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Public Finance and Financial Policy under Fiscal and Monetary Federalism: The Case of Bayelsa State of Nigeria

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ABSTRACT: *State public finance and financial policy cannot stand in a vacuum. Both the finance that a government needs and the financial policy it adopts must relate to the objectives of the government. So for proper examination of the state finances and financial policy, we must first answer the question: What is the objective of the State government? We assume that like any other government, the objective of the government is to enhance the economic and social welfare of the people of the state. This task in the case of Bayelsa State of Nigeria which assumes quite enormous and tremendous dimensions because in the context of the contemporary Nigeria Federal economy, we have been identified and described as one of the richest state. However it should be noted that Bayelsa State is rich but poor, underdeveloped and are where we are as a consequence of a long historical process heavily tinted with injustice and inequality resulting from our lack of powerful political muscles in the Nigerian political scene prior to 2007.*

Keywords: Public Finance, Financial Policy, Fiscal, Monetary Federalism, Bayelsa State, Nigeria.

I. INTRODUCTION

The main question in the context of the contemporary Nigeria's federation is, how can the government turn this oil rich but impoverish state to rich, in order to improve the social and economic welfare of the people? The task falls squarely on government because private efforts may take time to yield appreciable results.

The task has been limited and confined to the financing aspect of the problem. So, the main purpose of this paper is to examine in order to be able to improve its finances or financial position to finance the several programmes which it might undertake in an attempt to meet the new economic challenges that will be posed in an attempt to improve the economy of the state and the economic and social welfare of the people (see Baghebo 2012 for this and related issues).

The structure of the rest of the paper is as follows. In section two, we review related literature. Section three is on theoretical framework. In section four, we examine the relation between government finances and the efficiency of the system of public administrative finance and propose that "government finance can be doubled by mere improving efficiency of the collecting and administrative machinery without increasing the rates". In section five, we go on to look at the interrelationship between tax base, taxable capacity and the government finance. Here we show that with judicious government spending, the taxable capacity of the state can be considerably improved. In section six, we deal with the government finance of public project. Finally, in section seven, we conclude the work.

II. LITERATURE REVIEW

Baghebo (2012) examine the effective utilization of tax revenue in Nigeria. He asserts that Nigeria has been one of the most disappointing development stories of the modern era – a contemporary tale of the risk of huge revenue from taxation in an environment of weak governance. He stressed that in recent years, the most conspicuous fact about Nigeria's economy is that, corruption and mismanagement of Nigerians post-colonial government has prevented the channeling of the country's resources from taxation and other sources into lasting improvement in infrastructure and the construction of a sound base for self-sustaining economic development. He recommended for an improvement in the quantity and quality of resources available to the government for its activities and; the ways in which the resources available to the government are managed.

Abdulrazaq (2004) examine tax laws in Nigeria. He starts by setting the implicit premises on which administrative arrangements for the Nigerian tax system are based; the central assumption is that the tax payer is incompetent and dishonest. The procedure therefore seeks to ensure that as far as possible the correct amount of any tax liability is deducted from income before it is received, to ensure that the administrative burden on the tax payer is reduced to a minimum, and that wherever possible, such obligations are imposed on employers and other payers of income and on the revenue itself. He concludes that with financial and intellectual reservoirs of great depth and breadth to draw from in Nigeria, we need to combine insight, knowledge and original thinking to create new opportunities in tax administration.

Tetsuya Nosse (1981) examines the effect of tax structure change upon income redistribution under inflationary economic growth. Whilst economic growth has evident automatic effects in reallocating tax base (absolute and relative) even in real terms, it may consequently have an influence on the relative change in tax burdens under fixed tax system. The central theme of Tetsuya's study is therefore to formalize the prices through which the inflation will affect tax structure change and henceforth redistribution, and to observe the facts in these formulae with the long run empirical evidence. The study attempt to investigate the long-run shifting process of the U-shaped pattern of the tax burden. In dividing the elements of tax structure change into automatic factors and discretionary measures, the author seek for the appropriate measure of fiscal indexations.

Devinder et al (1981) seeks to fill a gap in the literature by using the ordering rules of stochastic dominance (SD) to examine the effects of taxation on risky investment decision. The application of the SD rule provides a theoretical appealing and operationally usable method for ordering pairs of uncertain alternatives, while having limited or no knowledge of the form of the decision makers' utility function. Thus, while it is still assumed that the investor maximizes expected utility, SD ordering rules consider the entire distribution of outcomes without requiring specific information on each of the n moments that affect expected utility. As a consequence, less restriction is imposed on the nature of utility function and/or return distributions.

Evidently, from the studies reviewed so far, state public finance and financial policy under fiscal and monetary federalism receive little attention in the orthodoxy. This has created a vacuum which this work tends to fill

III. THEORETICAL FRAMEWORK

The theoretical framework for this study is drawn from the Peacock and Wiseman theory of public expenditure and government finance. Allan Peacock and Jack Wiseman theory, otherwise known as PWT, was based on the political theory of public expenditure determination which states that government likes to spend more money, that citizens do not like to pay more taxes and that government needs to pay some attention to the aspiration and wishes of their people.

The PWT attempted to explain the circular trend or time pattern of change in government expenditure in response to development in the political economy while the taxable capacity of the people acts as a constraint. Their theory is known as Displacement Hypothesis that government expenditure grows in step wise fashion.

During periods of catastrophe or wars, government expenditure grew rapidly and remain constant during the war, famine or disaster otherwise catastrophe period. They argued that government expenditures are largely determined by government revenue or taxations. PWT maintains that as the economy and income grew, tax revenue would rise thereby enabling government expenditure to rise in the line with GNP.

The acceptance of the existence of a tolerable level of taxation which acts as a constraint on government behavior is consistent with Clark's "Catastrophe School" of taxation. Government imposes higher taxes which are regarded as acceptable during period of crisis.

IV. GOVERNMENT FINANCE AND THE EFFICIENCY OF THE ADMINISTRATIVE SYSTEM

The usual sources of finances for any government under the private enterprise or mixed economic system are different types of taxes and debt. In Nigeria, under fiscal federalism, the state governments are however limited to certain forms of taxes and debt, while the Federal or central government has exclusive or concurrent jurisdiction over certain revenue sources (see CITN Nigerian Tax Guide and Statutes 2002). For the state, the most prominent of these sources of revenue are personal income tax, property tax, sales and purchases tax on selected commodities like produce, licenses, stamp duties, estate duties, hotel services, etc. the most significant of these taxes however is the personal income tax. Taxes on income of bodies un incorporated under the company's law of 1968 go to the Federal government.

Apart from the taxes, the other sources of the state government finances are statutory grants and debts.

In this section, we shall examine how the government can improve its finances from taxes, by improving the efficiency of the state administrative system (see Bassey 2007).

The monthly internally generated revenue in the state has not improved significantly compared to states like Lagos, Rivers that can comfortably pay salaries of civil servants and embark on some meaningful development projects in the event of delay in the disbursement of Federal allocation. The question now is, what are the factors responsible for this poor performance and how can the performance be improved so as to increase the tax earnings

4.2Factors Responsible for the low earnings from personal income tax (PIT): Problems of income taxation

Several factors are responsible for the poor performance of personal income tax as a source of revenue to the government. In this section, we shall examine the factors that account for the non-impressive contribution of personal income tax (PIT) as revenue earned to the government. For ease of exposition, we shall group the factors into three main categories: those relating to the tax system, those relating to our level of social and economic development, and those which are pure managerial. The taxonomy is by no means water-tight.

4.2.1 Factors relating to the tax system

In Nigeria, PIT is a concurrent issue between the Federal and State government. The Federal government sets the broad framework or rules within which the tax system operates, and the states merely fill in the administrative details. For instance, the Federal Government sets out in income tax management act (1961) what incomes are assessable to tax, what persons are subject to tax and which authority has the jurisdiction to tax a person or his income. Recently the scope of the ITMA has been extended to include the determination of the tax rates and personal statutory reliefs which are expected to operate uniformly throughout the Federation.

This system of dual control of PIT limits the scope of the state government considerably in manipulating PIT as a source of revenue. For instance, there has been considerable concern expressed about the low level of the tax rates and the rather over generous statutory allowances, but there is very little the state government can do, since these are issues within the purview of the Federal government authority. The state governments are actually in a sort of straight jacket, so that even if the local conditions and needs of the state were to dictate higher rates of taxes there is not much the state government can do.

This weakness reduces the ability of the states to use statutory PIT as an effective source of revenue. And this becomes quite a serious problem when it is realized that apart from statutory grants, PIT is the most important source of revenue for the state.

On their own there may not much the state Revenue Authority can do about the constraint imposed by the dual control of tax except probably to cooperate with other state authorities and press for reforms of the Federal tax laws though it must be remembered that the Federal government has been consistently moving the country towards uniform tax system.

Another factor relating to the system that has helped to reduce the potency of the PIT as a source of government revenue is the fact that the tax laws and provisions etc are extremely complex. The complexity reduces the ability of an average tax official to interpret and apply the provisions correctly and this could lead to considerable tax avoidance and or evasion and therefore loss of revenue to the government. The sheer complexity of the regulations could tempt one to opt for the easy way out rather than try applying the rules correctly. The complex aspects are partly of our colonial inheritance, since the Nigeria tax laws were handed down to us by our colonial masters.

4.2.2Factors which are largely managerial

Here we discuss factors associated with the managerial competence of the Revenue Authorities.

- Failure to re-enact important and relevant Federal provisions: Broad rules are set by the Federal government in the ITMA for the operation of the tax system throughout the Federation, the state government cannot rely on the provisions of the ITMA to administer personal income taxes in their respective areas of jurisdiction without first of all re-enacting such provisions in their local tax laws.
- However, many of the state Revenue Authorities have either deliberately ignore or forgotten to re-enact and incorporate some of these provisions, especially the amendments, into their tax laws, and this has often led to considerable loss of revenue. For instance decree No. 7 of 1975 and decree No. 65 of 1966 both amended the ITMA and subjected benefits in kind received by employees from employers to income tax.
- To give an idea of the amount of revenue the Bayelsa State is losing through the non-implementation of the amendment, suppose there is about 20,000 senior staff in the Universities, Polytechnics, government departments, State legislative members and parastatals, and also private companies who enjoy the staff accommodation facilities and assume that the rents are about ₦8,000 p.a. on average. Then if we make the usual deductions and adjustment, assuring that the staff have already earned their maximum personal reliefs on their salaries and apply tax rate of 15%, then it will be found that what the state government losses is in the order of about twenty one million naira (₦21,000,000) annually. With the application of an average tax rate of about 20%, the tax earnings from this source alone would have been nearly ₦24 million annually or about ₦2 million monthly.
- Special treatment of women: Another factor in this category that has led to the reduced potency of the PIT as a revenue earner is that the tax authorities to a large extent treat taxation as a male affairs. The system has for long been treating women as if they do not earn any income and if they do, theirs should be tax-exempted even though the ITMA does not exclude women in its definition of taxable persons. Thus they hardly ever bordered for tax except those in paid employment who unavoidably come under the PAYE system. This special treatment, apart from leading to loss of substantial revenue also leads to

large scale evasion by men who register many of their unincorporated business in the name of women. Since women are hardly ever bordered, most of the incomes of these businesses escape tax.

- To a large extent, PIT in this country is treated as a male affair. The amount of revenue lost by giving women a special treatment with respect to tax is quite enormous.
- Non or Under Assessment of Non-Salaried Workers: Another aspect of managerial problem that has resulted in a discriminatory tax system is that income tax is treated as an affair of only those who are in paid employment and caught within the PAYE system. Salaried workers are penalized and discriminated against in terms of financing the affairs of the state whereas the benefits of government programmes are enjoyed by all. Take for instance vulcanizers, mechanics and other self-employed, because they are not taxed afford the luxuries of life. There is no reason letting these people off the tax except probably for the plain ignorance or careless indifference of the officials. Even if the traders do not keep accurate or any records of their earnings, the law provides adequately for how such persons can be assessed.

- Closely connected with the above is the fact that the Revenue departments are ignorant of the tax laws and sometimes faces serious shortage of qualified manpower. Most of the Revenue officials especially those outside the state capital are not conversant with the tax provision. They do not even know what taxable income is. If they do, they would have known that the taxi driver operating between Yenagoa and other communities and makes N1,000 net per day is making income subject to tax.

- The tax officials have not been able to exploit the existing sources of taxable income fully and these have resulted in considerable under-assessment and tax evasion and avoidance. Moreover, the inability of many of them to interpret and apply the tax laws makes the clever businessman to easily manipulate the law to his advantage. The revenue staff should be properly trained and educated so that they can have the courage and the guts to examine and interpret the accounts prepared by businesses, be able to confront contractors, transport owners or their agents etc. Revenue staffs hardly have the will or conviction to pursue such evaders.

- Corruption and under assessment: Most tax officials are very corrupt. They are known to collude with employees caught within the PAYE system to arrange or workout maximum reliefs for them, so that they pay minimum tax. Nearly all junior staff have a wife, four children, dependent relatives etc. each and claim maximum personal relief and thereby pay little or no tax. The government loses considerable amount of money through these practices. Competent and honest Revenue Authorities should be able to check this.

4.2.3 Factors Relating to our level of Economic and Social Development

There are two important factors we would like to mention briefly under this heading. First is the negative attitudinal factor and the other is the low monetization of most of the rural economies in the far away parts of the state.

4.2.3.1: Attitude to Tax

There is a serious problem of negative attitude and apathy towards tax. The attitudinal factor is very important because even in a well-developed system with the best enforcement measures, the income tax objectives can be defeated if the majority of the tax payers wish to do so. The negative attitude derives partly from the fact that the public is not well informed about the need and usefulness of personal taxation. Quite a large number of people both in the urban and rural areas do not know why they pay tax nor does the government through its appropriate organs take the trouble to explain to the people why tax is demanded. There is a lot of cooperation required in tax in order to make it successful, and this cooperation can only come if the people are convinced of the need and propriety for tax. It is therefore necessary that the government evolve a well-organized information distribution system aimed at educating the public about the need for tax. The public should be told that they can object to an assessment by appealing to the appropriate authorities. And they should be told how they can seek such redress when they feel the tax officials have “cheated” them. There is no doubt the fact that a well-informed public would respond more easily and positively to demand for tax than an ill-informed lot.

The negative attitude can also arise as a result of reckless spending habit of the public authorities. So there is need for judicious spending of public money. Basic needs that affect the tax payers like food, shelter, roads, water, education, health, etc should receive priority attention before prestige projects.

4.2.3.2: The other factor in this category is the low monetization of the rural economy. This makes assessment based on income difficult. The rural economy operates more on the barter exchange system which makes it difficult for tax assessment and collection. Here the tax official is expected to monitor exchange and its monetary equivalent for tax purpose.

V. TAX BASE, TAXABLE CAPACITY AND GOVERNMENT FINANCE

The central argument here is that, with judicious public investment and management, the government can increase within a relatively short period, its taxable capacity and have the amount of income derivable from tax, given the present level of efficiency and legal constraints. This is a serious issue, the most important object subject to tax in the states are income and also sales and purchase of selected items. However with increased income or purchasing power, consumption, purchases and sales are likely to increase. The central question we shall address ourselves is how can we increase the income of the state and hence its taxable capacity.

The incomes in question are the income of the civil servant and other workers, sole traders and other business men, farmers, fishermen and various suppliers of services etc. Since the income of the civil servants depends to a large extent on the income of the government, we shall leave them aside yet, and see how the income of the other entities – the productive sector can be increased in order to increase the income of the government, which will in turn use these in paying civil servants.

- To increase the income of the suppliers of goods and services (those in the productive sector), the effective demand for the goods and services must be increased and their sales, turnover and profit will increase. Therefore how can we help to create the effective demand or the market for the various goods and services of those producers?

- This question is relevant and concerns the government as much as the traders, because the government income depends on the income of the productive sector. And this is why colonial and many other governments have always gone out of the way to acquire and secure markets for the productive enterprises of their economies. This is why despite the evils of apartheid, Europe and America protect South Africa because of the huge market that their firms have there. So in the present context of the Nigerian economy, how can the government help the productive enterprises of Bayelsa State to increase or enlarge their market?

- One distinguishing feature between the Nigerian economy, and the other economies we have studied, is the low level of consumer credit. Everything is either procured with cash or not at all. This limits effective demand. It might be difficult initially for individual traders to expand their sales effectively through credit. But supposing Bayelsa State Trading Company (BYTRACO) is willing to allow some monthly credit on some agreed terms to customer. There is no doubt that this will increase the sales and profit of BYTRACO. If it does so by 50%, its income and taxable profits are likely to increase by nearly 50%.

- In the event of excess demand, a logical sequence from the above is that when market and demand are expanded, supplies must also be expanded. BYTRACO would ensure increased supply by increasing or expanding productive capacities. For goods produced locally in the state (food, furniture, bricks for housing etc) BYTRACO or its associates can take steps to ensure effective collection and delivery system from small producers.

- There is no doubt about the need for a serious programme of local manufacturing. And the Universities should get seriously involved if not leading the way in various researches in light and heavy engineering and other areas of technology.

VI. GOVERNMENT FINANCE OF PUBLIC PROJECT

Having identified what programmes could be undertaken in order to increase the taxable capacity, the question now is, how do we get the money required to finance these projects in order to improve the finances of the government.

a. Finances of the government can be considerably improved with improved efficiency and administration of the tax system,

b. Another means of financing the project could be inviting direct public participation through sale of securities to them. This would be easier in the case of a public company. But since the tax of about 50 percent on the profit of limited liability companies goes to the Federal government, we would be reluctant to recommend this form of organization due to the limited benefits to state government. On the other hand, simple partnership has a limitation of maximum membership. So the government could sell investment credit certificate to public to raise special investment tax of about two or three naira on its taxable population.

c. Alternatively, the level of participation could be between the local governments and state government on 50 – 50 basis or between the local government, state government and villages or families of the state so as to keep the number down.

d. Still another important alternative is to go to the open capital market and borrow. Each project can be 50% geared. After all, an average level of gearing for most Nigerian enterprises is in excess of 150% of equity capital

VII. CONCLUSION

The "Missing Revenue" in all state governments especially in Bayelsa State is enormous and this account for Revenue loss. This takes the form of administrative inefficiency and lack of knowledge, understand and application of tax laws by Revenue officials in the respective states of the Nigerian federation. Ignorance of the tax law denied Revenue officials from knowing the proper definition of assessable income. Tax education, to enlighten the tax payers why they should pay tax by justifying government expenditure prudently should be carried out periodically. On the job training for Revenue officials to acquaint them with current trends on tax administration should be carried out on regular bases. A good and conducive working environment for tax officials equipped with modern technology will improve efficiency. Attitudinal change for both tax officials and the tax paying public is desirable. This will reduce the rate of tax evasion and avoidance and improve government finances.

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