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Federalism: Conceptual and Theoretical Issues

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Abstract

This paper addressed the conceptual and theoretical issues regarding the essence of federalism, and sought to investigate the presence of actionable federalism in the Nigerian political structure. A federal form of government is one with a multi-order structure with all orders of government having some independent as well as shared decision-making responsibilities. The main idea behind a federation is the acceptance of the view that a decentralized government functions better and tends to produce better social and economic results than totally centralized ones. However, the practice of federalism in Nigeria has been lopsided and the expected benefits (fast and steady economic growth and development) associated with fiscal federalism has been elusive. It was, therefore, recommend that Nigeria should adopt and practice true federalism in which constituent governments are given power in the constitution to generate and manage their resources for even development of their areas. This will forestall agitations for resource control. Also, Nigeria should put in place fair, unbiased and transparent electoral process and institutions for the functioning of true democracy where power absolutely rests on the electorates;

1. Introduction

Federalism has been a hotly debated and controversial concept especially in the fields of public finance and political economy. The reason for this controversy, as argued by Elazar (1980) is that there exist variations of political arrangements to which the term applies. As controversial as the term is, and as varied as its applications are, scholarly attempts have been made to give it a definitional direction. The term *federalism,* according to Elazar (1980) is a derivative of the Latin word *foedus* meaning league, treaty or compact. The term federal pertains to a form of government in which certain states agree by compact to grant control of common affairs to central authority but retain individual control over internal affairs (Webster's, 2010). The term federalism, *ipso facto,* can be conceptualized as a mode of political organization that units separate states or other polities within overarching political system in such a way as to allow each to maintain its own fundamental political integrity. In the federal system, the requirement is that the basic policies be made and implemented through negotiation, so that all the members can share in making and executing decisions.

2. Objectives:

This paper sought to address the conceptual and theoretical issues regarding the essence of federalism, and to investigate how actionable federalism is in the Nigerian political structure.

3. Conceptual Framework

Constitutionally, power among various orders of government can be classified into unitary, federal and confederal. In the unitary system of government all powers and authorities for the exercise of the functions of running a state are concentrated in the hands of a single central government. In this respect, powers are not shared between the central government and any other component units. Under this system, the constitution deposits all the powers of governance with the central government. However, the central government can delegate powers to the component units created by it. These powers are exercised in line with the wishes of the central government. This system facilitates centralized decision making to foster national unity and places emphasis on coherence and quality of access to public service (Shah, 2007).

A federal form of government is one in which there is constitutional division of powers among different levels or tiers of government. In a federal system, the federal or central authority represents the whole and acts on behalf of all in certain matters especially defense, external affairs, currency, national revenue, etc. A federal form of government is one with a multi-order structure with all orders of government having some independent as well as shared decision-making responsibilities. As argued by Shah (2007) federalism represents a coming together of constituent geographic units to take the advantage of greatness and smallness of nations in a globalized world. Most modern states come about as a result of unification of separate jurisdictions to form a federation on arrangement which according to Musgrave and Musgrave (2010) may be a reflection of historical forces of nation building, wars and geography. Alternatively, 'holding together' view of federalism or what is now known as new federalism represents an attempt to decentralize responsibilities to state-local orders of government with a view to overcoming regional and local discontents with central policies. This view is the driving force behind the current interest in principle of federalism in unitary countries and in relatively newer federations as well as emerging federations (Shah, 2007). In federal countries, two models are appropriate and a country either conforms to one of the two or both. The two models are dual federalism and cooperative federalism. In dual federalism both the federal and state governments have separate and distinct responsibilities. The system of dual federalism according to Riker (1969) is characterized by rulership of the land and people by two levels of government. The approach in dual federalism may either be layer cake or coordinate authority. In the layer cake approach, there is a unitary type of relationship among the various orders of government. The national government is at the apex and it has the option to deal with the local governments either directly or through the state governments. Local governments are not recognized as having any constitutional status, rather they are viewed as being the extension of the state, and derive their power from the state government. This approach fits the type of federation in Mexico, Russia and Malaysia. In coordinate-authority model of dual-federalism, states enjoy significant autonomy from the federal government, and the local governments are viewed simply as handmaidens of the state and have little or no direct relationship with the federal government. This model fits the type of federation in USA, Australia, Canada, India and Pakistan.

In cooperative federalism, the responsibilities of various levels of government are mostly interlinked. In this model, as in the dual federalism model, fiscal tiers are organized so that the national and state governments have independent authority in their areas of authority and act as equal partners. Like dual federalism, cooperative federalism is based on three approaches; interdependent spheres, marble cake and independent spheres. In interdependent spheres, there is a combination of unitary structure with federal features. The federal government determines policy, while the state and local governments act as implementation agents for federally determined policies. In view of the supremacy of central government in policy making in this model, the state and the local governments make their contributions to federal policy making through the upper house of parliament or second chamber as obtainable in the republic of Germany or the council of the provinces in South Africa.

In the marble cake model of cooperative federalism various levels of government have overlapping and shared responsibilities and all constituent governments are treated as equal partners in the federation. Republic of Belgium is a good example of federation with this model. Cooperative federalism with independent sphere of government is an approach in which all levels of government enjoy autonomous and equal status and coordinate their policies horizontally and vertically. Brazil is a federation with this type of model.

The argument for this system of government is that it will create leaner and more efficient government that would be more responsible and accountable to people. It should be admitted however, that while this may be true in some instances, it may fail to hold substance in some others. The reason for this is that countries with federal system of government tend to vary considerably in terms of federal influence on sub national governments. While this influence is very strong in some federations, moderately strong in some and very weak in others, the central government could use conditional grants to influence the priorities of the state and local government.

Conditional grant or transfer from a federal body to a province or other territories involves a certain set of conditions. If the lower level of government is to receive this type of transfer, it must agree to the spending instructions of the federal government. Jha (2012) argued that conditional transfer may consist of matching transfers; non-matching transfer for specific purposes; and block transfers.

In the case of conditional transfer, the federal government specifies the purposes for which the recipient sub-national government can use the funds. Such transfers are often used to address concerns that are highly important to the federal government such as project with inter-regional spill-over effects but which might be considered less so by the sub-national government

The influence of sub national governments on national policies could also create variation among federal states. In Australia and Canada for example, a clear separation of national and sub-national institutions exists and the two levels interact through meetings of officials and ministers. Also, in Germany and in South Africa, state and provincial government have a direct voice in national institution. And in the United States, regional and local coalition play vital role in the congress. Consequently, in some federations, constitutional provision give room for all legislation to recognize that power rests with the people and major legislative changes are affected through a referendum. Yet, in almost all the federations of the world, the influence of local government on the state and federal remain irrelevant and weak (Shah, 2007).

Asymmetric federalism connotes the idea of treating unequal unequally. What this implies is that federal government may be flexible in accommodating the special needs of constituent units but at the same time imposes a federal will in certain institutions. Watts (1999) concerning this type of arrangement stated that some federation offer constituent units freedom of choice to be unequal or more equal than others through opting-in and opting-out of federal arrangements.

Market preserving federalism put forward as an ideal form of federal system by Weingast (2006) stipulated that multiple government have clearly delineated responsibilities; sub-national government have primary authority over public goods and services for local autonomy; the federal government preserves the internal common marker; all governments face the financial consequences of their decisions and political authority is institutionalized.

According to proponents of this theory, government is assumed to be inherently benevolent and that there is no natural reason for political officials to further the interest of citizens. They argue further that if given opportunity, government officials will work for maximizing their own interest rather than serving the interest of the citizens. Contrary to the principles of equity and efficiency preached in public finance literature and in support of the public choice theory, market preserving federalism interprets federalism primarily as a way of imposing discipline on self-serving politicians and government and attacks the abuse of power and growth of public sector. The growth of public sector due to centralization of tax responsibilities has prevented multi-level government to compete with each other vertically or horizontally. Lack of competition it is believed leads to inefficiency. Proponents of market preserving federalism argue that the allocation of tax and expenditure responsibilities among different levels of government in a country should be so done that it would lead to a maximum degree of competition among governments. Competition among sub-national governments, it is believed, forces government to represent the interest of the citizens and preserve markets. The theory further suggests that besides efficiency, inter-jurisdictional competition serve as a disciplining device to punish inappropriate market intervention by lower government officials. Thus, the emphasis of market preserving federalism is on the natural process of equalization through competition and that political decentralization in terms of fiscal capacity to sustain a productive and growing market economy is the basis of state power (Jha, 2012; Weingast, 2006).

Pure or classical federalism is a federal system of government in which communities accept to work together nationally on a limited number of issues and for those issues only, and at the same time, are determined to preserve their separate identities and to remain the competent authority in their own territories for the regulation of other matters (Agiobenebo, 2003). Under this concept, federalism is considered as a consequence of the practical necessity of engaging in experimentation and innovation towards the achievement of a convenient, perhaps functional arrangement among the constituent communities.

Confederation, as a constitutionalized power, is the linking together of sovereign independent states in which each component unit is free to carry out all governmental functions (Agiobeneo, 2003). In a confederal state, the general government serves as the agent of the member units usually without independent taxing and spending powers (Shah, 2007) In this arrangement there is a linking together of sovereign states by treaty for particular purposes while internal sovereignty is preserved and external sovereignty is limited to only a very minor degree for component states. Here, emphasis is on the plurality rather than the unity of the numbers of the confederations. The assignment principle in such a system is to allocate to the union government only matters of confederal interest such as international spillover effects among union numbers. Examples of a confederal system are; UNO, OAU, ECOWAS and EU etc.

4. Fiscal Federalism

An aspect of federalism that has generated much interest and controversies in recent time is fiscal federalism. Jha (2012) argued that until the early 1990s, fiscal federalism was a largely unexplored area of fiscal policy. This is because the role of public finances as enunciated by classical economists was to raise sufficient revenue centrally and ensure transfer of such funds for addressing the problem of vertical and horizontal imbalance (Uko, 2015). However, economic globalization occasioned by domestic regional pressure brought about by the process of economic liberalization has brought about increasing interest in fiscal federalism. In addition, growing interest in fiscal federalism has been linked principally to growing dissatisfaction with the role of public sector which gives expanding role of income maintenance, income redistribution and economic stabilization to the federal government. In view of this dissatisfaction the neo-liberal economists started questioning the effectiveness of such system and agitated that greater reliance should be placed on the market and less power should remain in the hands of federal government. By questioning the effectiveness of the role of federal government in improving the distribution of income and in stabilizing the economy for the purpose of reducing poverty and unemployment, some neo-liberal economists have in essence undermined the legitimacy of federal government's overwhelming role and have taken a position in favour of reducing the size of the public sector while giving more powers to both market and sub-national level governments (Buchannan, 1995). Thus, in terms of efficient resource allocation, various arguments have been advanced in support of fiscal federalism as a machinery for understanding: (i) the factors determining the optimal degree of fiscal decentralization (ii) principles underlying the assignment of functions and sources of finance of government of different levels and (iii) the design of suitable inter-governmental transfer scheme to fulfill the objectives of equity and efficiency (Rao and Singh, 2005).

Apparently, fiscal federalism has been viewed as the devolution of fiscal responsibilities among federating units, the purpose of which is to ensure free choice of preferences and enhance easy allocation of resources to priority areas within the jurisdiction of each federating unit (Alad, Rapu and Tule (2003). For effective functioning of federalism, Akpakpan (2003) suggested that:

i. There must be people at the local level who are able to perform the functions of government.
ii. There must be appropriate procedures for forming the government and for selecting the people who will serve especially at the local level.
iii. There must be proper and adequate funding of government at the local government.

These suggestions informed why decentralization is believed to promote healthy competition among different tiers of government thereby promoting economic growth. Ekpo (2003) alluding to federalism cum growth nexus argued that the principal idea behind a federation is the acceptance of the view that decentralized governmental functions tend to produce better social and economic result than totally central ones. On this note, fiscal federalism is expected to bring faster economic growth and development than centralized fiscal operation would.

The debate for decentralization as the basis for faster economic growth and development has generated a lot of interesting relational and fiscal issues. Agiobenebo (2003) argued that decentralized system of government gives rise to a set of fiscal exigencies one of which is fiscal federalism. On the basis of this he described fiscal federalism as the miscellany of financial arrangement and relations among tiers and units of government that are driven by development in the fiscal constitution, itself acting more or less in harmony with development in political and economic activities of a nation state. We can deduce from this description that fiscal federalism is a financial arrangement among federating units in a federation, and that this arrangement is supported by the constitution for the purpose of promoting economic and political stability in the system. Furthermore, we can view fiscal federalism as an arrangement which subsists between different tiers of government within a federation to pool their resources together with a view to allocating such pooled resources among the federating units in proportion to agreed constitutional principles giving regard to the needs and preferences of the federating units in order to ensure oneness of purpose and for even development and unity in disparity. From this description of federalism, it is obvious that government at any level within a federation has the role of allocating and distributing resources so as to ensure overall stability of the system. Responsibility of allocating and distributing resources can be handled by any of the federating units based on their taxing power and assigned responsibility.

However, Musgrave and Musgrave (2010) suggested that macroeconomic stability and income distribution functions should come under the jurisdiction of the central government, while the allocation function should be shared among the lower level of government that make up the federation. Ubokudom and Ndiyo (2003) on this note argued that spending and taxing decisions that substantially affect the level of unemployment and inflation should be reserved for the federal government because no state or local government is financially strong and large enough to influence the overall level of economic activity. Stigler (1998) suggested that functional role of government work best the closer the government is to the people and that irrespective of the level of government which provides what people should be given the right to vote for the amount and type of provision they want belongs to the people. This means that decision making should occur at the order of government closest to the people and consistent with allocation efficiency. This argument leads us to examining various theories of fiscal federalism and how their application could bring about efficient and equitable distribution of public choice.

Theories of Fiscal Federalism

Theories of fiscal federalism can be discussed on two generational bases – first generation theory and second-generation theory. The first-generation theory of fiscal federalism also known as classical normative theory of fiscal federalism was spearheaded by Tiebout (1956), supported by Oates (1972) and Musgrave and Musgrave (2010). The theory states that the federal government should have basic responsibilities for the macroeconomic stabilization and income redistribution. This is because federal government possesses a far greater capability to maintain high levels of employment with stable prices than a sub-national government. One of the first-generation theories – the *'decentralization theorem'* put forward by Tiebout (1956) and supported by Oates (1972) stated that "Each public service should be provided by the jurisdiction having control over the minimum geographical area that would internalize benefits and costs of such provision".

The practical implication of this theorem according to Shah (2007) is that it requires a large number of overlapping jurisdictions. On the basis of this Frey and Eichenberger (1999) argued that jurisdiction can be organized along functional lines while overlapping geographically and that individuals and communities could be free to choose among competing jurisdictions.

Thus, decentralization according to Oates (1972) is justified on the bases that:

i. Provision of public goods and services by federal government leads to uniform level of consumption and utilization of goods and services respectively across all regions. Such uniformity, it is argued, may result in inefficiencies. But decentralized provision allows government to cater better for the tastes and needs of local residents.

ii. Welfare gains in case of decentralized provision of goods and services enhance consumer mobility. Citizens vote, to some extent, select a place of residence that provides a fiscal package that suites their preferences.

iii. Decentralization may result in greater experimentation and innovation in production of public goods and services. Availability of large number of independent producers of public goods will in the long run promise greater progress in the volumes of production of such goods and services.

iv. Inter-jurisdictional competition as a result of decentralization may also lead to efficiency in the provision of public goods and services.

v. Decentralization of allocation functions may lead to more efficient levels of public output because expenditure decisions are tied more closely to real resource cost.

From the forgoing, it can be deduced that classical normative theory of fiscal federalism strongly supports decentralization on the grounds of efficiency, accountability, manageability and autonomy principles.

It should be noted that emphasis of the theory is on expenditure decentralization while favouring revenue centralization. The theoretical argument for this arrangement is that if tax responsibility is decentralized, lower level government will engage in stiff competition to such an extent that capital and labour would be taxed and the whole exercise will be self-defeating resulting in low tax yield and under provision of public goods and services.

From this argument, it is apparent that the distribution of financial resources among tiers of government will not correspond to the distribution of expenditure responsibilities. Because while the federal government has more taxing power but comparatively less expenditure responsibilities, sub-national governments have fewer taxing authorities but more expenditure functions to perform. This in consequence contributes to what Sharma (2011) refers to as vertical fiscal imbalance (VFI).

The second-generation theory of fiscal federalism is an emerging theory which favours the decentralization of both expenditure and revenue responsibilities and gives minimal role to revenue sharing and intergovernmental transfers. Furthermore, the theory posits that inter-jurisdictional competitions, a common market and hard budget constraints may provide protection against infringements to market operations (Jha, 2012). Proponents of second-generation theory of fiscal federalism are Buchanan (1995), Weingast (2006), Inman and Rubinfield (1997). Prominent among the second-generation theories are; public choice theory and market preserving federalism.

Public choice theory takes a radically different view about government. It regards politicians as rent seeking individuals using their positions to pursue private goals, and government as institutions that encroach upon individual freedom and seek to increase their hold on the private economy as much as possible. According to this theory, government is a leviathan, and that there must be institutional rules and arrangements to force politicians to serve the public interest in the pursuit of their own goals and limit their discretionary power (Buchaanan, 1995). Inman and Rubinfield (1997) argued that such a complex positive theory of how the public expenditure programmes and budgeting should be carried out introduces a range of inefficiencies. The theory approaches the problems of fiscal federalism with the assumption of a malevolent government. Scholars of market preserving federalism build on the works of public choice theories but differ in their consideration of government as malevolent or inherently benevolent. Their theory is influenced by the theory of firm which studies a wide range of incentive problems that plague firm working under the assumption that no reason compels managers to favour shareholders. As in the theory of firm scholars in support of market preserving federalism also assume that there is no natural reason for political officials to further the interest of citizens (Qian and Weingast, 1997).

The new theory appears to favour efficiency considerations over equity. Its principal proponent, Weingast (1995) observed that;

A fundamental political dilemma of an economic system is that: A government strong enough to protect the property of right and enforce contracts is also strong enough to confiscate the wealth of its citizens. Thriving markets require not only the appropriate system of property rights and a law of contracts, but a secure political foundation that limits the ability of the state to confiscate wealth. To Weingast, the main attraction of federalism is its potentials for providing a political system that can limit the ability of the federal government to confiscate wealth of sub-national government while supporting an efficient system of markets. A federal system according to Weingast (1995) is market-preserving if the primary responsibility for regulatory and economic development policies remain with the sub-national government, common market is enforced; and sub-national governments have no access to money creation or to central government bail-outs for local projects or excessive debts.

In summary, market-preserving federation is concerned about the ill-effect of the growth of public sector as a consequence of centralization of responsibilities. Competition is the crux of the new approach. It favours common markets which imply that there is no restriction over the mobility of goods across a country. It demands that local government should be responsible for all policies of economic regulation and development while the federal government is responsible for developing a federal constitution to guide free and open markets.

Application of Federalism to Nigeria's Federation

Nigeria's federalism as argued by Agiobenebo (2003) is the creation of the British starting with the declaration of the Island of Lagos as British Colony in 1861 and culminating in 1885 when European powers met in Berlin and shared the entire African continent among themselves.

Nigeria's fiscal federalism allows some form of decentralization which gives rise to two inter-governmental fiscal relations namely; vertical and horizontal fiscal arrangement. In the vertical arrangement, revenue available to the federation account is shared among the three tiers of government mostly on monthly basis in the sharing formula of 52.68%, 26.72% and 20.6% at present for the federal, state and local government, respectively. Horizontal fiscal arrangement involves the use of certain principles such as; derivation, equality, population, terrain and landmass in determining share of each federating unit from the federation account. Lasisi (2003) posited that the fiscal relationship revolves around expenditure and revenue matters and fiscal federalism connotes revenue and expenditure decentralization. Uwatt and Umoh (2003) remarked that fiscal federalism consists of three elements, namely; the assignment of responsibilities and functions to the different tier of government, the assignment of tax powers, and the allocation of centrally collected revenue to the various tiers of government.

The aforementioned three elements of fiscal federalism have constitutional backings and are expected to contribute to overall economic and political stability of the polity besides contributing to economic growth and development. In the first element, each tier of government has functions and responsibilities assigned to it in line with its taxing ability. For example, item in the exclusive legislative list is the exclusive reserve of the federal government. Items in the concurrent list are shared between the state government and the federal government. While residual legislative list contains items shared between the state and the local government.

On the taxing power, the central government decides based on the constitution the tax jurisdiction of each tier of government. For federal government, taxing sources are companies' income tax, petroleum profit tax, value added tax, education tax, capital gains tax on companies, stamp duties on companies, personal income tax of military personnel and residents of federal capital territory, mining rent and royalties, custom and excise duties and miscellaneous revenues. For state government, the taxing sources include personal income tax of state's residents, stamp duties, road taxes, betting and gaming taxes, development levy, street name registration fees, rents on property.

For local government, tax sources are shops and kiosk rates, liquor license fees, slaughter slab fees, marriage, birth and death registration fees, markets / motor park fees, canoes, truck, wheel barrow and cart fees, among others.

A point of interest from these revenue-source allocations is that juicy tax sources are allocated to the federal government leaving less attractive sources to lower level governments. This arrangement has resulted in low internally generated revenue of the lower level governments and eventually increases the dependency rate of lower level governments on the central government.

Revenue allocation among the three tiers of government in Nigeria has continued to spark serious debate. Prior to and after the country's independence in the 1960, Udoh (2003) remarked that as many as thirteen different attempts have been made at devising an acceptable revenue allocation formula for the country. Each of these attempts is remembered for controversies it generated rather than issues settled. The current vertical allocation formula of 52.68%, 26.72% and 20, 60% for federal, states and local governments, respectively is considered inadequate, and pressure had been mounting since 2009 for a new vertical allocation formula of 53.69%, 31.01% and 15.3% for federal, states and local governments, respectively (Obiechina, 2010).

The inter-fiscal relations in Nigeria's fiscal federalism indicate that there is some degree of imbalances in the operation which often results in macroeconomic instability in the system. Thus, it is pertinent to examine Nigeria's fiscal federalism in line with earlier discussed theories of fiscal federalism. Should classical normative theory of fiscal federalism be adopted in the operation of Nigeria's fiscal federalism or should market preserving federalism be adopted? Whichever approach is desired, we should look at the overall impact of it on the generality of the populace and not just on some sections of the economy. The classical normative theory views federal government as benevolent and that it will do anything to counter market failure. On the other hand, market-preserving federalism theory suggests imposition of hard budget constraint on sub-national government. The two approaches sound plausible from the theoretical standpoint; however, what is envisioned in practice is often different from abstract theoretical postulations. What is noticed overtime is that inter-governmental fiscal relations are subject to political bargaining and compromise by different government and political forces in the federation. Thus, transfer can be made for vested political gains such as to stay in power and resources may be transferred to jurisdictions that do not really need them simply to keep some economically non-viable sub-national governments alive in power for purely political reasons (Bird and Smart, 2002).

5. Conclusion and Recommendations

It should be admitted that no simple uniform pattern of transfer is universally appropriate. Yet, if services are to be efficiently provided, transfer must be designed in such a way that those receiving the services have a clear mandate, adequate resource, sufficient flexibility to make decisions, and are accountable for results. The practice of federalism in Nigeria has been lopsided and the prospect of growth and development as the consequence of fiscal federalism has been elusive. The suggestion, therefore, is that potentials for fiscal decentralization as the basis for improving economic and political performance must be evaluated in terms of the specific circumstances of the country in question.

It is recommended that Nigeria should adopt true fiscal federalism in which constituent governments are given power in the constitution to generate and manage their resources for even development of their areas. This will forestall agitations for resource control. The country should also put in place fair, unbiased and transparent electoral process and institutions for the functioning of true democracy where power absolutely rests on the electorates.

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