liabilities to contractors.

(10). Tax and tariff exemptions should be eliminated.

(11). The federal government should put more programs on self-financing basis through cost recovery measures, such as user fees.

Next, let us take a critical look at the other side of the coin:

Three interrelated tasks face the federal government as she plans, budgets and implements her expenditure decisions. She must control the overall level of expenditure, set priorities for it's allocation and ensure quality within each expenditure category. This calls for fiscal planning whose primary goals should be to forecast and program public expenditure over a 3-5 years period and to take into account both likely resource constraints and the linkages of such spending within the economy. Federal government of Nigeria should improve public expenditure management through:

(1). Rehabilitation of the basic accounting system such that the correct and timely recording of expenditures as they occur, becomes an integral part of proper fiscal control. This may involve the preparation of simple standardized project profiles for tracking project expenditure.

(2). Effective coordination of budgeting decisions among the many but dispersed institutions involved.

(3). Assessment and projection of the macroeconomic outlook for the coming 3-5 years is very useful for estimating available financial resources.

(4). The preparation and updating of public investment program should be taken as a matter of screening such that projects are accepted on the condition that they meet satisfactory appraisal criteria at appropriate stages in the life cycle.

(5). Setting priorities and developing contingency plans for unexpected shortfall should be a part of fiscal planning and expenditure management such that "core" programs will receive funding when resources fall while others will receive funds only when additional funds become available and

(6). Speedy implementation of a comprehensive and consolidated federal budget with it's budget implementation / monitoring component, and thus making no room for extra – budgeting expenditures.

(7). There is a need to reform the budget process. This process effectively collapsed in the early 90's. The lack of commitment over expenditure controls in recent years has made the budget ineffective as a tool for economic stabilization or development. Federal governments policies addressing the desired level of spending in total, in a specific ministry, or in a specifics sector have been totally ineffective given the lack of adequate controls, checks and balances and accountability. Immediate and sustained corrective actions are required for effective fiscal management and for the provision of essential government services to Nigeria's population.

(8). Macro economic projections should guide the overall level of expenditure. As such, these projections need to be more realistic, internally consistent and based on more accurate and timely information. Sectoral strategies should be affordable and should include measurable targets in terms of level and quality services to be provided.

(9). In the current reforms going on in the public sectors, increased transparency should be vigorously pursued.

(10). There is a need to integrate all sources of extra-budgetary revenue and financing into the approved budgeting under the full control of the federal ministry of finance and the Accountant general of the federation for allocation to the ministries, subject to all financial guidelines and direct audit by the auditor general of the federation.

(11). Authority to incur expenditure should be limited to the budgeted amount for the contingency funds.

(12). Federal governments spending should not exceed the approved budget without a supplementary budget financed from the implementation of new revenue measures.

(13). Comprehensive budget for the federation account as well as for the federal government of Nigeria which includes the planned and actual level and uses of all revenues, all borrowing, including borrowing from the state and local governments as well as from the special funds and all expenditures should be published regularly.

(14). The Auditor general of the federation should be empowered to review all details of transactions in all federal government controlled accounts.

(15). Budget allocations need to match stated or perceived priorities. The federal government should:

(i). Identify projects which could be handled by the private sectors in order to avoid unnecessary government expenditure. The private sector should operate such projects.

(ii). Reject projects which compete with the private sector or which do not support private sector initiative and development.

(iii). Choose the least cost alternative for accomplishing social goals.

(iv). Emphasize maintenance of assets over the rehabilitation or replacement of damaged assets.

(v). De – emphasize project completion status. Emphasis should be on qualitative output as poorly designed project is a waste; no matter how far it has been accomplished.

(16). Federal government needs a majority private sector equity stake in most public enterprises. She should divest fully from public enterprises as they are better managed by the private sector.

(17). Lastly, the federal government should provide an enabling environment by:

- Encouraging business stability
- Achieving price stability
- Liberalizing interest rate
- Encouraging private sector development
- Reducing direct government provision of services
- And concentrating on the regulatory role of government.

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