Mobilizing Subnational Resources in Nigeria's South-East Zone: The Case of Imo State

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Abstract

Most of Nigeria's 36 states are dependent on the Federal Government for the bulk of their revenue. This is an aberration as they are supposed to meet their fiscal obligations from Internally Generated Revenue (IGR), augmented by funds from the Federation Account Allocation Committee (FAAC). Revenue from FAAC, which was supposed to be secondary, has become the mainstay of most states. Only a handful of them come close to meeting their financial obligations from IGR, casting a shadow of insolvency across the states. With the recent pandemic, the Russian invasion of Ukraine and its disruptions in the global economy, FAAC has dwindled significantly, compelling Nigeria and her subnational to look inwards towards sustainability. This study uses the descriptive data analysis method to examine the revenue performance of states in Nigeria's southeast, to advance strategies for increased IGR mobilization. It was found that on average, IGR was only 22 per cent of the total revenue of the states, based on 2018 revenue data. Ebonyi state had the lowest IGR contribution to total revenue at 12 per cent, while Enugu led at 29 per cent. Imo had the highest IGR Cumulative Average Growth Rate over the ten years to 2018 but was the most indebted. The poor IGR outcome is linked to weak revenue mobilization capacity, narrow tax net, rampant revenue leakages due to corruption and low technology application. Tax law reform and the use of technology are among the key recommendations along with fiscal management capacity building.

Key Words: Internally Generated Revenue, Subnational Governments, Debt Service H71, H72, H74.

Introduction

Nigeria has thirty-six states and a federal capital territory, which is often considered its thirty-seventh state. These thirty-six states are grouped under six geopolitical zones, three of which zones are in each of the northern and southern regions of the country. The geopolitical zones are North-Central, North-East, North-West, South-West, South-East and South-South. Although not constitutionally recognized, the zones have come to be accepted as adequately grouping the country into components with the closest sociocultural identity and commonalities, as well as an objective criterion for equitable distribution of power, enhancement of national unity and grassroots development. Many believe that the geopolitical zones provide a much better administrative structure, both for the regions and for interaction between the federal government and the federating units than the present structure whereby the federal government interacts with states individually. The regions have their disparities in resources endowment and contribution to the federal coffer. While the northern region is predominantly agrarian-based, the southern region hosts crude oil, which is the main source of Nigeria's foreign earnings.

The oil sector, complemented by some non-oil exports, continues to provide the mainstay of the Nigerian economy. Since the end of the civil war in 1970, oil has continued to play a pivotal role in Nigeria's revenue history, accounting for about 40 per cent of the country's GDP, 70 per cent of budget revenues, and 95 per cent of foreign exchange earnings, over the past several decades. In 2019, the export of oil and related mineral fuels accounted for 80 per cent of export values, worth over $47 billion (World Bank, 2020). The ownership of mineral resources in Nigeria is vested in the federal government. Thus, revenue from oil and other minerals is also vested in the federal government. These and other revenues,
including the Value Added Tax (VAT) is collected in a pool and distributed among the federal, state and local governments under the revenue sharing formula prescribed by the Constitution. In addition, thirteen per cent of petroleum revenue is paid to oil-producing states as a derivation fund. Indeed, Nigerian governments at all levels, federal, state and local government, rely very heavily on oil revenue to fund their perennial budget deficits. The states and the federal government meet every month in the capital Abuja, at the Federal Accounts Allocation Committee (FAAC) meeting, to share and collect their portions of oil and other elements of Federally Collected Revenue. The distribution of the fund in the FAAC also depends on several factors, including population, landmass and equality of states.

Although the current revenue sharing formula is under review, it is still the basis of revenue sharing at the moment. Currently, the Revenue Allocation Formula for the Distributable Pool Account (FAAC) gives the Federal Government 52.68 per cent; State Governments 26.72 per cent; Local Governments 20.60 per cent and the derivation share of 13 per cent given to the oil-producing states. This amount, which has been a source of tension between the federal government and the oil-producing states remains in force until reviewed. Another revenue source, which is shared among the federal, state and local governments, is the Value-added Tax where the Federal Government takes only 15 per cent and the State and Local Governments get 50 per cent and 35 per cent respectively. However, the ongoing court case with suit number (FHC/PH/CS/149/2020) between Rivers State and the Federal Government of Nigeria (FGN) could change the narrative of VAT collection in Nigeria.

Since the COVID-19 pandemic broke out in 2020, the global economy has been unstable. It contracted by approximately 3 per cent, leading to an increase in global poverty for the first time in a generation (Mahler et al., 2021). What looked like a timely and commendable response by governments around the globe has turned out to be the trigger for economic contraction. Steps were taken to check the spread of the pandemic including the locking down of whole countries, states and regions, resulting in further economic losses. Production cutback in advanced countries affected commodity prices and led to intense financial pressures on developing countries and worsening inflation. The pressures on federal revenues have manifested in dwindling FAAC allocation and the constrained capacity of the subnational governments to meet the basic needs of their citizen. It is now inevitable for the states to find new sources of revenue if they are to continue to function.

This study uses the descriptive data analysis approach to examine the potential for improved revenue mobilization in the south-East zone, and the current performance of the states in their Internal Revenue generation efforts. Although focused on the South-East, the study will use Imo State for more specific references and analyses of the region's revenue performance.

Overview of the South-East Economy

The South-East is made up of five states comprising Abia, Anambra, Imo, Ebonyi and Enugu. It has the smallest number of states, compared to other zones with either six or seven states per zone. The fact that the flow of resources to the zones in Nigeria is partly driven by the number of states and local governments in each of them, among other factors, has fueled agitation by the Southeast zone against marginalization, and it has continually asked for an additional state to match the number of states in the other zones. Its argument that the fewer states created in the zone by the undemocratic military regimes were meant to deprive of certain benefits, though the sound on grounds of equity and justice, has not been favored by successive federal governments. The zone is essentially agrarian, producing a variety of crops. Its main cash crops include yams, cassava, rubber and groundnuts. It is also endowed with hydrocarbon resources with some of its states participating in the membership of the Niger Delta Development Commission – an umbrella organization of oil-producing states in Nigeria. This entitles such states to a share in the 13 per cent Derivation Fund reserved for oil-producing states.

Imo state, which is the reference state of this study on the Southeast, was created in 1976 and has a land area of 5,280 square kilometers. Its population is estimated at below 5 million people, mostly youthful, industrious and enterprising. The economy is agrarian with considerable commercial activity but limited industrial and manufacturing sectors. Imo state is one of the highly indebted states of Nigeria and among those with low internally generated revenue. The study reviews the finances of Imo state with others in the same geopolitical zone and suggests ways of improving its revenue position and enhancing development. The 21 local government areas of the state have different natural resource endowments that give the state a high potential for industrialization. These include oil palm fruits available in all the local government areas including, Rice and Cassava in Idiato North, Limestone in Aboh Mbaise, Clay in Ahiazu Mbaise, and Cashew nuts in Okigwe, Hydrocarbon in

Oguta. Others are Caolin and Bentonite in Idiato South and Ehime Mbano and many others. Although coal is found in commercial quantities in Enugu State, most of the states have an identical natural endowment in agriculture and solid minerals while Imo has oil.

Stylized Facts on South-East States Financial Data

In this section, the study discusses the demographic characteristics of the region and the financial standings of the states as of the year ending 2018.

Table 1: South-East Economic and Financial Statistics, 2018

SOUTH-EASTERN STATES' INDICES	**ABIA STATE**	**ANAMBRA STATE**	**EBONYI STATE**	**ENUGU STATE**	**IMO STATE**
Est. 2018 Population	3,934,157	5,846,198	3,046,287	4,683,887	5,766,234
2018 IGR (NGN)	14,834,904,447.49	19,305,267,646.94	6,144,587,065.65	22,145,937,216.00	14,884,271,810.31
10-Year CAGR of IGR ('08-18)	35.97%	34.03%	33.44%	35.86%	37.30%
2018 -On-2017 Growth in IGR (%)	(0.55)	11.17	20.41	0.48	117.26
Q4 2018 on Q3 2018 Growth %	59.3	98.44	34.7	37.56	(24.09)
2018 NET FAAC Allocation (NGN)	55,326,313,520.15	55,249,945,897.31	44,955,009,442.29	53,104,455,149.92	54,181,645,137.52
2018 Total Revenue (NGN)	70,161,217,967.64	74,555,213,544.25	51,099,596,507.94	75,250,392,365.92	69,065,916,947.83
% Of IGR to Total Revenue (2018)	21%	26%	12%	29%	22%
Total domestic debt (NGN) Dec. 2018	67,017,185,656.92	33,490,668,536.72	55,597,352,310.28	55,032,067,848.83	98,782,494,271.48
Total Foreign Debt (USD) Dec. 2018	98,582,798.91	107,041,487.48	66,653,026.12	126,177,662.23	59,515,586.62
Total Debt in NGN (@N307/$)	97,282,104,922.29	66,352,405,193.08	76,059,831,329.12	93,768,610,153.44	117,053,779,365.01
2018 Avg. Monthly FAAC Deductions	8.82%	2.75%	9.74%	5.18%	14.75%

Sources: Debt Management Office, Central Bank of Nigeria, Imo Finance Committee and National Bureau of Statistics

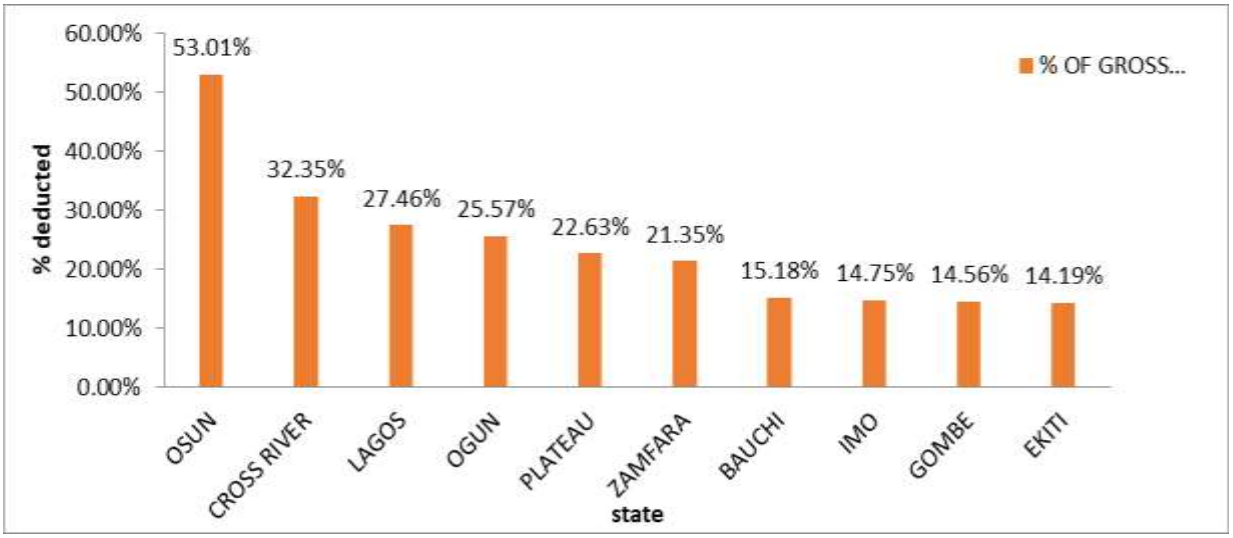
Population

In 2022, the South Eastern region accounts for 10% of the total estimated population of Nigeria, with 22 million people who are mostly concentrated in Aba and Enugu (the two most populous cities in South East). As depicted in Table 1, as of 2018, Anambra State had the largest population among them, with 5.85 million people, followed by Imo State with a population of 5.77 million people. Enugu State is third in population followed by Abia and Ebony states in the order of magnitude. These numbers are however subject to some controversy as many doubts have been raised about the authenticity of the current census figures. However, the population strength determines the market size of the region, which influences the size of IGR and the revenue from FAAC.

Internal Revenue and Debt

Regarding Internal Revenue Generation, Enugu state earned the most, with over N22.2 billion, followed by Anambra at N19.3 billion, and Imo state is number three and trails behind Enugu and Anambra States with significant differentials at N149 billion. Abia and Ebonyi keep the rear. In particular, Ebonyi was concerning indebtedness, Imo has the highest total debt (local and foreign), in naira terms at N117 billion, with a domestic component as high as N99 billion, but its foreign debt is the lowest. Relatedly, the state has the highest average monthly FAAC deductions, at 14.75 per cent. All the others have a single-digit deduction, which has less impact on their revenues. The importance of revenue growth is not lost on the states of the South-East as shown by the Cumulative Average Growth Rate (CAGR) of the IGR. In this regard, Imo state ranks first in mobilizing Internally Generated Revenue (IGR), amongst the five South-Eastern States during the review period between 2008 and 2018.

This growth achievement is significant, although it was made from a low base. However, the state is the least indebted in foreign currency with its foreign debt, which stood at approximately 59.5 million US dollars. The states continue to depend heavily on Federal allocation, for the bulk of their revenue. In the 2018 fiscal year, Enugu state received a total revenue of N75.2 billion (the highest in the region), with only N22.2 billion coming from internal sources. This was followed by Anambra State with a Net FAAC receipt of N74.6 billion and an IGR of about N19 billion. In general, the contribution of IGR to the total revenue of the states was about 22 per cent. In other words, over 75 per cent of their total revenue comes from the Federation account. The instability in FAAC allocations, which mirrors the developments in the oil industry and market, has been graphically highlighted as the weaknesses in the domestic oil market driven by oil theft and other global issues became more pronounced. This speaks directly to the question of sustainability and viability of the states.



Sources: CBN, NBS and DMO

Figure 1 - States with 15% or more in FAAC deduction in 2018

The monthly FAAC deductions against the indebtedness of the states have become a very significant drag in the efforts of the zone to develop and deploy social infrastructure. Imo is the worst hit in this regard. Other states with significant deductions (15% or more), from their FAAC, are shown in Figure 1, which indicates that Imo is not the worst hit in this regard when viewed holistically in the country. However, some states that have reached financial viability, such as Lagos and Ogun states, may not feel the impact of the deductions as much as Imo state would feel it, even if they shed more funds to deductions than Imo State, as shown in the figure above.

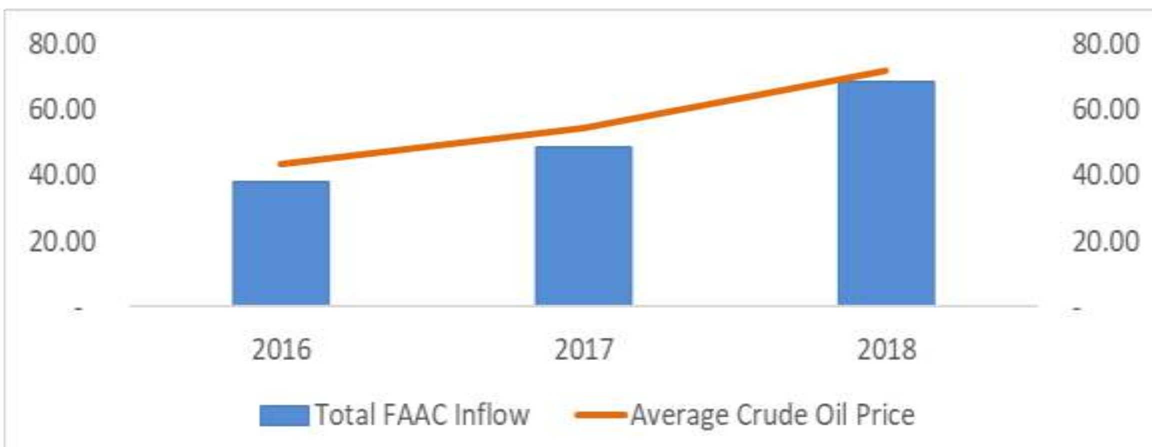
Revenue Growth Performance

The revenue achievement of most of the states leaves much to be desired many of the total FAAC Inflows grew at a CAGR of 21.47 per cent to N68.33 billion from 2016 to 2018, while FAAC fewer Debt Obligations grew at a CAGR of 21.51 per cent to reach N54.18 billion over the same period. IGR grew less aggressively at a CAGR of 36.36 per cent to N14.88 billion during the period. This growth comes from a low base and therefore may not represent the full potential of the state.

Sources: CBN, NBS and DMO data

Figure 2: Growth of Key Revenue Sources, 2016 - 2018.

The two leading revenue components for the state are the FAAC and the Pay as You Earn (PAYE). In 2018, Gross Statutory Allocation (the leading component of FAAC) contributed 53 per cent to the State's total revenue. This was an improvement over its contribution in 2017, which was 46 per cent. PAYE (the leading component of IGR) accounted for only 8% of total revenue. Its contribution declined from 11 per cent in 2017. The dependence of the state revenues on the federation account reflects the potential risk if federal revenues face uncertainties in its main source, crude oil exports. This relationship is mirrored by the positive relationship depicted in Figure 3. Clearly, State FAAC inflow showed a positive trend as crude oil prices increased. While Crude oil prices grew at a CAGR of 18.19 per cent, FAAC grew at a CAGR of 21.47 per cent as shown in Figure 3.

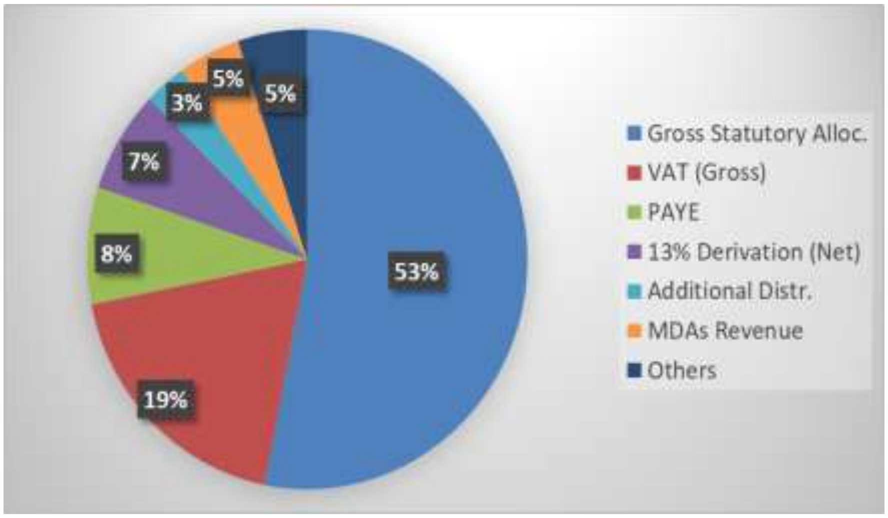


Sources: CBN, NBS and DMO Data

Figure 3 Imo FAAC and Crude Oil Prices Relationship

Key Sources of Revenue for Imo State

The state gets its funding from the following sources: IGR, PAYE, VAT, 13 Per cent Derivation Revenues from MDAs FAAC and others. Figure 4 indicates the relative importance of each source.



Source: CBN, NBS and DMO Data

Figure 4: Revenue Sources

Comparative IGR Performance of South-East States

One of the biggest challenges for the states is how to increase their IGR, to reduce the ratio of revenues coming from the volatile FAAC. The IGR of the states may be grouped into PAYE, Direct Assessment, Road Taxes, and Revenues from Ministries, Departments and Agencies (MDAs). The PAYE is the most significant source of revenue for Imo state, though the state ranks third in the volume of income from that source. Enugu earns the most from PAYE while Ebony collects the least. In terms of Direct Assessment and Road Taxes, Imo State performed better than the rest (Table 2).

The zone is not industrialized to any meaningful level. The income from PAYE is therefore most likely to come mainly from civil servants and other workers in the state. Its dominance over all other sources indicates the extent of the revenue problem in the zone – the tax on personal income of workers in a purely civil service state being the dominant source of IGR is an incongruity.

Table 2: Relative IGR Achievements by the South-East States, 2018.

State	PAYE	Direct Assessment	Road Taxes	Other Taxes	MDAs Revenue	Total IGR
Enugu	9.16	0.19	0.53	2.66	9.61	22.2
Anambra	8.89	0.82	0.64	3.93	5.02	19.3
Imo	6.84	2.45	1.47	0.32	3.8	14.9
Abia	5.14	0.75	0.32	1.75	6.88	14.8
Ebonyi	3.12	0.06	0.32	1.77	0.87	6.14

Sources: CBN, NBS and DMO data.

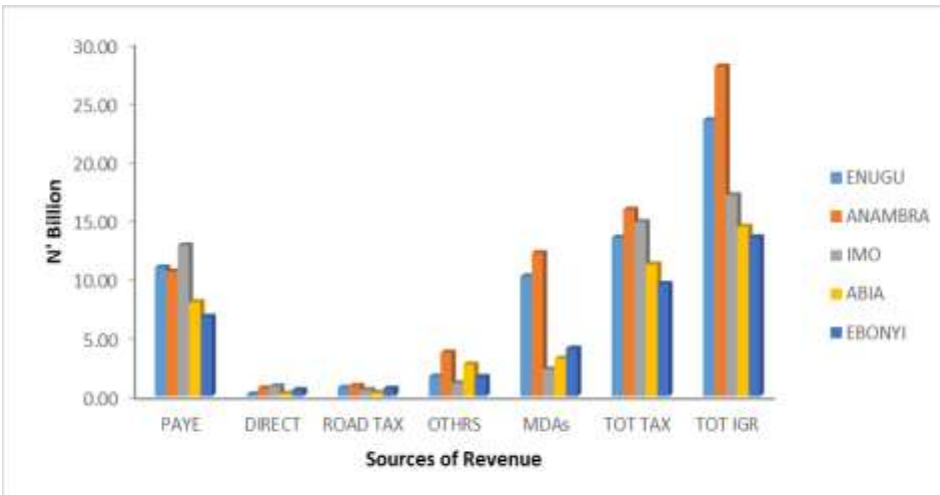
There has been some argument about companies located in one state and operating in another, thereby remitting their PAYE to the states where they locate rather than the one in which they operate and make their revenue. Where companies that are resident in Imo State remit PAYE to states where they are headquartered, such practices, though endorsed by tax laws may need to be reexamined based on equity. This practice influences the relative IGR of states across the nation, and particularly within the region as presented in Table 3 below.

Table 3: Comparative IGR for the South-East States, 2020 (₦'billion).

STATE	PAYE	DIRECT	ROAD TAX	MDAs	TOT TAX	TOT IGR	OTHERS
ENUGU	10.94	0.14	0.70	10.19	13.46	23.46	1.67
ANAMBRA	10.60	0.67	0.87	12.16	15.85	28.01	3.71
IMO	12.82	0.84	0.53	2.29	14.8	17.08	1.11
ABIA	8.00	0.23	0.30	3.20	11.20	14.40	2.70
EBONYI	6.74	0.52	0.64	4.05	9.53	13.50	1.63

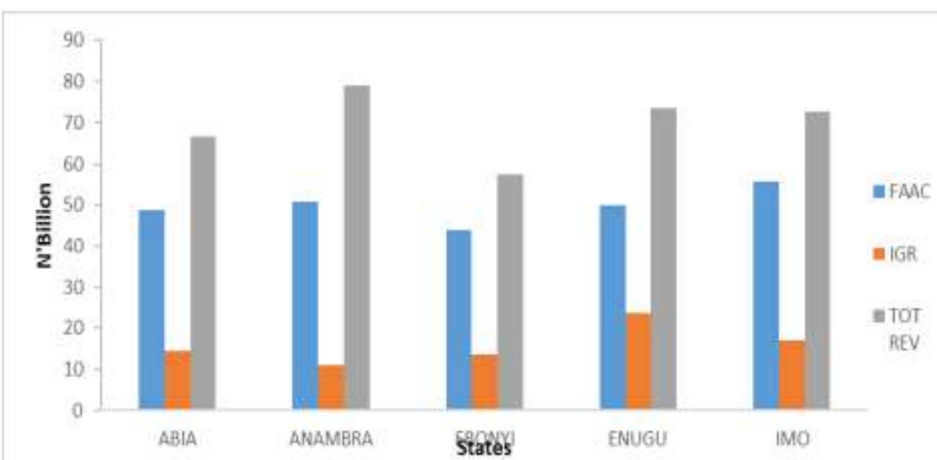
Source: NBS Data

Further, evidence has shown that the relative level of IGR influences revenue per head in these states as shown in Figure 5 below. The comparative descriptive statistics have revealed that in 2020, revenue by heads was highest in Anambra state at ₦78.93 billion; Enugu state recorded ₦73.54 billion; and Imo state came third at ₦72.81 billion in 2020. The components or sources of revenue heads were mainly from the FAAC, while IGR accounted for a meagre proportion of the total revenue heads within the period under consideration. Fortunately, while Imo state got the most resources from FAAC in 2020 worth ₦55.72 billion, it only generated only 17.08 billion in IGR, a record that places the state below Enugu state which generated ₦23.65 billion in 2020 as decomposed in Figure 6 below.



Source: Extracted from NBS data

Figure 5: South-East: Revenue by Heads, 2020



Source: NBS data

Figure 6: South-East: Revenue by Heads, 2020

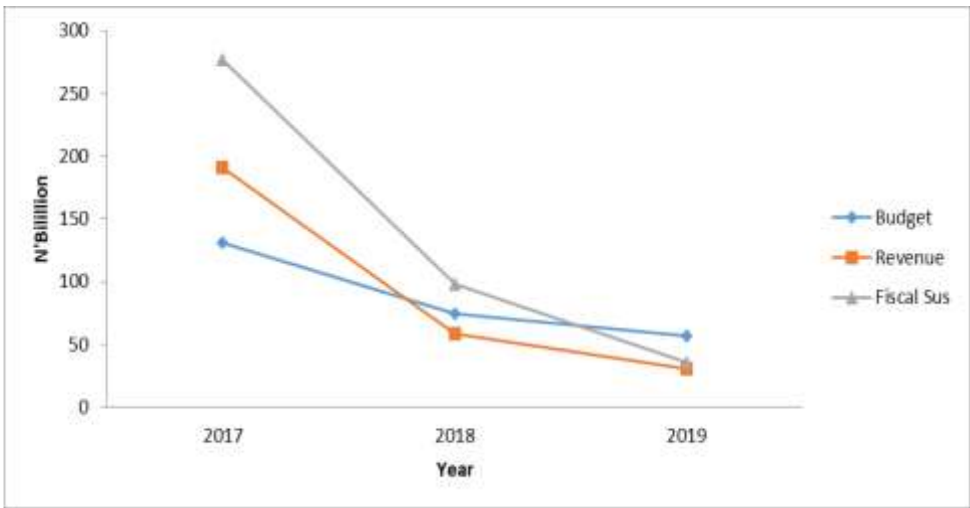
Zonal IGR Comparison, 2019

Compared to other zones in the country, the South-East does not come out with flying colours on IGR generation. Enugu is the leader of the zone with IGR contributing about 29 Per cent of total revenue; followed by Anambra and Imo with 26 per cent and 22 per cent respectively. This leadership pales to insignificance when compared to other zonal leaders like Lagos (South-West), Rivers (South-South) and Bauchi, Enugu only outperformed Bauchi. The least Imo State could do is to match Enugu state, which is equally a civil service state with a limited industrial base.

Table 4: Key IGR Sources among Zonal Leaders

State	PAYE	Direct Assessment	Road Taxes	Other Taxes	MDAs Revenue	Total IGR
Lagos	239.45	16.07	9.28	59.82	57.55	382.18
Rivers	57.10	0.55	0.20	13.51	41.43	112.78
Kano	14.90	1.65	1.66	14.06	11.83	44.11
Enugu	9.16	0.19	0.53	2.66	9.61	22.15
Bauchi	7.42	0.23	0.26	0.37	1.41	9.69
Imo	6.84	2.45	1.47	0.32	3.80	14.88

Sources: CBN, NBS and DMO Data



Source: NBS data

Figure 7: South-East: Revenue by Heads, 2020

In figure 7, the study analysed the if the state is fiscally sustainable, evidence from the budgetary provisions, revenue generation and the revenue to budget ratio shows that Imo state is not fiscally sustainable as all indicators are downward sloping. For instance, in 2017, revenue to budget ratio was 56%, but dropped to 35% in 2019.

Conclusion and Recommendations

This study examines the revenue performance of states in the South Eastern region (with emphasis on Imo state) of Nigeria to suggest IGR expansionary strategies in the face of dwindling revenue from FAAC. A descriptive analysis of the revenue drive of these states revealed that monthly allocation from FAAC accounts for over 78 per cent of their revenue, while about 22 per cent of the is derived from IGR, evidence of the lack of financial sustainability of the states. The challenge is aggravated by the disruption in trade flows due to the impact of Covid-19 and the Russia—Ukraine war. Thus, states are encouraged to be innovative in their revenue drive to meet their obligations to their citizenry. Specifically, Imo state, which recorded the fastest IGR cumulative growth rate between 2008 and 2018, has to sustain this temple of IGR expansion to meet her financial

obligations and cast off the shadow of insolvency threatening the state. One of the ways to rake in more IGR is to look inward to the endowments of the state across the 21 local government areas which are rich in
oil palm. The state should set up an oil palm revitalization committee to carry out an assessment of the present oil palm farms across the state and develop strategies on how to optimize this useful resource. In addition, the government could provide the enabling environment for the private sector to take over these state-owned enterprises for efficiency purposes.

Also, the Imo state government could commercialize the production of Rice and Cassava in the Idiato North local government area. This has the potential of encouraging domestic production and consumption of Rice and Cassava and possibly export to other states of the federation. Such commercialization would create jobs; enhance industrialization and taxable income, thus, contributing to a broader tax base for higher IGR. The study further suggests that the Imo state government could exploit the limestone in Aboh Mbaise, the clay in Ahiazu Mbaise, and hydrocarbon in Oguta, Caolin and Bentonite in Idiato South and Ehime Mbano as a medium- and long-term IGR expansion strategies.

The immediate strategy is to develop and adopt revenue optimization initiatives such as tax reformation; business enumeration; automation of all revenue collection processes; and building financial management capacity through training and retraining of staff members of the Imo Inland Revenue Service (IIRS).

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