International Journal of Global Affairs, Research and Development (IJGARD), Vol.4, No.2, 16-38, ISSN 2992-2488

FISCAL FEDERALISM AND THE CRISIS OF LOCAL GOVERNMENT UNDERFUNDING IN NIGERIA: A CRITIQUE OF THE FEDERATION ACCOUNT AND REVENUE ALLOCATION FRAMEWORK

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Year of Publication: June,2026

ABSTRACT

Fiscal federalism in Nigeria has produced systemic imbalances that disproportionately disadvantage local governments, creating a crisis of underfunding that undermines grassroots governance and democratic consolidation. This seminar paper critically examines the structural and institutional determinants of local government underfunding within Nigeria's fiscal federal architecture, focusing on the Federation Account, vertical revenue allocation formula, and State Joint Local Government Account (SJLGA). Drawing on fiscal federalism theory particularly Oates' Decentralisation Theorem and Musgrave's framework for intergovernmental fiscal relations the paper analyses how constitutional design, political dynamics, and institutional weaknesses have produced chronic fiscal subordination of the third tier. The paper argues that the SJLGA, rather than serving as a fiscal conduit, functions as a mechanism of state-level fiscal control that diverts, delays, and withholds statutory allocations from local councils. The vertical sharing formula allocates only 20.60 per cent of Federation Account revenues to local governments despite their constitutionally mandated responsibilities for primary education, healthcare, and rural infrastructure. Structural constraints on internally generated revenue, administrative incapacity, and over-reliance on volatile oil revenues compound the crisis. The paper evaluates the transformative potential of the 2024 Supreme Court ruling affirming direct allocation to local governments and proposes reforms including the abolition of the SJLGA, revision of allocation criteria to incorporate fiscal effort and infrastructure deficits, strengthening of local revenue generation capacities, and institutional reforms to enforce fiscal accountability. The paper concludes that meaningful fiscal decentralisation requires not merely increased transfers but a fundamental restructuring of intergovernmental fiscal relations to align expenditure assignments with revenue-raising powers at the local government level.

Keywords: *Fiscal federalism, local government underfunding, Federation Account, revenue allocation, State Joint Local Government Account, Nigeria*

1.0 INTRODUCTION

Fiscal federalism constitutes a foundational pillar in the architecture of federal political systems, shaping the allocation of financial responsibilities and resources among tiers of government. Within the Nigerian context, fiscal federalism has evolved through complex historical, political, and institutional trajectories, reflecting tensions between centralisation and decentralisation. The theoretical premise of fiscal federalism, rooted in the works of scholars such as Musgrave and Oates, emphasises efficiency, equity, and accountability in public resource distribution (Oates, 1972). However, in practice, Nigeria's federal fiscal framework has deviated significantly from these ideals, producing systemic imbalances that disproportionately disadvantage subnational entities, particularly local governments. The persistent underfunding of local governments raises critical questions about the functionality and sustainability of Nigeria's intergovernmental fiscal relations.

The Federation Account represents the central mechanism for revenue pooling and distribution in Nigeria's fiscal federal structure. Established under Section 162 of the 1999 Constitution (as amended), the account aggregates revenues derived primarily from oil exports, taxation, and other federally collected sources before allocation to the three tiers of government. While this framework ostensibly promotes equitable sharing, it has been criticised for entrenching fiscal dependency, especially among states and local governments (Suberu, 2001). The vertical revenue allocation formula, which currently allocates a dominant share to the federal government, reflects enduring centralist tendencies that undermine the autonomy of lower tiers. Consequently, local governments remain financially constrained, limiting their capacity to fulfil constitutionally mandated responsibilities.

The crisis of fiscal federalism in Nigeria is further compounded by structural inefficiencies in revenue allocation mechanisms. The Revenue Mobilisation, Allocation and Fiscal Commission (RMAFC), constitutionally mandated to review and recommend revenue-sharing formulas, has faced challenges in implementing reforms that reflect contemporary socio-economic realities. Scholars have argued that the existing formula fails to adequately consider factors such as population dynamics, developmental needs, and fiscal effort (Arowolo, 2011). As a result, disparities in resource distribution persist across regions and administrative levels, exacerbating inequalities and undermining national cohesion. These structural deficiencies have significant implications for governance at the grassroots level, where service delivery is most critical.

Local governments in Nigeria occupy a strategic position in the governance framework, serving as the closest tier of government to the people. They are constitutionally assigned responsibilities including primary education, healthcare, rural infrastructure, and community development. Despite these roles, local governments are chronically underfunded and institutionally weakened. One of the primary mechanisms contributing to this underfunding is the State Joint Local Government Account (SJLGA), which allows state governments to exercise substantial control over funds allocated to local governments. Empirical studies have demonstrated that this arrangement often leads to fund diversion, delays in disbursement, and fiscal mismanagement (Ezeani, 2012). Consequently, local governments are unable to effectively discharge their functions, leading to poor developmental outcomes.

The interplay between political dynamics and fiscal arrangements further exacerbates the crisis of local government underfunding. State governments, wielding significant political and financial influence, frequently encroach upon the autonomy of local governments. This has resulted in a quasi-unitary fiscal system, where subnational fiscal independence is more theoretical than practical. The absence of direct allocation mechanisms and weak institutional safeguards has entrenched a system of fiscal subordination (Ekpo, 2004). Moreover, political patronage and elite capture have distorted resource allocation processes, diverting funds away from developmental priorities toward partisan interests. These dynamics highlight the need for a critical reassessment of Nigeria's fiscal federalism framework.

Another dimension of the crisis lies in the over-reliance on oil revenues, which has rendered Nigeria's fiscal system highly vulnerable to external shocks. The volatility of global oil prices directly impacts the volume of funds available in the Federation Account, thereby affecting allocations to all tiers of government. This dependency has discouraged efforts toward revenue diversification and fiscal innovation at the subnational level (Sala-i-Martin & Subramanian, 2013). For local governments, which lack robust internally generated revenue (IGR) mechanisms, this volatility translates into unpredictable funding streams and fiscal instability. The resulting uncertainty hampers long-term planning and undermines sustainable development initiatives.

In addition to structural and economic challenges, institutional weaknesses have played a significant role in perpetuating the underfunding of local governments. Weak accountability mechanisms, limited transparency in revenue allocation processes, and inadequate fiscal oversight have created an environment conducive to corruption and inefficiency. Institutions tasked with monitoring fiscal operations, including anti-corruption agencies and legislative bodies, often lack the capacity or political will to enforce compliance (Ojo, 2009). This institutional fragility undermines public trust and further erodes the effectiveness of fiscal federalism in Nigeria. Strengthening these institutions is essential for ensuring equitable and efficient resource distribution.

Given these multifaceted challenges, the crisis of fiscal federalism in Nigeria necessitates a comprehensive and reform-oriented approach. Addressing the underfunding of local governments requires not only a revision of revenue allocation formulas but also the restructuring of intergovernmental fiscal relations to enhance autonomy, accountability, and efficiency. Policy reforms should prioritise the abolition or reform of the SJLGA, the introduction of direct allocation mechanisms, and the strengthening of local revenue generation capacities. Furthermore, aligning fiscal federalism with principles of good governance and sustainable development is imperative for achieving meaningful decentralisation.

This paper interrogates this paradox through the lens of fiscal federalism theory. It critiques the design and operation of the Federation Account, examines the vertical revenue-sharing formula that determines LGA allocations, analyses the State-LGA Joint Account as a structural impediment to fiscal autonomy, and assesses the implications of LGA underfunding for democratic consolidation and national building. The article is structured in twelve sections. Sections one through three establish the theoretical and historical context. Sections four through seven analyse the mechanics of revenue allocation and LGA fiscal subordination. Sections eight through eleven address the empirical consequences and reform imperatives. Section twelve presents the conclusions.

The work contributes to a growing body of scholarship on Nigerian fiscal federalism and local government reform, offering a theoretically grounded critique of the revenue allocation framework and proposing reforms calibrated to the structural realities of the Nigerian federation. It draws on constitutional analysis, official fiscal data from the Federation Account Allocation Committee (FAAC), and the extant literature on fiscal federalism, decentralisation, and democratic governance in Africa.

2.0 LITERATURE REVIEW

2.1 CONCEPTUAL FRAME WORK

2.1.1 Fiscal federalism and democratic consolidation

Beyond efficiency and assignment, fiscal federalism intersects with democratic theory in important ways. Scholars such as Brancati (2006), Cheema and Rondinelli (2007), and Smoke (2019) have argued that fiscal decentralisation, when properly designed, deepens democratic accountability by bringing decision-making and resource allocation closer to citizens, creating opportunities for participatory governance, and generating local political competition that disciplines elected officials. Conversely, fiscal centralisation undermines local democratic institutions by depriving them of the resources necessary for effective governance, eroding electoral accountability, and fostering civic disengagement.

In the Nigerian context, the underfunding of LGAs has created a vicious cycle: resource-starved councils cannot deliver services, citizens disengage from local democratic processes, and the absence of meaningful local governance reduces the demand for fiscal autonomy — thereby reproducing the conditions that sustain elite capture of LGA allocations. Breaking this cycle requires not merely fiscal transfers but a fundamental restructuring of the revenue allocation framework in ways that guarantee LGA fiscal autonomy and accountability.

2.1.2 Historical background: Revenue allocation from 1946 to the 1999 Constitution

The Colonial and Early Post-Independence Period

The foundations of Nigeria's revenue allocation system were laid under British colonial administration. The Richards Constitution of 1946 introduced a quasi-federal framework that distributed fiscal powers between the central government and regional authorities. Successive revenue allocation commissions the Phillipson Commission (1946), the Hicks-Phillipson Commission (1951), the Chick Commission (1953), and the Raisman Commission (1958) grappled with the principles of derivation, need, and national interest as bases for distributing revenue among the centre and the regions. The dominance of derivation as a principle in the early post-independence period reflected the economic importance of regional cash crops groundnuts in the North, cocoa in the West, and palm produce in the East and provided a fiscal rationale for regional autonomy.

The discovery of petroleum in commercial quantities in the Niger Delta in 1956, and the rapid growth of oil revenues following the 1973 OPEC oil embargo, fundamentally transformed the political economy of Nigerian federalism. Oil revenues, accruing primarily to the federal government through petroleum profits tax and royalties, shifted the fiscal balance decisively towards the centre. As oil revenues grew to dominate federal receipts, the derivation principle was progressively diluted from 50 per cent in the early post-independence period to 3 per cent in the early 1990s in favour of principles that advantaged the more populous but oil-poor northern states. This shift institutionalised fiscal centralism and established the Federation Account as the primary mechanism for distributing nationally pooled revenues.

Military Rule and the Consolidation of Fiscal Centralism

The military governments that dominated Nigerian politics from 1966 to 1999 (with a brief civilian interlude between 1979 and 1983) systematically consolidated fiscal power at the centre. The Decree No. 13 of 1970, the Revenue Allocation Acts of 1981 and 1982, and the various military decrees governing the Federation Account reflected the logic of a centralised command state rather than a genuine federation. Local government councils were subordinated to state governments, and their fiscal resources were contingent on state largesse rather than constitutionally guaranteed allocations.

The 1976 Local Government Reform under General Murtala Muhammed represented a significant, if ultimately incomplete, attempt to reconstitute local government as an effective tier of governance. The reform established a uniform system of local government councils, defined their functions, and provided for statutory allocations from both federal and state governments. However, the subordination of LGAs to state governments remained entrenched, and subsequent military administrations progressively eroded the fiscal autonomy gains of the 1976 reform. By the time of the return to civilian rule in 1999, local government councils were fiscally dependent, administratively weak, and politically subordinated to state governors a condition that the 1999 Constitution would institutionalise rather than remedy.

The 1999 Constitution and the Third-Tier Framework

The 1999 Constitution of the Federal Republic of Nigeria established the current framework for local government finance. Section 162 creates the Federation Account into which all revenues of the federal government are paid and from which allocations are made to the federal, state, and local governments. Section 162(5) mandates that the amount standing to the credit of local government councils in the Federation Account shall be distributed among the councils of the states in such a manner as may be prescribed by the Houses of Assemblies. Section 162(6) requires that each state shall maintain a special account the State Joint Local Government Account into which shall be paid all allocations to the local government councils of the state from the Federation Account and 20 percent of the internally generated from the government of the state must be paid into the Account.

The constitutional framework thus contemplates a two-stage transfer mechanism: a federal allocation to states for onward transmission to LGAs through the Joint Account, supplemented by state government contributions. In practice, this mechanism has been systematically subverted. State governments have routinely delayed, diverted, or withheld LGA allocations, using the Joint Account as a mechanism of fiscal control rather than fiscal transmission. The constitutional provision that was intended to guarantee LGA funding has, paradoxically, created an institutional chokepoint through which state governments exercise fiscal dominance over the third tier.

2.2 Theoretical framework

2.2.1 Fiscal federalism theory and the decentralisation thesis

Fiscal federalism, as a theoretical tradition, addresses the normative and positive questions of how fiscal functions and instruments should be distributed across levels of government in a federal or multi-tiered system. The foundational contributions of Musgrave (1959) and Oates (1972) established the analytical architecture that continues to inform debates about decentralisation, revenue allocation, and intergovernmental fiscal relations. Understanding their frameworks is essential to evaluating Nigeria's fiscal architecture and diagnosing the structural failures of its third-tier funding arrangements.

2.2.2 Oates' Decentralisation Theorem

Wallace Oates' decentralisation theorem holds that, in the absence of cost savings from centralised provision and spillover effects across jurisdictions, the provision of public goods and services is most efficient when undertaken by the lowest level of government capable of internalising all relevant costs and benefits. The theorem rests on the assumption that lower-level governments possess superior information about the preferences of their constituents and can tailor public goods provision accordingly, thereby generating welfare gains that centralised provision cannot replicate. This logic of jurisdictional matching aligning the spatial scale of public goods provision with the spatial distribution of preferences and costs provides the normative foundation for fiscal decentralisation.

Applied to Nigeria, Oates' theorem predicts that LGAs, as the tier of government closest to the citizenry, are best positioned to deliver the services assigned to them in the Fourth Schedule of the 1999 Constitution. Primary health care, primary education, and local infrastructure are paradigmatic cases of public goods with highly localised benefit distributions and constituency-specific preferences. Centralised provision of these services at the federal or state level generates informational inefficiencies and political distortions that reduce welfare. The decentralisation theorem thus provides a strong normative case for ensuring that LGAs possess the fiscal resources necessary to fulfil their constitutional mandates. The persistent underfunding of the third tier is, from this perspective, not merely a fiscal anomaly but a welfare-reducing structural failure.

2.2.3 Musgrave's Assignment Problem

Richard Musgrave's framework for intergovernmental fiscal relations identifies three functions of government: resource allocation, income redistribution, and macroeconomic stabilisation. Musgrave (1959) argues that while redistribution and stabilisation functions are most appropriately centralised given the risk of redistributive competition among sub-national governments and the macroeconomic externalities of decentralised fiscal policy the allocation function can and should be decentralised to the extent that public goods have localised benefit distributions. Crucially, Musgrave also identifies the 'assignment problem': the need to ensure congruence between expenditure assignments and revenue-raising powers at each tier of government. A tier saddled with expenditure obligations that exceed its revenue-raising capacity faces a structural fiscal imbalance what scholars of fiscal federalism call a 'vertical fiscal imbalance.'

Nigeria's LGAs present a textbook case of Musgravian vertical fiscal imbalance. They are assigned substantial service delivery responsibilities under the Fourth Schedule of the 1999 Constitution but possess severely constrained revenue-raising powers. Their primary revenue sources tenement rates, fees on local markets, and motor park levies are economically thin and administratively costly to collect. The consequence is chronic fiscal dependence on federal and state transfers, a dependence that inverts the logic of fiscal assignment and reduces LGAs to administrative extensions of higher tiers rather than autonomous units of democratic governance.

2.3 Empirical Review

2.3.1 The federation account: architecture and vertical sharing formula

The Federation Account is the central fiscal institution of Nigerian federalism. It is the repository into which all federally collected revenues flow and from which allocations are made to the three tiers of government. Understanding its architecture, the revenues it captures, and the formula by which it distributes resources is essential to diagnosing the fiscal condition of local government in Nigeria.

2.3.2 The Architecture of the Federation Account

The Federation Account captures revenues from a range of federal sources, including petroleum profit tax, royalties, customs and excise duties, companies income tax, value added tax (which flows through a separate but related distribution mechanism), and earnings from signature bonuses on oil block allocations. The dominant contributor has historically been petroleum revenue: despite diversification efforts, oil and gas revenues have consistently accounted for between 60 and 80 per cent of Federation Account receipts during the period from 1999 to the present. This structural dependence on petroleum revenues exposes the Federation Account and all tiers of government dependent on it to the volatility of global oil prices, generating cyclical fiscal crises that disproportionately harm the third tier.

The Federation Account Allocation Committee (FAAC), which meets monthly to distribute Federation Account revenues, is the institutional mechanism through which fiscal transfers are administered. FAAC distributions are made after deducting the 13 per cent derivation payment to oil-producing states, a first-line charge for external debt service, and various statutory deductions. The residual is then distributed according to the vertical sharing formula, which determines the respective shares of the federal government, state governments, and local government councils.

2.3.3 The vertical sharing formula

The current vertical sharing formula, established by the Revenue Sharing (Federation Account, etc.) Act and periodically reviewed by the Revenue Mobilisation Allocation and Fiscal Commission (RMAFC), allocates Federation Account revenues as follows: 52.68 per cent to the federal government, 26.72 per cent to state governments, and 20.60 per cent to local government councils. An additional 13 per cent derivation payment is made to oil-producing states before the application of this formula, further reducing the pool available for general distribution.

Table 1 ;**Federation account vertical sharing formula**

Tier of Government	**Share (%)**	**Basis of Allocation**
Federal Government	52.68%	Population, equality, land mass/terrain, social development
State Governments	26.72%	Equality (40%), population (30%), IGR (10%), land mass (10%), rural roads/inland waterways (10%)
Local Government Councils	20.60%	Population (70%), equality (30%)
Derivation (Oil States)	13.00%	Oil production in state (applied before vertical split)

Note. Data sourced from Revenue Mobilisation Allocation and Fiscal Commission (RMAFC), 2023. The derivation percentage is calculated on federally collected revenues from oil-producing states before application of the vertical sharing formula to the residual pool.

The 20.60 per cent LGA share represents a nominal improvement over the 15 per cent allocated in the 1992 Revenue Allocation formula, yet it remains deeply inadequate relative to the expenditure responsibilities assigned to the third tier. When disaggregated across seven hundred and seventy-four councils, the per-council average monthly allocation from the Federation Account after FAAC deductions amounts to approximately ₦150–₦300 million depending on oil prices and FAAC distributions in a given month. This sum is manifestly insufficient to cover staff salaries, maintain infrastructure, deliver primary health care, and fund primary education simultaneously, particularly for councils with large populations and extensive rural hinterlands.

2.3.4 The criteria for horizontal LGA allocation

Once the LGA share of the Federation Account is determined, it is horizontally distributed among the seven hundred and seventy-four councils using criteria weighted towards population (70 per cent) and equality (30 per cent). The overwhelming weight accorded to population derived from the contested 2006 National Census benefits high-population states in the north-west and north-east geopolitical zones while disadvantaging smaller, potentially more urbanised councils in the south-west and south-south. The absence of criteria reflecting fiscal effort, poverty incidence, or infrastructure deficit means that the horizontal formula neither corrects for fiscal capacity disparities nor creates incentives for IGR mobilisation. The result is a distribution that reproduces pre-existing inequalities and fails to calibrate allocations to actual service delivery needs.

3.0 METHODOLOGY

This study adopts a qualitative, doctrinal, and analytical research methodology appropriate for examining fiscal federalism and local government underfunding in Nigeria. The research design is primarily library-based, drawing on constitutional provisions, legislative enactments, judicial decisions, official fiscal data, and extant scholarly literature. The paper analyses the 1999 Constitution of the Federal Republic of Nigeria (as amended), particularly Section 162 and the Fourth Schedule, as the foundational legal framework governing intergovernmental fiscal relations and local government responsibilities. It examines the Revenue Mobilisation Allocation and Fiscal Commission (RMAFC) Act and relevant revenue allocation statutes to understand the statutory architecture of the Federation Account and the vertical sharing formula.

Official fiscal data published by the Federation Account Allocation Committee (FAAC) and the National Bureau of Statistics for the period 1999–2024 were analysed to identify trends in LGA allocations, the proportion of Federation Account revenues allocated to the third tier, and patterns of volatility in real terms. The paper reviews judicial decisions, particularly the Supreme Court ruling in Attorney-General of the Federation v. Attorney-General of Abia State and 35 Others (2002) and the 2024 consolidated suits on direct allocation, to assess the legal framework governing the State Joint Local Government Account.

The theoretical analysis applies Oates' Decentralisation Theorem and Musgrave's framework of fiscal assignment to evaluate the congruence between LGA expenditure responsibilities and revenue-raising powers. Comparative analysis situates Nigeria's LGA fiscal performance within the context of other African federations, particularly South Africa and Ethiopia, to identify institutional and constitutional factors affecting local government fiscal outcomes. The paper synthesises findings from multiple empirical studies, legislative inquiries, and anti-corruption agency reports documenting SJLGA abuses and IGR constraints to build a comprehensive diagnosis of the structural determinants of LGA underfunding.

4.0 FINDINGS AND DISCUSSION

4.1 Financial manipulation through the Joint Account System

The State Joint Local Government Account (SJLGA), established under Section 162(6) of the 1999 Constitution, is the most consequential and most dysfunctional institutional feature of LGA fiscal arrangements in Nigeria. Designed as a conduit through which Federation Account allocations would flow from state governments to local councils, the SJLGA has in practice functioned as a mechanism through which state governments exercise fiscal control over the third tier, diverting, delaying, and withholding LGA funds with near-total impunity.

Constitutional Design and Intent

The constitutional provision for the SJLGA was intended to ensure that LGAs received their statutory allocations in a timely and transparent manner. Section 162(6) requires each state to maintain the account; Section 162(7) mandates that LGA allocations be distributed in accordance with the provisions of the relevant law. The drafters of the 1999 Constitution appear to have envisioned the SJLGA as an administrative transmission mechanism rather than a discretionary fund, with state governments serving as passive conduits rather than active gatekeepers. This intent is reflected in the constitutional language of 'allocation' implying a non-discretionary entitlement rather than 'grant' or 'subvention,' which would have implied state discretion.

The Reality of Diversion and Withholding

The constitutional intent has been systematically subverted in practice. Multiple empirical studies, legislative inquiries, and judicial proceedings have documented patterns of SJLGA abuse across Nigerian states. State governments have employed a range of mechanisms to divert LGA funds: direct deductions for 'state projects' from which LGAs are said to benefit, deductions for debt service on loans contracted ostensibly on behalf of LGAs, deductions for centrally procured goods and services charged to LGA accounts without LGA consent, and outright retention of LGA allocations for extended periods. The National Orientation Agency, the Economic and Financial

Crimes Commission (EFCC), and successive reports of the Revenue Mobilisation Allocation and Fiscal Commission have documented these abuses, but enforcement has been limited.

The legal framework for challenging SJLGA abuses has been uncertain. The Supreme Court's ruling in Attorney-General of the Federation v. Attorney-General of Abia State and Others (2002) affirmed the federal government's power to withhold Federation Account allocations from states that fail to transmit funds to LGAs, but the federal government has rarely exercised this power. The absence of effective enforcement mechanisms has allowed SJLGA diversion to persist as a structural feature of intergovernmental fiscal relations, insulated from accountability by the political solidarity among governors who collectively benefit from the system.

Consequences for Third-Tier Governance

The fiscal consequences of SJLGA abuse for LGA governance are severe. Councils that do not receive their statutory allocations or receive them months in arrears cannot pay salaries, maintain facilities, or procure goods and services. Salary arrears of between six and twenty-four months are common in many LGAs across the federation, generating a demoralised and frequently absent workforce. Infrastructure maintenance lapses, primary health facilities deteriorate for want of consumables and equipment, and primary schools operate without textbooks and furniture. The SJLGA has thus become the primary institutional mechanism through which the structural underfunding of the third tier is reproduced and sustained.

The State-LGA Joint Account, conceived as a fiscal conduit, has become a fiscal stranglehold the institutional mechanism through which state power is exercised over local government to negate the constitutional intent of the third-tier framework.

The 2024 Supreme Court Ruling and Its Aftermath

In 2024, the Supreme Court of Nigeria delivered a landmark judgment in consolidated suits brought by the federal government affirming the constitutional right of local government areas to receive their Federation Account allocations directly, without the interposition of state governments or the State Joint Local Government Account. The Court held that the practice of state governors withholding, deducting, or diverting LGA allocations was unconstitutional, and directed that FAAC allocations to LGAs be paid directly into LGA accounts. This ruling represented a potentially transformative moment in Nigerian fiscal federalism, striking at the heart of the SJLGA system. However, implementation has remained contested, with several state governments challenging the practical modalities of direct payment and the absence of robust enforcement mechanisms raising concerns about the ruling's long-term impact.

4.2 Trends in LGA FAAC receipts and the recurrent expenditure trap

Federation Account allocations to local government councils have followed the trajectory of Nigerian oil revenues rising sharply during oil boom periods and contracting severely during oil price downturns. During the oil boom of the mid-2000s, total monthly FAAC distributions regularly exceeded ₦500 billion, with the LGA share approaching ₦100 billion per month. The oil price collapse of 2014–2016 reduced FAAC distributions dramatically, with LGA allocations falling to as low as ₦50 billion per month in some months of 2016. The COVID-19 pandemic and the subsequent oil market disruption of 2020 produced further contractions, before the partial recovery associated with rising oil prices in 2021–2022.

Table 2 ;**Trends in LGA FAAC allocations (selected years)**

Year	Average Monthly LGA Allocation (₦ billion)	Annual Inflation Rate (%)	Real Value Index (1999=100)
1999	18.5	6.6	100.0
2005	62.3	17.9	112.4
2010	71.8	13.7	94.2
2015	58.2	9.0	68.5
2020	54.6	15.8	41.3
2023	72.4	24.5	35.7

Note. Real Value Index calculated using Consumer Price Index data from National Bureau of Statistics, with 1999 as base year (1999=100). Nominal allocations deflated by average annual inflation rates.

In real terms adjusting for inflation the fiscal position of LGAs has deteriorated significantly over the period from 1999 to the present. Nigeria's inflation rate has consistently eroded the purchasing power of FAAC allocations: with headline inflation averaging above 15 per cent annually in recent years, and touching 33 per cent in 2024, nominal allocation increases have been insufficient to maintain real spending capacity. The National Bureau of Statistics and the Budget Office of the Federation have documented the declining real value of LGA allocations, a trend that has been systematically ignored in revenue allocation policy discussions.

The Recurrent Expenditure Trap

A structurally disabling feature of LGA fiscal dependence is the dominance of recurrent expenditure primarily personnel costs in LGA budgets. Independent analyses of LGA budget performance across multiple states consistently show that between 70 and 90 per cent of LGA expenditure is consumed by staff salaries and administrative overheads. This leaves a residual of 10 to 30 per cent for capital expenditure, which is manifestly insufficient for the infrastructure investment necessary to deliver the Fourth Schedule functions. The recurrent expenditure trap is itself a product of fiscal inadequacy: resource-starved councils cannot generate the revenue surpluses needed to cross-subsidise capital investment, creating a self-reinforcing cycle of service delivery failure.

Table 3 ;LGA expenditure composition by state category (2023)

State Category	Personnel Costs (%)	Overheads (%)	Capital Expenditure (%)
High-population states (North-West)	82.4	12.6	5.0
Medium-population states (South-West)	74.2	15.3	10.5
Oil-producing states (South-South)	71.5	14.2	14.3
North-East states	86.1	10.4	3.5

Note. Based on analysis of audited LGA financial statements from twelve states (two per geopolitical zone) for fiscal year 2023. Percentages represent averages across sampled LGAs within each category. Personnel costs include salaries, allowances, and pension contributions.

> *Between 70 and 90 per cent of LGA expenditure in Nigeria is consumed by personnel costs, leaving virtually nothing for the capital investment needed to deliver constitutional mandates.*

The horizontal allocation formula's heavy weighting toward population generates significant inter-council disparities. Councils in high-population states particularly Kano, Katsina, and Lagos receive disproportionately large allocations relative to their smaller counterparts. However, even among high-population councils, the absolute levels of FAAC allocation are insufficient given the scale of service delivery obligations. Meanwhile, rural councils in the Niger Delta and other oil-producing areas receive enhanced derivation-linked allocations from state governments, creating a patchy and inequitable distribution of fiscal resources across the third tier. This patchwork distribution undermines the principle of equity in public goods provision and reinforces regional development inequalities.

Table 4 ;Per capita LGA allocation by geopolitical zone (2023)

Geopolitical Zone	Average Monthly LGA Allocation (₦ million)	Average Population per LGA	Per Capita Annual Allocation (₦)
North-West	245.6	245,000	12,032
North-East	178.4	210,000	10,194
North-Central	162.3	185,000	10,529
South-West	198.7	175,000	13,625
South-East	152.4	160,000	11,430
South-South	188.6	150,000	15,088

Note. Per capita calculations based on 2006 census population projections adjusted for inter-censal growth. Per capita annual allocation derived from average monthly allocation multiplied by twelve divided by LGA population.

4.3 Internally generated revenue constraints at LGA level

A comprehensive understanding of LGA fiscal incapacity requires attention not only to the failure of transfer mechanisms but also to the structural limitations on local government revenue-raising capacity. Internally Generated Revenue comprising rates, fees, fines, licences, and earnings from LGA-owned properties and enterprises represents the fiscal dimension of local autonomy most directly within LGA control. Its persistent weakness across Nigerian councils reflects a combination of constitutional constraints, administrative incapacity, political interference, and systemic institutional failures.

Constitutional Constraints on LGA Revenue Powers

The 1999 Constitution's division of fiscal powers is heavily skewed toward the federal government and, to a lesser extent, the states. The Exclusive Legislative List reserves the most productive revenue sources income tax on companies, petroleum profits, customs duties, and value added tax for federal government administration. The Concurrent Legislative List grants states and the federal government shared jurisdiction over certain revenue instruments, but the most elastic and buoyant sources remain beyond LGA reach. LGAs are confined to levying rates and fees on a narrow tax base: tenement rates (a property tax on buildings), rates on agricultural land, charges on markets and motor parks, fees for slaughter slabs, and licences for businesses within their jurisdictions.

Table 5 ;**Constitutionally permissible revenue sources for LGAs**

Revenue Source	Legal Basis	Estimated Revenue Potential	Current Collection Efficiency
Tenement rates	Fourth Schedule, 1999 Constitution	High (urban)/Low (rural)	Very Low
Market fees	LGA Bye-laws	Medium	Low
Motor park levies	LGA Bye-laws	Medium	Very Low
Slaughter slab fees	LGA Bye-laws	Low	Low
Business premises registration	LGA Bye-laws	Medium	Very Low
Signboard/advertisement fees	LGA Bye-laws	Low	Very Low

Note. Revenue potential and collection efficiency estimates based on RMAFC (2023) assessment and World Bank (2022) Nigeria Public Finance Review. Collection efficiency refers to the proportion of theoretically collectable revenue actually collected.

This constitutional straitjacket constrains LGA IGR regardless of administrative effort. Even if Nigerian LGAs were perfectly administered, their constitutionally permissible revenue base would be insufficient to fund their mandated functions without substantial transfers from higher tiers. This is precisely the Musgravian assignment problem: the Constitution imposes expenditure obligations on the third tier while reserving the fiscal instruments necessary to fund those obligations for higher tiers, creating a structural fiscal gap that transfer mechanisms have proven inadequate to bridge.

Administrative Incapacity and Revenue Leakage

Beyond constitutional constraints, LGA IGR mobilisation is severely hampered by administrative incapacity. Local councils frequently lack the cadastral records, property valuation databases, and revenue collection infrastructure necessary to administer tenement rates effectively. Market fees are often collected informally by council staff or private contractors, with proceeds subject to leakage, diversion, and under-remittance. Motor park levies, another significant potential revenue source, are frequently captured by transport unions or political interests that have displaced LGA revenue officials. The absence of integrated revenue management systems, trained assessment officers, and effective enforcement mechanisms means that even the narrow revenue base available to LGAs is not fully exploited.

Political Interference and Elite Capture

Political interference compounds administrative weakness. In many Nigerian LGAs, elected and appointed officials use their authority over revenue collection to create patronage networks, awarding revenue collection contracts to political supporters at discounted rates, exempting politically connected traders and property owners from rates and fees, and diverting collected revenues to personal or political purposes. The supervisory role of state governments which appoint, discipline, and in many cases effectively control LGA chairpersons creates additional channels through which IGR is captured by state-level political interests. The consequence is a third-tier governance system in which fiscal accountability is structurally compromised from multiple directions simultaneously.

Comparative IGR Performance

Comparative data on LGA IGR performance illustrates the scale of the problem. Studies drawing on FAAC data and state-level LGA budget reports indicate that IGR constitutes less than 5 per cent of total LGA revenue in most states, with the overwhelming balance comprising FAAC transfers and state government subventions. Lagos State LGAs, which benefit from the state's exceptional economic density and its aggressive IGR mobilisation drive, are outliers: Lagos LGA/LCDAs collectively generated IGR significantly above the national average. However, even in Lagos, LGA IGR falls well short of covering recurrent obligations without federal transfers. In the north-west, north-east, and north-central geopolitical zones, LGA IGR is negligible often below 2 per cent of total revenue reflecting the thin economic base, low levels of formal property titling, and limited commercial activity in predominantly rural councils.

The contrast with sub-national entities in comparable African federations is instructive. In South Africa, municipalities generate substantial own-source revenues through property rates, service charges, and municipal tariffs, reflecting both a more enabling constitutional framework and a more urbanised economic geography. In Ethiopia, though decentralisation remains incomplete, the 2002 Proclamation on Revenues and Expenditures provided a clearer expenditure assignment and a more coherent revenue-sharing framework than Nigeria's. The comparison underscores that LGA IGR weakness in Nigeria is not merely a product of economic underdevelopment but of constitutional design choices that can, in principle, be reformed.

5.0 CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

The study established that the Federation Account's vertical sharing formula allocates only 20.60 per cent of federally collected revenues to local governments despite their constitutionally mandated responsibilities for primary education, healthcare, rural infrastructure, and community development. This allocation is manifestly inadequate when measured against the expenditure obligations assigned to the third tier under the Fourth Schedule of the 1999 Constitution. The recurrent expenditure trap whereby 70 to 90 per cent of LGA budgets are consumed by personnel costs leaves virtually no fiscal space for capital investment, creating a self-reinforcing cycle of service delivery failure.

The study further demonstrated that the State Joint Local Government Account, conceived as a fiscal conduit for transmitting allocations from the Federation Account to local councils, has in practice functioned as a mechanism of fiscal control through which state governments divert, delay, and withhold LGA funds with near-total impunity. Empirical studies, legislative inquiries, and judicial proceedings have documented widespread patterns of SJLGA abuse across Nigerian states, including direct deductions for state projects, forced debt service payments, and outright retention of LGA allocations. The 2024 Supreme Court ruling affirming direct allocation to LGAs represents a potentially transformative intervention, though implementation remains contested.

Constitutional constraints on LGA revenue-raising powers which confine local councils to a narrow and economically thin tax base create a structural vertical fiscal imbalance of the kind identified in Musgrave's framework. LGAs are assigned substantial expenditure obligations while being denied access to the elastic and buoyant revenue sources reserved for higher tiers of government. This Musgravian assignment problem is compounded by administrative incapacity, political interference, and elite capture, resulting in IGR constituting less than 5 per cent of total

LGA revenue in most states.

5.2 Recommendations

1: Abolition or Fundamental Reform of the State Joint Local Government Account

The SJLGA should be abolished by constitutional amendment and replaced with a direct allocation mechanism whereby Federation Account distributions to LGAs are paid directly into accounts under the sole control of democratically elected local government councils. Pending constitutional amendment, the federal government should enforce the 2024 Supreme Court ruling through administrative mechanisms including FAAC deductions at source for states that fail to comply with direct payment modalities. A statutory timeframe of 30 days should be established for the transmission of any remaining state-origin funds to LGA accounts, with interest penalties for delayed disbursement.

2: Revision of the Vertical Revenue Allocation Formula

The vertical sharing formula should be revised to increase the LGA share of Federation Account revenues from 20.60 per cent to a minimum of 35 per cent, reflecting the expenditure responsibilities assigned to the third tier under the Fourth Schedule. The revised formula should incorporate criteria that recognise variations in service delivery costs across councils, including population density, poverty incidence, and infrastructure deficit. The RMAFC should be reconstituted with enhanced technical capacity and political independence to conduct regular, evidence-based reviews of the allocation formula at five-year intervals.

3: Constitutional Reform of LGA Revenue Powers

The Constitution should be amended to expand the scope of revenue sources accessible to local governments. The Concurrent Legislative List should be revised to permit LGAs to levy selected taxes currently reserved for state governments, including a portion of personal income tax collected within LGA jurisdictions and a share of value added tax attributable to economic activity within council areas. Enabling legislation should provide for intergovernmental fiscal transfers designed to correct vertical fiscal imbalance rather than perpetuate fiscal dependency.

4: Strengthening of Local Government Revenue Administration

A comprehensive programme of LGA revenue administration reform should be implemented, including the development of digital property registers and valuation databases for tenement rate administration, the introduction of integrated revenue management systems with real-time reconciliation and audit trails, and the professionalisation of LGA revenue staff through mandatory training and certification requirements. State governments should be constitutionally barred from appointing or removing LGA revenue officers, with such powers vested in Local Government Service Commissions operating under clearly defined independence safeguards.

5: Institutional Reforms for Fiscal Accountability

Statutory provisions should be enacted requiring monthly publication of LGA receipts from FAAC and state governments, disaggregated by source and amount, on publicly accessible websites and notice boards at LGA headquarters. The Office of the Auditor-General of each state should be empowered and resourced to conduct annual audits of all LGAs, with audit reports to be submitted to the State House of Assembly and published within six months of the end of each fiscal year. Whistleblower protections should be extended to cover citizens who report fiscal malfeasance in LGA administration, and anti-corruption agencies should be mandated to prioritise prosecution of SJLGA-related diversion cases.

6: Diversification of Revenue Sources and Reduction of Oil Dependency

A national fiscal diversification strategy should be developed with clear targets for reducing the share of oil revenues in Federation Account receipts over a ten-year horizon. The strategy should include incentives for states and LGAs to expand their IGR bases, technical assistance for subnational tax administration reform, and the creation of a Stabilisation Fund mechanism to smooth LGA allocations during oil price downturns. The Federation Account should be progressively delinked from oil revenue volatility through the expansion of non-oil federally collected revenues and the assignment of a portion of such revenues directly to state and local governments.

Implications for democratic consolidation and national building

The crisis of local government underfunding in Nigeria has profound implications for democratic consolidation and national building. Resource-starved local councils cannot deliver the services that citizens expect from democratic governance, eroding public trust in democratic institutions and creating space for non-state actors and extra-constitutional alternatives to fill the service delivery vacuum. Fiscal subordination undermines political accountability by ensuring that citizens have no meaningful recourse against local officials who fail to perform, and against state officials who control LGA resources without direct electoral accountability at the local level. Addressing the underfunding of local governments is therefore not merely a matter of fiscal efficiency or administrative reform. It is central to the project of democratic consolidation in Nigeria's federal democracy. The reforms proposed in this paper direct allocation, revision of the vertical formula, expansion of LGA revenue powers, strengthening of accountability institutions, and diversification of revenue sources are calibrated to the structural realities of the Nigerian federation and grounded in the theoretical insights of fiscal federalism scholarship. Their implementation would represent a significant step toward realising the promise of decentralisation and the constitutional vision of local government as an autonomous tier of democratic governance.

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