London Study Tour Report

12th -19th February 2012

Revenue Mobilisation Allocation and Fiscal Commission (RMAFC)

The Presidency

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1.0 INTRODUCTION

The RMAFC senior management team of twenty staff led by T K Kasali, Secretary to the Commission visited London from the 12th February – 19th February 2012, at the invitation of the London Knowledge Innovation Centre (LKIC) in collaboration with the Institute of Public Policy Analysis & Management and Fortunegate Consulting .

2.0 PROGRAMME

The study tour programme included visits to some key developments and two days of experience based workshops conducted by the LKIC.

Included in the visit programme was a visit to the O2 arena which provides a significant example of the very high costs incurred by UK Central Government in creating a showpiece public arena for a one-off event and not properly planning for its subsequent maintenance and long term use. After several years with O2 being empty the arena was finally converted into an entertainment venue by an American leisure company and is now the most successful concert arena in the World. It will also become one of the venues for the London 2012 Summer Olympics.

Another visit was made to the Westfield East Shopping Centre which adjoins the London 2012 Summer Olympics site at Stratford. This extremely large and successful covered shopping centre was entirely planned, financed, built and managed by international retail developers. Government created the infrastructure framework only.

The study tour also included LKIC, which is leading knowledge based incubation centre that helps high growth businesses to start-up, grow and prosper. LKIC's client knowledge based industries are critical for London's future economic growth. LKIC attracts local and entrepreneurs from all over the world to start their businesses in London where they enjoy a very high business success rate.

Innovation is seen by LKIC as being key to the modern global economy, with the need to take into account the quickening pace of change and how many new highly successful global businesses have adopted "blue ocean strategies" adding considerable value added to the base cost of their products.

Information gained from these visits was able to used during the main workshop sessions which were directed towards four main areas:

- Fiscal Transparency and Accountability
- Management of Natural Resource Revenue (Oil and Gas)
- Intergovernmental Fiscal Relations
- Revenue Forecasting

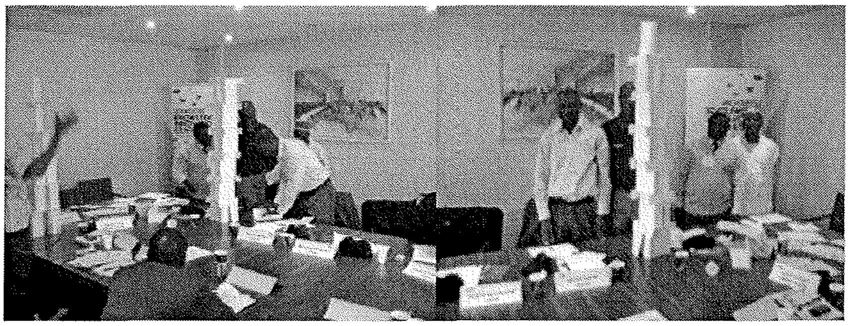
In order to fully exploit the benefits of the study tour to better promote the important work of the RMAFC and share collaborative experience with current practices in the UK preparatory interactive sessions were conducted. These sessions concentrated on introducing and developing the use of team based ideation techniques applied to interactive problem solving exercises. The techniques draw upon the latest approaches to generating sustainable innovation through ideation to help generate new directions in thinking and stimulate "outside the box" solutions for organisations.

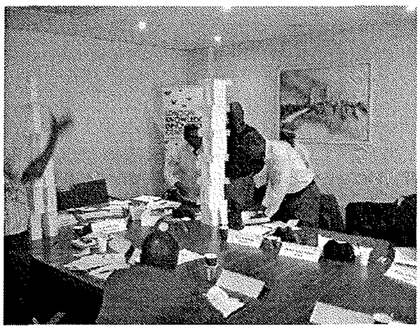
3.0 OUTCOMES

3.1 Ideation exercises

The group session covered a wide range of warm-up exercises and techniques. In one warm –up session the group spilt into four teams and had to construct a paper tower without any glue or fastenings using only 34 sheets of plain paper within a time constrained period.

Three of the groups produced physical structures of 147cm, 126cm and 63cm in height. Pictures of the exercise are shown below:





The outcomes of the exercise compared well with other groups in terms of the groups being able to work together to solve new and challenging problems in a time constrained context.

The application of the ideation techniques approach to the work of the RMAFC was covered in two interactive group based sessions covering two problem areas identified by the group, the raising of additional revenue and the creation of new taxes.

The results of the two sessions are shown below:

RMAFC Study Tour - 15 February 2012

Group Problems

Raising New Taxes

1. Inheritance Tax

   (Beneficiary has not worked)

   1.1 Problems:

   - Social and religious
   - No data
   - Legal status not defined
   - Who collects it?
   - What are the benefits?
   - What will be the Net Marginal Income?
   - How will it be allocated?

2. Tenement Rate

   (Tax on property)

   2.1 Problems:

   - Little legal framework
   - No database
   - Assessment difficult
   - Who has the income?
   - Cultural aspects
   - Local government collection?
   - Lack of political will
   - No capacity to assess and collect
   - State to act
   - Enlighten tax payers about the benefits of the tax in terms of services
   - Tax payers see no obvious benefits

3. Parking Space

   (Taxes on car parking spaces

   Tax vehicles using cities and congested areas)

   3.1 Problems:

   - Acceptability?
   - Level of tax
   - Undercharging for real cost
   - Establish in Lagos and Abuga
   - Extend to all areas
   - Create a database
   - Collection by pre-paid parking permit maybe more cost effective

Creating Additional Revenue - 16 February 2012

Group 1

2. Revenue Census - survey
3. Short-term money earning projects
4. Enhance infrastructure (tourism)
5. SME development
6. Compliance, assessment and collection

Group 2

1. Database
2. Agricultural mechanisation and investment
3. Informal sector involvement
4. Tourism
   - Security
   - Renovation
   - Admin support
5. Training and marketing

Group 3

1. Land speculation tax
2. Mobile handset tax
3. Database – compliance

Group 4

1. Simplified tax for small businesses
2. Create centres of excellence (health, education and research & development etc)
3. Improved attitude of tax payer
4. Justify benefits of taxation
5. Include informal sector
6. Many existing taxes not collected, so enforce collection
7. Reward people for paying taxes
8. Institute self-assessment of tax to increase tax collection and payment
9. Motivate states to spend less

Group 5

1. Property tax
2. Environmental tax (cars and phones)
3. Facilitate investment to create employment
4. Mine solid minerals
5. More HRD investment
6. Encourage private partnerships with public sector
7. Promote tourism and hospitality
8. Avoid duplication of admin costs
9. Amend constitution
10. Create a better revenue-sharing framework

3.2 Revenue Forecasting

The study team first went through the UK public finance position concentrating on the work of the independent, Office for Budget Responsibility (OBR), which is a fairly recent institution (created in 2010) under the Treasury (UK equivalent of a ministry of finance). It was established to create greater transparency through publishing five year **forecasts** on the UK economic and fiscal outlook (twice a year) linked to an annual evaluation of those forecasts to improve the techniques they use in forecasting. **Judgement** is also made by the OBR against the fiscal targets set by the Treasury. They establish if there is a 50%+ possibility of the Treasury meeting its targets? The robustness of the judgement is also critically looked at, given the uncertainty inherent in all fiscal forecasts. The focus of these activities is forward looking to 2015-16 and not (say) the current budget year.

In addition, the OBR looks at the **long - term sustainability of public finances** and publishes an annual fiscal sustainability report which looks forward 50 years in advance.

The OBR has a fourth role and that is to scrutinise the Treasury's costings of all the measures in the annual budget prior to the budget being finalised and then when they are satisfied they publicly endorse the budget forecasts which are also published for the general public.

A key concept of the revenue (and expenditure) forecasting and fiscal sustainability of the UK is the creation of Whole Government Accounts (WGA) which consolidates the assets and liabilities of some 1500 public bodies in the UK into one document that shows all public sector assets and all public sector liabilities. In the UK for 2009-10 this has shown Net Liabilities of £1212bn, representing 86% of GDP. This clearly provides the framework for the need of taxed based revenue linked to management of future public expenditure and borrowing to cover budget deficits.

The OBR use a mix of revenue forecasting techniques Including: judgemental, consensus, time series, casual models and quantitative forecasting with qualitative modification.

The WGA approach does not exist in Nigeria but would greatly benefit the basis for future budgets if it was in place. The lack of a proper dataset in Nigeria clearly limits RMAFC's abilitiy to carry out fiscal forecasting. Whilst oil export revenues constituted 95.3% of all Nigeria's export revenues in 2010 there are some thirty-four solid minerals that exist in Nigeria that need to be considered as alternative sources of the revenue. The need to look at alternative revenue needs to be looked at critically given the very expensive federal , regional, state and local government institutions, the growing trend in the increased import of finished goods and the challenging demographic circumstances.

The critical need for the RMAFC to be able better forecast likely fiscal trends and make timely suggestions for changes needs to viewed in the context of the national economy being more like a giant super tanker that cannot suddenly change its course but has to go through a long series of carefully planned manoeuvres before it can go in a different direction and reach a new destination.

3.3 Intergovernmental Strategies and Resource Utilisation

The study team briefly looked at the challenges of inter-governmental fiscal relations and identified some common problems:

1. Lack of Formal and Clear Assignment of Roles: With the need for written functional responsibilities in the context of a well defined framework. Government must never leave something unclear or ill-defined. Sufficient authority must be given commensurate with responsibility.

2. Inefficient Assignments: where do capital projects and social protection belong?

3. Ambiguity in assignments

4. Co-sharing of responsibilities. Education responsibilities can be at a number of levels of government

5. Neglect of expenditure responsibilities is very common as the main concentration is often on revenue.

Measures that could be adopted on the **expenditure** side include: formal assignment by law; reassignment of selected expenditure responsibilities particularly capital; give responsibility closest to the point of delivery and establish a co-ordinated national policy to facilitate the divestiture of social responsibilities. The measures need to address minimum standards and include measureable outcomes, outputs, key milestones and show value for money. Measures also need to be linked to sector policies in key areas.

Measures that could be included on the **revenue** side include: sub-national governments generating their own revenues at sufficient levels vis-a vis their expenditure demand; sub-national governments must have their own marginal revenue sources; revenue and its collection must be assigned to the lowest level relative to its benefit and there could be variable sub-national surcharges.

3.4 **Managing Natural Resource Revenues (Oil and Gas**)

The study team reviewed Nigeria's experience:

- Federation primarily a mechanism to distribute centrally controlled petroleum sector revenues;
- Potentially decentralisation can encourage policy innovation and help to promote national stability, development and democracy;
- In practice this has not happened. It has created a corrupt and often violent system of political patronage with widespread pre-occupation with revenue sharing and not creating an efficient, effective and equitable public and fiscal policy strategy

Reasons for the current failure can be attributed to:

- Framework is defective
- Lack of transparency and short-changing of states and local government
- Sub-national authorities lack an incentive to raise revenues themselves.
- Legal obstacles (80/20 Rule)
- Unequal distribution causing inequality
- Misuse of funds by states (eg Niger-Delta)
- Reforms lack transparency and leave power in the hands of elite political class- that transparency measures need to contain.

Future policy needs to take into account:

- Oil extraction model- long term wealth maximisation or target revenue (match to budget).
- Petroleum fiscal system used: service fee system (no foreign ownership); production sharing (sharing revenues) and concession system (royalties paid European, N.America and Australia)
- Stabilisation Funds: set aside a portion of income for national fiscal reserves (Norway) needs strong control
- Inter-Generational Funds: set-up to share oil income for future generations (Alaska, Chad, Kuwait) also needs strong control

Nigeria has just started with its own fund. The funds set aside in other countries are shown below and some are massive where countries have decided not to use a lot of petroleum sales for government budgets, but are saving and investing for the future.

Country	Inception	Value US$ bn
Kuwait	1960	65
Alaska	1976	27.4
Norway	1990	82
Iran	1999	1.2
Venezuela	1999	3.7
Oman	1980	2

Another way of achieving an inter-generational fund is not to produce so much oil and gas and keep the reserves in the ground.

The considerable practical problems of revenue sharing petroleum revenues in Nigeria would it appear need constitutional changes change but until these problems are solved the production of other minerals may create new and more complex revenue sharing problems.

The Need for Fiscal Transparency

The study team looked at the UK and international approaches to create fiscal transparency and reviewed the situation of the RMAFC in Nigeria, which was set-up in Nigeria way ahead of when similar institutions have been established in other countries. The role of the RMAFC clearly reflects the needs of the Federation following the Richard's Constitution in 1946 and its current powers and independence deriving from the 1999 Constitution.

The rationale for the OBR in the UK included:

(i) Democratic governments prone to 'deficit bias' and 'pro-cyclicality' in management of the public finances

(ii) Possible sources of deficit bias

- Differential access to information
- Impatience
- Electoral competition
- 'Common pool' problems
- Use for macroeconomic management
- Exploiting future generations

(iii) Public mistrust of the government and management of public finances

The UK situation has to deal with corruption at all levels. Part of the approach is create transparency in all public arenas through regular dissemination of information at all levels and using a wide variety of media by organisations like the OBR. Through providing good quality and up to date information this then makes it much easier for corruption to be detected. When potential corruption is spotted in the public sector immediate action is taken to investigate and bring the culprits to public trial if they have broken the law. This process has to be seen to be done to create confidence in the public sector.

In the context of the OBR they are independent of politicians and make a strong effort to explain to the public why governments have to tax, spend and lend and why governments have to borrow and linked to providing an objective account of the current state of the economy and future plans and potential opportunities and problems. This is critical to help to get public support for necessary fiscal measures that have to be introduced by government.

In contrast the role of the RMAFC in Nigeria is to: monitor accruals into and disbursements from the Federation Account; reviews revenue allocation formulae; advise government on fiscal efficiency and methods for increasing revenue; determine remuneration of political office holders plus other key functions. Like the OBR in the UK the RMAFC is autonomous and is only advisory and does have the direct power to take action (ie cutting salaries). However, it has a very challenging operational role because of secrecy, fraud and corruption in accounting for key expenditure revenue, with even key oil revenues paid into a Morgan Stanley Bank Account by NNPC and not Federation Account as well as the NNPC making illegal deductions from these revenues? In the context of the oil revenues what is not clear to the public is what income is received and how it is distributed throughout the country. The use of allocation percentages in various debates is misleading because the size of the cake is not quantified to make the percentages quoted meaningful.

3.5 **Intergovermental Fiscal Relations**

A key feature of the situation in Nigeria is the Federal Government is responsible for the allocation of oil revenues to sub-national governments but the Federal Government, through the RMAFC is not legally allowed to check on how the money is used or to require the sub-national governments to generate their own revenue.

Clearly this situation prevents the RMAFC from carrying out one of its key roles to monitor accruals into and disbursements from the Federation Account and undermines future fiscal sustainability.

Accepted good practice is that sub-national governments should be given adequate resources to carry out their responsibilities but at the same time they must be fully accountable for the use of those resources. Without this basic transparency the RMAFC cannot discharge its constitutional duties.

4. **Future Support for the RMAFC**

In order to further support the important role that the RMAFC has to undertake in Nigeria we would like to offer the following:

1. Training needs analysis of staff;
2. Developing specialist staff training programmes that were linked to UK based and internationally recognised qualifications;
3. Developing a multi-media communications strategy for the RMAFC to better provide fiscal information so as to create awareness and hence improve fiscal transparency and to better promote the public's awareness of the RMAFC;
4. Developing systems and related training for the organisations that provide information to the RMAFC so that a better data set can be assembled and linked to the building of socio economic models to develop independent forecasts of fiscal sustainability.
5. Further developing an innovation based leadership culture throughout the RMAFC so that is better able to discharge its responsibilities and become more influential as an advisory body.

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20th February 2012