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Chapter 9

Lessons in fiscal federalism for Somalia

Building fiscal sustainability and national cohesion

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9.1 Introduction

Federal or decentralised systems are not 'one-size-fits-all' arrangements. They cannot be regarded in essence as either beneficial or harmful; nor are they the answer to all governance problems. The solution to these depends both on an institutional design that responds to critical challenges faced by a particular country and on the political will to make that design work successfully in the context of existing political forces.[1]

With that noted, federal or decentralised systems have proven useful in managing diversity and resolving political conflict. They have helped ensure the fair distribution of resources and the deepening of democracy and rule of law, particularly once the relevant local context has been taken into account.[2] This is so because diversity or conflict manifests itself in such forms as regional economic imbalance, clan-based mobilisation, and regionalism.[3]

Similarly, the perennial conflict in Somalia can be attributed to state and institutional failure, clannism, and regionalism, all of which make the prospect of restoring order a daunting task. Consequently, as is the case in many African countries, Somalia has embarked on the creation of a federal structure that could address these problems.

As the country ponders the question of what a meaningful system of the federation would be, a central question is whether the current fiscal arrangement provided by the 2012 Provisional Constitution is adequate. Could it help in the implementation of a system that ensures an equitable distribution of national financial resources?

The chapter examines this key question by analysing the scholarly literature on fiscal federalism and examining how Somalia's Provisional Constitution identifies the basic features of fiscal federalism. In so doing, the chapter focuses on major issues of institutional architecture, including the assignment of functions and revenue sources, the question of natural resources and intergovernmental transfers, and the nature of managerial capacities involved in decentralisation. It is argued that important lessons can be drawn from the literature on fiscal federalism and applied in Somalia to address conflicts around autonomy, equity, political stability, and intergovernmental relations.

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The chapter is divided into four sections. The first is the present introduction; the second examines the political background of Somalia's federal structure, while the third presents the theoretical framework of and rationale for fiscal federalism. These initial discussions lay the foundations for the analysis in the final section, which engages with the design of Somalia's Provisional Constitution and its implications for fiscal federalism. In this analysis of the constitutional design of fiscal federalism (and the related assessment of various constitutional lacunae), the study identifies some valuable fiscal lessons that should be borne in mind in an attempt to institutionalise a full-fledged federal system in Somalia.

9.2 The political background to Somalia's federal structure

Somalia, located in the north-eastern region of Africa known as the Horn of Africa,[4] is one of the most homogeneous countries on the continent.[5] It was declared an independent state in 1960 when it arose from a union of British and Italian Somaliland. After the fall of President Siad Barre in 1991, it descended into conflict and insecurity; within months, the national state and its institutions collapsed. The governance of various regions was taken over by warlords with armed clan militias, while control of the capital, Mogadishu, was divided along clan and sub-clan lines. The armed conflict resulted in the loss of life, destruction of property, and human displacement on a scale unprecedented in Somali history.

In 1991, Somaliland declared independence (though this was not recognised by the international community), and in 1998 Puntland followed suit. These two regions are relatively stable and enjoy constitutions, elected parliaments, presidents, courts, and other public institutions. Meanwhile, the rest of the country remained volatile, with control shifting between warlords, the Union of Islamic Courts (UIC), al-Shabaab, and foreign militias.

A number of peace processes were brokered by the international and regional community, all aimed at security, state reconstruction, and nation-building, while military interventions were mandated by the African Union (AU), the Intergovernmental Authority on Development (IGAD), and the United Nations (UN). These efforts led to multiple transitional arrangements and culminated in the formation of the Federal Government of Somalia (FGS) in 2012.[6]

The present federal government was formed after Somalis held their first post-civil war election in September 2012. It is mandated by the Provisional Constitution, which was approved in August 2012 by the 824 members of the Constitutional Assembly, a body established by means of a clan-representation formula. With regard to governance, the Constitution provides for a blend of parliamentary and presidential systems. The President is elected by a minimum of two-thirds of the members of the two federal houses, who vote together in a special joint session. He appoints a Prime Minister, who in turn appoints cabinet members in consultation with him. Executive power is divided between the President and Prime Minister (leading at times to a power struggle between them). Parliament is given the power to either approve or reject the cabinet and its programme of action.

As in other federations, the central aims of Somalia's federal system are to seek unity through diversity, strengthen the economy, ensure the fair distribution of resources, and maintain peace and security throughout the land. It is, however, important to bear in mind the particular circumstances of Somalia's acceptance of a federal system.

With regard to diversity, while almost all Somalis speak the same language and practise the same religion, namely Islam, individuals have strong allegiances to the clan system and hold to the cultural differences between clans. Fiseha is hence correct to argue that diversity in Somalia has unique characteristics and that they should be taken into account when considering the role federalism can play in Somalia. He observes that

> [t]hough Somalia is perceived as constituting a single ethnic group speaking same language and practicing Islam, the clan structure remains a primary source of affiliation and basis for political action just like ethno-nationalist mobilization is in other parts of [Africa]. It appears to [outweigh] class, religion or other forms of socio-political mobilization.[7]

Lack of security and political stability have fuelled the country's economic and fiscal challenges, while prolonged conflict and the devastation inflicted on public institutions have led to a dismally low level of public service provision. Although pastoral and rain-fed agriculture is the backbone of the economy, international assistance and remittances from the Somali Diaspora play a significant role as well.

As a result of these factors, the system of government is constrained by a variety of issues not addressed as such by the Constitution. While some of them have been left for further negotiation (among them questions regarding taxation and the basis for creating states), others require the establishment of institutions and the assurance of security. For the moment, the federalisation process is incomplete: issues regarding the allocation of powers between the two levels of government and those concerning key institutions such as the highest court have yet to be settled. So, although the 2012 Provisional Constitution of Somalia has declared a federal system, the latter's effectiveness remains to be seen. One of the key factors in ensuring that system's effectiveness will be the implementation of a sustainable form of fiscal federalism.

9.3 Fiscal federalism: theoretical framework and rationale

Fiscal federalism, widely discussed under the heading of 'fiscal decentralisation',[8] is concerned with the distribution of expenditure responsibilities, the allocation of taxation power, the execution of intergovernmental transfers for adjusting fiscal imbalances, the management of regional borrowing, and the establishment of mechanisms for enabling fiscal relations between levels of government.

The traditional normative approach to fiscal federalism (often dubbed 'first-generation theory') is based on the three major functions it serves in the public sector: macroeconomic stabilisation, income distribution, and resource allocation.[9] The approach is in favour of assigning a macroeconomic stabilisation function to the central government, as the latter is considered inherently national in nature; conversely, subnational levels of government are regarded as ineffective in dealing with the issues of unemployment and inflation or as lacking the necessary instruments (such as fiscal and monetary policies) for dealing with them.

Income distribution is also understood as the responsibility primarily of a national government. Similarly, the view is that the central or federal government is well placed to manage taxation policies (aimed at bringing about desirable levels of income redistribution from the wealthy to the poor) and address any regional disparities in this regard. Nevertheless, it is sometimes argued that, in certain countries at least, subnational governments do indeed have some redistribution functions inasmuch as they distribute benefits in kind: the allocation function is then, in principle, the responsibility of all tiers of government.

Traditional normative theory is associated, above all, with the decentralisation of expenditure responsibilities and the centralisation of revenue responsibilities, for the purpose of achieving 'efficiency' and 'equity' in the federation. It also emphasises the importance of transfers in addressing the problem of vertical and horizontal imbalances.

However, the theory has been challenged for its unquestioned assumption of 'benevolent government'.[10] Such an assumption fails to consider the impact of individuals, political parties, and corruption, all of which suggest the need for an approach grounded in political economy. Above all, the legal, political, and administrative aspects of institutional building and intergovernmental collaboration to enhance good governance have not been duly considered.[11] This critical position reflects the 'second-generation' approach to fiscal federalism, one which assumes public officials have goals that are induced by political institutions and which may diverge from maximising the welfare of citizens.

Literature about fiscal federalism focuses on a number of interrelated issues. It deals with the question of 'who does what' – that is, the distribution of expenditure responsibilities, something which in a federal system depends on the constitutional division of powers. The literature also examines the division of revenue-raising powers between the federal government and the regions, as well as the causes of fiscal imbalances between tiers of government and the effects these have on the execution of their respective responsibilities. The literature deals, too, with the design and objectives of intergovernmental transfers, which can help establish a meaningful relationship between tiers of government, and analyses institutional arrangements for managing fiscal relations between the tiers of government – a scope of enquiry that includes the regulation of regional borrowing arrangements.

The rationale for fiscal federalism is best understood in relation to the broader objectives of federalism or decentralisation. Ebel and Yilmaz assert that addressing ‘inefficient governance, macroeconomic instability, and inadequate economic growth’ are the main objectives of decentralisation.[12] At the same time, federalism is regarded as a useful institutional arrangement for accommodating diversity, ensuring self-rule at a subnational level and fair representation at a national level, managing regional economic disparities, and maintaining national unity.

In a decentralised or federal system, fiscal federalism provides important tools for realising such objectives since it helps promote efficiency, improves service delivery, emphasises the equitable distribution of resources, manages conflicts arising from resource claims, and generally enhances transparency and accountability. Various studies suggest that federal financial arrangements can do much to help a particular system be efficient, equitable, autonomous, and, at the same time, accountable.[13]

It should be noted that the application of the principles of fiscal federalism is influenced by the political and economic system, financial resources, level of economic development, and constitutional and legal framework of the particular country in question. Shah argues that federal or decentralised systems show a considerable degree of success when fiscal arrangements respect diversity in local identities and preferences and ‘pay special attention to regional economic divisions to ensure a level playing field to strengthen the economic union’.[14] An effective fiscal arrangement is, according to Ahmad and Searle, ‘the glue that holds the nation together’.[15]

9.4 The building blocks of fiscal federalism in Somalia

This section examines key political and legal issues around fiscal federalism. Consequently, it addresses the following areas: (i) the institutional framework that was designed to ensure participation of the constituent units in the federal power-sharing arrangement; (ii) the constitutional model for the distribution of expenditure responsibilities; and (iii) the assignment of revenue sources in general and natural resource taxation in particular. Other aspects of fiscal federalism are considered in the subsections which follow.

9.4.1 Institutional framework for subnational governments

In any federation, the main elements of fiscal federalism need to be anchored in the Constitution and related jurisprudence. This simple fact reminds us that the fiscal arrangement functions within the broader objective of balancing self-rule with a shared rule.[16] If a country adopts federalism so as to promote non-centralised decision-making, enhance democratic participation, and efficiently address diverse interests or preferences, an evaluation of the institutional architecture concerning subnational governments is essential. From the viewpoint of fiscal federalism, three main issues need to be examined.[17]

The first is the question of the number and size of the constituent units. Are these sufficient to provide needed goods and services at the local level? As Dafflon puts it, '[F]iscal federalism is about sharing power: one cannot decentralise responsibilities and revenues to subnational government levels without institutionally organising the effective participation of subnational governments in the decision-making process.'[18] The representation of subnational units at the federal level is necessary for sharing power in the legislative process and deciding on matters to do with expenditure and revenue. This is usually made possible through the Upper House or second chamber.

Secondly, federalism brings the government closer to the people so that public goods can be delivered according to the needs of local residents. The constitutional division of power between the federal and regional governments and the decentralisation of power from the regional to the local level are intended to enhance citizens' participation, their ability to express preferences, and their influence over public decisions.

The third issue concerns institution-building and the promotion of accountability at the subnational level. Appropriate institutions have to be built and maintained so that they can structure the devolution of power to subnational levels and thereby promote accountability and public participation. Almost all constitutions recognise the importance of building institutions and promoting efficiency and accountability. However, emerging federations like Somalia struggle to fulfil their commitments and abide by their constitutional obligations.

9.4.1.1 The status of Somalia's constitutional framework

Article 48 of the Provisional Constitution of Somalia establishes two levels of government: the level of the federal government (FGS) and the level of the Federal Member States (FMSs), comprising state as well as local governments. The Constitution provides that the boundaries of districts (local governments) are determined by a law enacted by Parliament, but it remains unclear whether the powers and functions of local governments are to be defined by the Federal Constitution or by the respective member states. Unlike the general practice in other federations, the Somali Constitution provides only guidelines for determining the number of constituent units and their powers and functions. According to article 49 of the Constitution, the number of member states and their boundaries is to be determined by the House of the People of Federal Parliament upon the recommendation of a commission established by the House. The article states that 'the boundaries of member states shall be based on the boundaries of administrative regions as they existed before 1991', but also insists that 'two or more of these regions may voluntarily merge to form a state'.

Somalia's institutional structure is still a work in progress. Article 48(1)(b) of the Provisional Constitution provides, as noted, that the FMS level is made up of state and local governments. Consequently, Somalia is defined as a federal republic with three layers of government: the centre, the member states, and the local governments. This implies that functions should be assigned to the three levels, a process that, as per article 54, involves negotiation between the federal government and the member states. The outcome of the negotiation decides whether the allocation of powers to the local level is left to individual member states alone without leaving an option open for the federal government to bypass the regional government level.

The Federal Constitution serves to define federal institutions and allot their powers and functions; however, state legislatures and executive bodies are to be defined by the respective state constitutions – the latter in turn need to be harmonised with the provisions of the Federal Constitution, as per article 121. This implies that each level of government has the power to establish and control its own public institutions so as to ensure its autonomy. At the same time, the Constitution emphasises collaboration between levels of government, further to which it sets out principles governing the establishment of, and relationships between, institutions that facilitate interaction between the different levels of government.

For example, the Constitution establishes an Upper House as a means of ensuring the participation of constituent units in federal law-making. According to article 49, the Upper House serves to represent the interests of the member states and safeguard the federal system, while, according to article 50, the House of the People is there to represent the citizens. Although the FMSs thus participate in the law-making process at the federal level through the Upper House, the latter – aside from its role in the passing of budget laws – has no special power over fiscal matters relating to the allocation of federal grants or sharing of revenue. Institutional dialogue is there to enhance collaboration in the law-enactment process in case of disagreement between the Upper and Lower Houses, or in case of disagreement about the introduction and passing of laws.

Members of the House are directly elected by the people in each state, but the Constitution does not mention whether they can assume office in the state executive. In terms of article 72, each state has an equal numerical representation, with the total number of representatives limited to no more than 54. In addition to its legislative power, the Upper House assumes a shared role in any amendment to the Constitution and in the establishment of federal institutions.

All in all, the legal framework for bringing the government closer to the people is still under development in Somalia. Once the institutional framework is complete, the next steps would be to ensure the continuous participation of citizens in government planning, implementation, and overseeing of service delivery activities. However, as with so many emerging federations,[19] there are still concerns around downward accountability and continuous societal participation.

9.4.2 Assignment of functional responsibilities

Central to expenditure assignment is the question of which functions are to be divided between the tiers of government. From the economic point of view, the need for this is argued on the grounds of efficiency, manageability, autonomy, and accountability. In federations, the distribution of responsibilities for expenditure is determined primarily by the Federal Constitution. In this regard, the division of responsibility turns mainly around the constitutional division of legislative and executive powers. Federal systems vary widely in the form, scope, and content of the functions they assign to different tiers of government. To understand the division of expenditure responsibilities, we focus on the division of executive powers. There are two models in this respect:[20] the dualist and the integrated model.[21]

In the dualist model, each jurisdiction delivers on functions which are assigned exclusively to it; the integrated model, by contrast, involves strong collaboration between the federal government and the states. As Saunders argues, many federations design their constitutions so as to meld the two approaches, making them dualist in some respects and integrated into others.[22] In general, though, Federal Constitutions specify 'exclusive', 'concurrent' and 'residual' powers on the basis of the approach they take to the division of legislative and executive powers; there can also be asymmetrical arrangements that require sustained negotiation.

As shown in Table 9.1, Shah, proceeding in terms of normative economic theory, proposes a framework which assigns expenditure on the basis of the divisions between policy-making and standard-setting, production, supervision, and regulation. In reality, of course, things are always messier than this neat depiction suggests – even where economic criteria provide the rationale for assigning a function to either level of government, the final decision remains a political one. Shah's conceptualisation also fails to take into account the fact that collaboration between local governments can take extremely diverse forms. However, as Dafflon and Madies note, 'This classification of functions is rudimentary but it has the merit of insisting on the distinction to be made between [policy-making], regulatory functions and public service supply functions.'[23] The proposal thus retains some relevance, albeit the need remains for collaborative approaches.

9.4.2.1 Expenditure assignment in Somalia: A work in progress

The principles for allocating powers and functions between levels of government in Somalia are contained in the Provisional Federal Constitution. Its article 54 assigns four functions to the federal government: '(a) Foreign Affairs; (b) National Defence; (c) Citizenship and Immigration; (d) Monetary Policy'. In terms of this article, the allocation of the remaining powers is to be negotiated and agreed upon by the FGS and FMSs. Until such an agreement is reached, the question of how to assign powers and functions between federal and state governments remains open.

Another important principle in the Constitution is that of subsidiarity. Here, article 50(b) declares that 'power is given to the level of government where it is most likely to be effectively exercised'. Though not synonymous

Table 9.1 A representative assignment of expenditure responsibilities

Function	*Policy, standards, and oversight*	*Provision and administration*	*Production and supervision*	*Comments*
Interregional and international conflict resolution	U	U		Benefits and costs international in scope
External trade	U	U, N, S		Benefits and costs international in scope
Telecommunications	U, N	P		Has national and global dimensions
Financial transactions	U, N	P		Has national and global dimensions
Environment	U, N, S, L	U, N, S, L		Externalities of global, national, state, and local scope
Foreign direct investment	N, L	L	P	Local infrastructure critical
Defence	N	N	N, P	Benefits and costs national in scope
Foreign affairs	N	N	N	Benefits and costs national in scope
Monetary policy, currency, banking	U, ICB	ICB	ICB, P	Independence from all levels and banking essential; some international role for common discipline
Inter-state commerce	Constitution, N	N	P	Constitutional safeguards important for factors and goods mobility
Immigration	U, N	N	N	U due to forced exit
Transfer payments	N	N	N	Redistribution
Criminal and civil law	N	N	N	Rule of law, a national concern
Industrial policy	N	N	P	To avoid beggar-thy neighbour policies
Regulation	N	N, S, L	N, S, L, P	Internal common market
Fiscal policy	N	N, S, L	N, S, L, P	Coordination is possible
Natural resources	N	N, S, L	N, S, L, P	Promotes regional equity and internal common market
Education, health, and social welfare	N, S, L	S, L	S, L, P	Transfers in kind
Highways	N, S, L	N, S, L	N, S, L, P	Benefits and costs of various roads vary in scope
Parks and recreation	N, S, L	N, S, L	N, S, L, P	Benefits and costs of various roads vary in scope
Police	S, L	S, L	S, L	Primarily local benefits
Water, sewer, refuse, fire protection	L	L	L, P	Primarily local benefits

Note: U, supranational responsibility; ICB, independent national bank; N, national government; S, state/provincial government; L, local government; P, non-government sector/civil society.
Source: A Shah, 'Introduction: Principles of Fiscal Federalism' in A Shah (ed), The Practice of Fiscal Federalism: Comparative Federalism, Montreal, McGill-Queens University, Forum of Federations (2007), pp 8–9.

with it, subsidiarity is often linked to decentralisation. The subsidiarity principle requires that functions be carried out by the lowest levels capable of doing so. The advantage of subsidiarity is thus that it maximises accountability and responsiveness to citizen preferences and, at the same time, allows for diversity (that is, similar but not identical levels of service).

In such assignments, questions of limited local capacity, spillovers, and economies of scale and scope also demand attention. Capacity and subsidiarity have to be weighed against each other, and only when this is done can a function properly be reserved to the local level. Hence, it is strongly recommended that functions which cross jurisdictions at the local level (public health, environmental policy, national roads) should not be assigned. Federations vary in the allocation of some expenditures, as for instance with regard to health and education. Thus, for instance – following the principle of subsidiarity – efficiency and responsiveness to local needs suggest that health and education should be decentralised; at the same time, the need for equity and national standards suggests that the national government must play a role.

Unsurprisingly, arrangements differ significantly from one country and sector to another: principles as such cannot provide a simple, single answer in which 'one-size-fits-all'. Somalis likewise do what appears to fit the specific circumstances best, as shown in Table 9.1.

Currently, the de facto arrangements are highly asymmetrical in terms of resources and autonomy, while the federal government assumes responsibility for other matters within Mogadishu and Benadir states. Any constitutional revision has to make it clear whether this is what Somalis want to build into the system. A federal government restricted to the capital city and with no spending power in the states is not a common feature of federations, though the experience of other countries always needs to be carefully analysed and assessed.

Asymmetry may be used as a means to accommodate regional political claims but is likely to result in variable capacity and the sharing of resources, consequently exacerbating rather than relieving tensions between regions. 'Learning by doing' is always a good option, but the kind of constitutional framework that Somalis want will need to be clarified over time.

9.4.3 Assignment of revenue-raising powers

Once expenditure responsibilities are defined, a framework is needed in which each tier of government can levy or generate its own finances without creating conflict between the tiers. In practice, however, fiscal disputes have shown themselves to be inevitable and the degree of tax autonomy enjoyed by subnational governments varies widely. In this subsection, we consider how the assignment of taxes is discussed in the literature and compare this with the situation in Somalia.

As a matter of principle, finance follows function: the allocation of financial sources enables or constrains governments in the exercise of the responsibilities for expenditure assigned by the Constitution.[24] While it is often said that there is no ideal system for allocating tax powers, the principles of allocation regularly lead to the centralisation of taxes and significant decentralisation of expenditure responsibilities. This fact can be attributed to the four general principles for assigning tax powers to different levels of government.[25]

The first principle – economic efficiency – dictates that taxes which contribute to macroeconomic stability should be allocated to the national government; similarly, taxes on mobile factors that affect economic efficiency should be assigned to the centre. The other side of this argument is that subnational tax sources should be stable. The next principle relates to concerns about 'national equity'. This dictates that tax bases that are unevenly distributed (such as taxes on lucrative natural resources) should be assigned to the central government.

The third principle, administrative feasibility, aims at minimising tax evasion and administrative cost and increasing tax compliance. In this regard, user fees and other benefit taxes are seen as better addressed by the level of government that renders the particular service. The fourth principle, suggested by Anwar Shah, is 'fiscal need or revenue adequacy', which entails that, 'to ensure accountability, revenue means should be matched as closely as possible with expenditure needs'.[26] It is worth remarking, however, that it is not always easy to make this principle fit coherently with the other three.

Although federations differ in how they implement these principles, we may observe three broad approaches to the assignment of the tax power. A constitution may assign tax sources to the federal government and the states separately and allow each to have *exclusive* tax powers within its own sphere. A *concurrent* power of taxation may also exist where the federal government and the states have equal constitutional authority to levy the same kind of tax with respect to the same category of persons, business, or item. Furthermore, a constitution could provide for *joint or shared* taxes. Here, the power of legislation and levying taxes is assigned to the federal level, while the states reserve the right to share some or all of the proceeds from specified taxes. Table 9.2 outlines various ways of assigning revenue-raising power through taxes, fees, and charges to the federal and subnational levels of government.

9.4.3.1 Tax assignment in Somalia

The 2012 Provisional Constitution does not categorise sources for the federal government and the member states with respect to the allocation of revenue-raising powers but rather sets out a few general principles. Article 54 provides that 'the allocation of powers and resources shall be negotiated and agreed upon by the Federal Government and the Federal Member States' (pending the formation of Federal Member States). A further guiding principle, stipulated in article 50(f), is that 'revenue-raising responsibilities should be given to the level of government that can exercise that responsibility most effectively'.

Accordingly, the details of the division of revenue-raising power (for example, the listing of revenue sources, tax bases, and the revenue-sharing arrangements between the different levels of government) would have to be

Table 9.2 Representative assignment of taxing powers

Type of tax	*Determination of base*	*Collection and rate*	*Administration*	*Comments*
Customs	F	F	F	International trade taxes
Corporate income	F, U	F, U	F, U	Mobility factor, stabilisation tool
Resource taxes				
• resource rent, profit tax, royalties, fees, charges, severance taxes, production	F	F	F	• Highly unequally distributed tax bases
• output and property tax, conservation charge	SL	S, L	S, L	• Benefit charges for state local services to preserve the local environment
Personal income tax	F	F, S, L	F	Redistributive, mobile factor, stabilisation tool
Wealth taxes (taxes on capital, wealth, inheritance, bequests)	F	F, S	F	Redistributive
Payroll	F, S	F, S	F, S	Benefit charge, e.g., social security coverage
VAT	F	F	F	Border tax adjustment possible under federal assignment; potential stabilisation tool
Single stage sales tax				
• Option A	S	S, L	S, L	• Higher compliance cost
• Option B	F	S	F	• Harmonised, lower compliance cost
'Sin' taxes				
• excise on alcohol, tobacco	F, S	F, S	F, S	• Health care a shared responsibility
• betting and gambling	S, L	S, L	S, L	• State and local responsibility
• lotteries	S, L	S, L	S, L	• State and local responsibility

(*Continued*)

Table 9.2 (Continued) Representative assignment of taxing powers

Type of tax	*Determination of base*	*Collection and rate*	*Administration*	*Comments*
Taxation of 'bads'				
• carbon	F	F	F	• To combat global pollution
• BTU taxes	F, S, L	F, S, L	F, S, L	• Pollution impact may be national, regional, or local
• motor fuels	F, S, L	F, S, L	F, S, L	
• congestion tolls	F, S, L	F, S, L	F, S, L	• Tolls on federal, provincial, or local roads
• parking fees	L	L	L	
Motor vehicles				
• Registration, transfer taxes, annual fees	S	S	S	State responsibility
• Driving license and fee				
Business taxes	S	S	S	Benefit tax
Excises	S, L	S, L	S, L	Residence-based taxes
Property	S	L	L	Immobile factor
Land	S	L	L	Immobile factor, benefit tax
Frontage, betterment	S, L	L	L	Cost recovery
Poll	F, S, L	F, S, L	F, S, L	Payment for local services
User charges	F, S, L	F, S, L	F, S, L	For services received

Note: U, Supranational agency; F, federal; S, state or province; L, municipal or local.
Source: A Shah, 'Introduction: Principles of Fiscal Federalism' in A Shah (ed), The Practice of Fiscal Federalism: Comparative Federalism, Montreal, McGill-Queens University, Forum of Federations (2007), pp 22–23.

negotiated in the process of establishing a permanent constitution. Despite this lack of detail on the division of tax sources, taxes are being levied and collected on a geographical basis, primarily by FMSs, as demonstrated in Table 9.3.

Currently, the FMSs levy and collect taxes within their geographical boundaries, while the FGS collects taxes from Mogadishu and the Benadir region (sharing a proportion of these with Benadir).[27] In general, there are a variety of reasons as to why the federal government's ability to raise revenue has been weak and that it is therefore unable to provide much-needed public goods and services throughout Somalia.

The primary reason is that the federal government lacks a constitutional mandate to diversify and implement its federal tax power across Somalia. But there are also other reasons. According to Abdinasir and Isak,[28] some of the main challenges arise from dealing with 'hard-to-tax' sectors,[29] poor administrative capacity, insecurity and political instability, the incomplete transition to the federal system, outdated laws and poor enforcement of those laws, and customs-related problems. Further reasons for limited revenue capacity include a lack of transparency and accountability in enforcing tax laws, as well as weak public trust in the government's commitment to spending taxes for public purposes.

Despite these challenges, the federal government aims at increasing its revenue capacity by broadening its tax bases in the Benadir region, adjusting tax rates, harmonising tax laws with member states, and modernising its tax administration system. In this regard, the Federal Ministry of Finance claims to have introduced a number of tax reforms since 2013. Policy changes have introduced tax and custom charges on certain imported items, broadened income

Table 9.3 Distribution of tax bases in Somalia (in practice)

Type of tax	*Federal Government of Somalia*	*Puntland*
Customs duty	√	√
Sales tax		√
Telecoms charges	√	√
Corporate income tax	√	√
Turnover tax	√	√
Personal income tax (public sector)	√	√
Personal income tax (private sector)	√	√
Land/property taxes		√
Stamp duty	√	√
Vehicle taxes	√	√
Business taxes		
Departure/visa fees	√	√
Airport/harbour fees and charges	√	√
Administrative fees	√	√

Source: World Bank, Somalia Economic Update, Washington (2015), p 54.

tax bases, and revised the colonial tax laws. The government also made some changes to its tax administration by introducing a tax identification number, establishing a large tax-payers office and IT-based revenue collection, and cancelling the outsourcing of tax collection to private agencies.[30] According to the Ministry of Finance report, these reform programmes increased revenue capacity from USD 69 million in 2013 to USD 183.5 million in 2018.[31]

Nevertheless, the federal government is able to exercise its taxing power only in Mogadishu, while all the member states continue to raise tax unilaterally within their territories. The new member states also collect their own taxes, with the Jubaland Administration collecting customs and other port-related taxes. Such practices undermine the norm of sharing the revenue raised by these kinds of taxes with other states that do not have (for example) the same access to ports.

If fiscal federalism is to be implemented in a meaningful way, the federal government and member states will need to redefine the assignment of taxation so that the taxation power of the federal government extends to the states and harmonises the taxation regime. To do this, the federal government has to negotiate and design a workable revenue-sharing system and equalisation mechanisms so that states like the Interim South West Administration, the Galmudug Interim Administration, and other financially weak states benefit from such arrangements. Ultimately, a system produced by successful negotiation would avoid the current possibility of double taxation by the federal government and the states, increase government revenue, and minimise Somalia's dependency on foreign aid.

9.4.4 Revenue from natural resources

Raising revenue from natural resources is one of the most contentious issues in the assignment of tax powers. Natural resource revenue is different from other kinds because while it can be a significant source of funds for a federation, natural resources tend to be unevenly distributed among the federation's constituents. In most cases, the Constitution defines the ownership of natural resources, but the definition is subject to multiple disputes related to resource control and administration, revenue-sharing between the federal government and the producing or non-producing constituent units, and issues around transparency and accountability.[32]

In Africa in particular, achieving equitable shares in oil revenue has been undermined by a culture of corruption, a lack of transparency, and a great deal of waste and inefficiency. As a result, the delivery of social services, the development of infrastructure, and provisions for environmental protection are matters that remain almost entirely unaddressed.[33] This underlines the need not only for equitable sharing of natural resource revenue but for financial transparency and accountability.

The sharing of revenue from oil and gas (and other rare minerals) is usually regarded as a subset of the sharing and transfer of grants. Revenue from oil and gas can be captured in different forms, such as royalties; licenses and fees; export, excise, and environmental taxes; special corporate income taxes; and payments from state-owned companies. In many federations, issues of revenue-sharing are often separated from questions of control and management.[34] Consequently, political negotiations are crucial in deciding how much control to allocate to producing regions and how much to allocate to the federal government on behalf of the citizens of the country as a whole. Equally important in natural resource taxation are the stabilisation of funds and issues of transparency and accountability.[35]

In deciding on the allocation of natural resource revenues, there is no uniformity among federations, but the following considerations often favour an allocation to the federal government:

- the overall significance of the revenues for the economy and their corresponding macroeconomic impact;
- the volatile and non-renewable nature of natural resources revenues and the impact of those characteristics on subnational government's fiscal management;
- the potential to create significant interregional inequity if revenues are unevenly distributed.[36]

A number of African countries have recently been engaged in producing in and taxing the oil and gas sector, and countries like Somalia are looking forward to succeeding in their exploration efforts in order to boost their revenue yield. Much can be learnt from the experiences of other countries that have been engaged in oil production and the consequent administration of revenue. Bryan and Hofman, for instance, warn that the 'prospects for successful management of natural resources significantly improve when democratic institutions are in place prior to the exploration of mineral wealth'.[37] Suberu argues, furthermore, that

> democratic institutions, including mechanisms of vertical and horizontal accountability like elections and parliaments, can be harnessed to foster rules and procedures that can restrain the ability of political leaders to misallocate natural resources rents to themselves and/or their cronies.[38]

When the flow of natural resource revenue precedes the development of democratic institutions, it is much more difficult to establish effective institutions for the transparent and accountable allocation of resource revenues.[39] Resource governance requires all levels of government to work together to constrain corrupt practices, to institute meaningful decentralisation, and to entrench the equitable and accountable sharing of oil revenue.

9.4.4.1 Taxing natural resources in Somalia: Whose power is it anyway?

Although the prospect of generating revenue from natural resources such as oil and gas was well known in Somalia prior to the federal system, the Provisional

Constitution does not provide any detail on the sharing of natural resource revenues. It asserts a general principle of equity with regard to the sharing of these revenues between federal and state governments, but it makes no provision for federal powers of taxation, for sharing revenue on a derivative basis with oil-producing subnational governments, or for the allocation of any general or specific grants. All in all, the Provisional Constitution evades the issues and simply provides, in its article 44, that '[t]he allocation of the natural resources of the Federal Republic of Somalia shall be negotiated by, and agreed upon, by the Federal Government and the Federal Member States in accordance with this Constitution'.

The FGS and FMSs have entered into serious discussion on the division of taxation powers and modes of equitably sharing natural resource revenue. The outcome of the negotiations will have both political and technical implications. These will be political in the sense of defining the allocation of natural resource tax bases to each level of government in ways that lead to decentralising, centralising, or concurring tax powers; they will also involve establishing institutions to build democracy and curb corrupt practices so as to ensure the transparent, fair, and equitable sharing of resources. In technical terms, the outcome of the negotiations will entail designing effective economic policies and building the necessary administrative, regulatory, and oversight capacity through the training and development of skilled personnel and the adoption of 'checks and balances' mechanisms.

9.4.4.1.1 INITIAL STEPS IN NATURAL RESOURCES REVENUE-SHARING

Along with other transfer mechanisms (such as sharing revenue from customs and international trade), the sharing of revenue generated by natural resources is intended to equalise the revenue capacity of member states. At present, however, monies collected from customs at different ports, and from trade taxes in general, are not centrally pooled; instead, they fall under the control of the states where the ports are located. Some progress has been made recently with regard to revenue from natural resources.[40] The federal government entered into a series of agreements with FMSs, namely the June 2018 Baidoa Agreement, the November 2018 Fisheries Agreement, and the 2019 Revenue Administration Act, though it remains to be seen how fully these agreements will be implemented and what their impact will be on increasing the revenue capacity of states.

The 2018 Baidoa meeting forged an agreement that settled the division of oil and other mineral revenues between the FGS, the producer FMS, the producer districts, and the non-producer FMS.[41] According to the agreement, different shares are allocated to the FGS and FMSs. Thus, for instance, the federal government will receive 55 per cent of offshore oil profits but only 30 per cent of onshore oil profits; similarly, 25 per cent of offshore oil profits goes to the producer states, but this portion increases to 30 per cent in the case of onshore

Table 9.4 FGS and FMS petroleum revenue shares as per the Baidoa Agreement

Revenue (percentage share)	*FGS*	*FMS (producing)*	*District (producing)*	*FMS (all non-producing)*
Offshore profit oil	55	25	10	10
Onshore profit oil	30	30	20	20
Royalty	40	40	10	10
Signing bonus	40	60		
Surface rent	30	50	20	
License fee	50	50		
Production bonus	30	50	10	10
Corporate income tax	100			
Export tax	60	40		
Capital gains tax	50	30	20	
Seismic data	50	50		
Capacity-building	50	50		
Local community development		30	70	

Source: Agreement on Ownership Management and Sharing of Revenues from the Natural Resources of the Country (Oil & Minerals), signed in Baidoa, June 2018; and World Bank (n 27), p 49.

oil profits. As can be seen in Table 9.4, the overall effect of the arrangement may bring about substantial horizontal imbalances between member states, as the proposed division favours producer states. In these cases, horizontal disparities could have been minimised through the use of other transfer instruments, but this would always have been challenging in cases where the federal government's tax power is highly constrained.

At the same time, the implementation of the agreement hinges on several factors. The first and most important of them is the commitment of the FMSs to adhere to the terms of the agreement, closely followed by the ability of the FGS to convince oil exploration companies that their investment will not be affected by the nature of the oil-revenue-sharing arrangement. It is also necessary to clearly delimit the FGS's tax legislation and tax administration powers. Of course, much depends, too, on ensuring the good sectoral governance necessary for adequate and efficient taxation of the oil companies. The stakes are high, since gathering the expected national revenue from this sector is crucial not only for socio-economic development but for peace-building in the country and developing trust between the FGS and FMSs.

The Fisheries Agreement of February 2018 also brought together the FGS and the FMSs in a revenue-sharing accord.[42] This concerned the licencing for the exploitation of tuna and tuna-like species outside the international water zone reserved for Somali fisheries and the sharing of consequent revenues. Such licencing generates a total of USD 1.045 million per year. Table 9.5 shows the revenue was shared between the FGS and FMSs in March 2019.

Table 9.5 FGS and FMS revenue shares from tuna licencing

Allocation to	*% share*
FGS	29
Puntland	18
Jubaland	13
South-West	13
Galmudug	13
Hirshabelle	14
Total	100

Source: Agreement on the Management of Fisheries & Revenue Sharing, signed in Addis Ababa, March 2019; World Bank (n 27), p. 47.

9.4.4.1.2 NATIONAL TAX ADMINISTRATION: REACHING CONSENSUS?

The Revenue Administration Law of October 2019 is another important instance of agreement and collaboration. This legislation aims at increasing the country's revenue capacity by broadening its tax base, harmonising taxes at federal and state levels, and generally improving the tax administration system. The tax base is to be broadened by expanding the sales tax on imports, increasing excises and customs duties on selected imported items, and introducing fees for various government services. The aim of improving the tax administration system is to enhance tax compliance and increase government revenue. Such improvement is to be achieved through the introduction of tax identification numbers, the automation of government services at registration, renewal and payment for services, and the reduction of corrupt practices.

However, a consensus is needed if the new law is to be implemented throughout the FMS. This has not yet materialised as there is no agreement as to whether the federal government should have the power to raise taxes outside Mogadishu and the Benadir region.

9.4.5 Intergovernmental transfers

To overcome the vertical and horizontal imbalances that often exist in federal arrangements, Federal Constitutions envisage intergovernmental transfers in the form of sharing tax bases, joint tax revenue, and the allocation of grants. Horizontal disparities in revenue capacity mean that better-off regions are in a position to deliver more and better services than poorer ones; this situation calls for a system of equalisation transfers that enable the poorer states to provide comparable levels of public services to their residents – such transfers serve to equalise spending and services across regions. However, federations vary in the nature and extent of the transfers necessary to reach the desired level of equalisation.[43] In many cases, the nature and extent of the transfers are mandated by the Constitution, while in others the power to determine these matters is left to the discretion of the federal government.

Intergovernmental transfers may take the form of general, or unconditional, grants or specific-purpose, conditional, or categorical grants; sometimes there are also separate revenue-sharing mechanisms. In principle, designing a mechanism for revenue-sharing or allocating general grants needs to address two main questions. First, how should the total volume of revenue transferred from the centre (to the states as a whole) be determined? Secondly, how should this gross amount (known as the total pool) be distributed between the states?[44]

Specific-purpose, conditional, earmarked, or categorical grants are intended to finance particular programmes or projects. Also, conditional grants are classifiable as either matching (cost-sharing) or non-matching (where the states are not required to spend a portion of their income to match the funding by the central government). Ahmad and Craig argue that specific-purpose grants seek to impose conditions on the use of grants in order to maintain nationwide standards for the provision of services such as health and education.[45] But the objective may go further and seek to address the problems associated with the provision of public goods by allocating funds to scarcely endowed areas. Such grants may also play a role in curbing financial embezzlement, inefficiency, and corruption, as the federal government retains the power to set conditions as well as control and audit spending.

In general, fiscal transfers to subnational levels of government can have several objectives. These include addressing vertical imbalances (by improving revenue adequacy); equalising fiscal capacity horizontally (through inter-jurisdictional redistribution); correcting any inter-jurisdictional spillover effects; correcting any major administrative weaknesses; and streamlining bureaucratic procedures.[46] The objectives may be achieved in various ways. The use of a grant formula to define the transfer objectively is one that has been widely adopted. Other formulas include those for equalisation transfers, expenditure, revenue-raising capacity, per-capita equalisation, and equalising revenue-raising capacity.

9.4.5.1 The prospects for transfers in Somalia

The available reports show that all of Somalia's member states have fiscal deficits, along with widely divergent revenue-raising capacities.[47] In the 2019 financial year, the fiscal disparity between the states was high, ranging from a little less than USD 3 million in the state of Hirshabelle to more than USD 62 million in Puntland as shown in Table 9.6. Such disparities can be attributed to the fact that the major sources of revenue in Somalia are customs duties and trade taxes, with the yield from these taxes differing considerably from one state to another. The states of Puntland and Jubaland, for instance, can rely on port services, customs, and international trade taxes, whereas the South-West,

Table 9.6 FGS and FMS revenue capacity, 2019 fiscal year (in USD millions)

Governments (FGS and FMS)	*Revenue collected*	*Grants received*	*Total*
Puntland	62.4	4.9	67.4
Jubaland	21.3	17.1	38.5
South-West	4.7	19.8	24.5
Galmudug	2.8	6.9	9.6
Hirshabelle	2.7	14.8	17.5
Federal government	173.3	109.2	338.9

Galmudug, and Hirshabelle have very limited tax sources. There are also considerable variations in management and administrative capacity between the states as a result of differences in infrastructure, skilled personnel, urbanisation, and success in attracting businesses. This asymmetry causes problems in measuring the imbalances between the jurisdictions.

Notwithstanding that imbalances are inevitable and transfer mechanisms have to be used to correct them, the Provisional Constitution does not provide for a division of resources or a system of transfers. What it does provide for is the 'fair distribution of resources'. Although fairness is one of the general principles animating federalism in Somalia, it is a difficult term to apply to fiscal imbalances. In countries where subnational governments are guaranteed their share of federally collected revenue, intergovernmental transfers are the manifestations of the assignment of lucrative tax sources to the federal government.[48] For there to be meaningful and effective transfers in Somalia, the FGS and FMSs would need to engage in committed negotiations to redefine the tax assignment issue and ensure the fair distribution of resources.

Currently, the FMSs are strongly in favour of the fair distribution of grants (bilateral or multilateral) between the FGS and themselves. Revenues from local taxes are collected by the FGS only from the Benadir region and the city of Mogadishu. Transfers from the FGS are hence limited to the share of grants unilaterally decided by the federal government. The available evidence, including that from a recent World Bank report, indicates that 'there is no rule or formula that determines the amount allocated to states'.[49] Nonetheless, the federal government also makes transfers to the FMSs from the direct foreign aid it receives.

The FMSs thus finance their expenditure from local revenue sources, their federal share of foreign aid transfers, and any direct aid they receive from foreign partners. However, a lack of transparency and the underreported flow of direct aid make it difficult to assess the fairness of the allocation of foreign aid and the overall revenue capacity of FMSs.[50] More than one-third of the total revenue available for both the FGS and the FMSs comes from foreign aid, but this cannot be considered a reliable source of government finance as it is unpredictable and volatile due to the unforeseen circumstances that donors might encounter.

It is, therefore, advisable to shift the transfer mechanism from sharing foreign aid to sharing local revenue generated from unevenly distributed sources such as international trade taxes, customs duties, and natural resource taxes. This approach, however, would require a firm commitment to addressing tax assignment issues in the upcoming constitutional reform process so as to strengthen the fiscal power of the federal government.

9.4.6 Functional and administrative capacity

The political rationale for self-rule in a federal system is that subnational governments need legislative and administrative autonomy in order to follow the priorities assigned by local preferences and to allocate revenues accordingly. Administrative autonomy is there to enable each level of government to establish and control its own administration and public services and execute its own policy decisions. This entails strengthening the capacity of local institutions to discharge their devolved powers and functions effectively. It is therefore essential to define the governance structure at the regional level, as well as to strengthen the capacity of subnational governments in various areas, including planning, implementation strategies, budgeting, accounting practices, and understanding laws and regulations.[51] 'Political capacity' is also an important part of administrative capacity. As Dafflon puts it:

> Political capacity is the ability of elected members of the local government to understand the residents' preferences and demands, to apprehend the policy issues, and to behave appropriately in political assembly. It is also the ability to distinguish between private, pressure group and general local interests. 'Policy capacity' belongs to the same category: identify the demand and clarify the issues in order to define the objectives, fix the supply and delivery of local public services and find the appropriate means and tools.[52]

With regard to Somalia, the key challenges are its overall political stability, peace, and security and the need for some degree of trust in and consensus on the workings of the federal system. Addressing these challenges requires completing the process of establishing member states, dividing powers and resources between the levels of government, and designing the necessary institutions. The Constitution provides important guidelines for the formation of a professional civil service. This would be one in which different Somali communities are represented in a competitive manner and excluded from party leadership.[53] Article 119 of the Constitution provides:

(1) the FGS and the FMS may recruit their employees;
(2) there shall be a civil service both at the Federal level and at the level of the Federal Member States;

(3) the Federal Government and the Federal Member States may cooperate in the deployment of staff, in order to ensure that expertise and experience are available where needed and in order to promote national unity;
(4) the Civil Service of the FGS and FMS shall be formed on the basis of proportional representation of the resident population.

Government institutions are meant to improve the performance of governance in general and the delivery of services in particular; it is thus imperative to improve the technical and professional capacity of the public sector. Somalia has a great deal of work to do both in clarifying the administrative autonomy of each level of government and in putting in place (especially at the subnational level) the skilled, committed, and accountable civil service it needs.

9.4.7 Institutions for fiscal transfer

Determining the responsible organ for designing the system of federal–state local transfers is a key issue for any intergovernmental transfer system. According to Shah, the usual tactic is for the federal government to design the system on its own since it is directly responsible for spending the revenue transferred to it by the subnational government.[54] This, however, has the side effect of limiting subnational autonomy. The problem can be minimised if the task is constitutionally conferred on a specific institution well regarded by the constituent units of the federation.

Federal experience suggests several ways of doing this. Some federations opt for the formation of independent commissions mandated with advisory roles. Others use the federal legislature or work through the Upper House or some form of the intergovernmental council. Watts identifies four ways of shaping institutional processes for intergovernmental fiscal relations.[55] The first, as in Australia, India, and South Africa, is to use independent commissions that are entrusted with the power to determine appropriate transfer formulas. Another method is for the Constitution to establish an intergovernmental council composed of federal and state representatives, while in a third method – as in Germany, Switzerland, the United States, and Belgium – federal grants are determined by the legislature but with strong input from the states through their second chambers. Finally, there is the constitutional design in which all forms of federal transfer mechanisms are placed under the unilateral control of the federal government, although in practice this involves a discussion between representatives of the federal and provincial governments.

For Somalia, the most urgent need is to protect the system from unilateral control either by the federal government or by the states. Establishing an independent body to design and enforce intergovernmental transfers is the strongest option, noting at the same time that, in regard to federal–state relations, the Provisional Constitution often emphasises securing representation and consent from the FMSs (but is open to the possibility of establishing independent commission). It may be possible to combine technical input from an independent commission with giving the final say to the second chamber (where FMSs are represented). In this way, the system could secure a political decision from all jurisdictions and make the system transparent.

9.5 Conclusion

Somalia decided to adopt a federal form of governance with its 2004 Charter and its 2012 Provisional Constitution (which outlines some of the necessary key institutions). The latter requires that consensus be reached on various aspects of fiscal federalism. While some progress has been made in defining the relationship between the federal government and the member states, the key decisions that would define the form of fiscal federalism in Somalia have still to be made. In this regard, the following question remains unaddressed: What type of fiscal transfer arrangement seems feasible for a country like Somalia, both to ensure fiscal sustainability and to build national cohesion?

The present chapter explored this question by looking at the building blocks of fiscal federalism and asking whether these were adequately laid down in the Provisional Constitution and to what extent they have been put into practice. The key components of fiscal federalism were identified: institutional design (the constitutional organisation of subnational units and their participation at the federal level); the assignment of functions; the assignment of revenue sources; natural resource revenue-sharing and intergovernmental transfers; and the administrative capacity necessary for ensuring fiscal discipline.

The chapter also investigated the available options for crafting both a viable vertical distribution of resources between the federal government and the states, as well as identifying the variables for horizontal distribution between the states. In this regard, it looked at recent developments such as the 2018 Baidoa Agreement on Petroleum and Mineral Revenue Sharing and the 2018 agreement between the federal government and the states governing the fisheries industry.

If federalism is to remain Somalia's political preference, some important decisions still need to be made. All in all, it is clear that Somalia has yet to decide just what kind of fiscal federalism it wishes to adopt. The division of powers, functions, and revenue sources between the different tiers of government remains a crucial question. The chapter has sought to identify a number of options that would help in the country's effort to find its way through the complex economic, social, and political forces that are in play. If fiscal federalism is to act in the interests of social cohesion, we argue for the importance of assigning custom duties, international trade tax and natural resource tax to the federal government while implementing a system of intergovernmental revenue transfer that would ensure the sustainability of common economic development. We recognise, too, that all of these ultimately depend on a prior political commitment to federalism that would enable their successful implementation.

Notes

1 RT Suberu, 'Lessons in Fiscal Federalism for Africa's New Oil Exporters', in AC LeVan, et al. (eds), *African State Governance: Subnational Politics and National Power,* London, Palgrave Macmillan (2015), p 33.
2 A Fiseha, *Federalism and the Accommodation of Diversity in Ethiopia: A Comparative Study,* Nijmegen, WLP (2006). There are also different power-sharing and consociational arrangements for managing diversity. Equally important are the rule of law, democracy, accountability, the equitable distribution of resources, and economic development, which should be given due recognition in either federal or unitary systems in the region.
3 A Fiseha, 'Federalism and Decentralisation in the Horn', Draft Proceeding of a *Conference on Governance in the Horn of Africa*, Addis Ababa, Forum of Federations, unpublished (2013), p 3.
4 The country's land area is roughly 637,600 km^2 (SM Hassig and A Latif, *Cultures of the World: Somalia,* 2nd ed., New York, Marshall Cavendish International (2008)). In 2014, Somalia had a population of approximately 12 million (UNPF, *Population Estimation of Somalia*, Nairobi, UNPF (2014)).
5 *Ibid.* In terms of language, all Somalis speak the Somali language; in religious terms, 99 per cent of them are Sunni Muslims.
6 The federalisation process remains under military guard by the African Union Mission to Somalia (AMISOM).
7 Fiseha (n 2), p 5.
8 Given that federalism in economics entails decentralisation, literature on fiscal federalism or decentralisation deals in either case with similar issues and phenomena – that is, with the fiscal implications of a decentralised system of multilevel government, irrespective of its constitutional status as a federal, decentralised unitary, regional, or (as in the case, for instance, of the European Union) supranational arrangement.
9 RA Musgrave, *The Theory of Public Finance*, New York, McGraw Hill (1959), p 179.
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11 See, for example, B Weingast, 'Second-Generation Fiscal Federalism: The Implications of Fiscal Incentives', 65(3) *Journal of Urban Economics* (2009), pp 279–293.
12 RD Ebel and S Yilmaz, 'On the Measurement and Impact of Fiscal Decentralization', *Policy Research Working Paper* 2809, Washington, DC, World Bank (2002), p 157.
13 See Ahmad and Brosio (n 10).
14 A Shah, I Rajaraman, and F Rezende, 'Emerging Issues in Fiscal Federalism' in R Watts and R Chattopadhyay (eds), *Unity in Diversity: Learning from Each Other*, New Delhi, Viva Books, Forum of Federations (2007), p 30.
15 E Ahmad and B Searle, 'On the Implementation of Transfers to Subnational Governments' in A Ehtisham and G Brosio (eds), *Handbook of Fiscal Federalism,* Cheltenham, Edward Elgar (2006), p 390.
16 G Anderson, *Federalism: An Introduction*, Toronto, ON, Oxford University Press, Forum of Federations (2008), p 72.
17 B Dafflon, 'The Political Economy of Decentralization: Fiscal Federalism in Practice', unpublished paper presented at HESPI Conference on Federalism in Somalia, 23–25 October, Addis Ababa (2014), p 12.
18 *Ibid.*
19 For some preliminary studies on devolution in Africa, see S Negussie, 'Fiscal Federalism and Decentralization in Selected IGAD Member Countries', Addis Ababa, The Horn Economic and Social Policy Institute (HESPI), Working Paper 04/16 (2016).
20 R Watts, *Comparing Federal Systems*, 2nd ed., Montreal, QC, McGill-Queen's University Press (1999).
21 In dualist or classical federalism (as in Canada and the United States), each level of government retains executive responsibility for those matters in which it exercises the

legislative power; in the integrated or functional model of federalism (also called the German model), the federal government is concerned primarily with policy initiation, formulation, and legislation, while states are responsible mainly for implementation and administration. For further detail, see Anderson (n 16), pp 11–18.

22 C Saunders, 'Constitutional Arrangement of Federal Systems', 25(2) *Publius* (1995), pp 61–79.

23 B Dafflon and T Madiès, 'Decentralization: A Few Principles from the Theory of Fiscal Federalism 1', 42 *Notes et Documents*, Paris, Agence Française de Development (2009), p 35.

24 Watts (n 20), p 43.

25 A Shah, 'Introduction: Principles of Fiscal Federalism' in A Shah (ed), *The Practice of Fiscal Federalism: Comparative Federalism,* Montreal, QC, McGill-Queens University, Forum of Federations (2007), pp 19–20.

26 *Ibid.* p 15.

27 World Bank, 'Somalia: Moving the Federalism Agenda Forward', Washington, DC (2020).

28 AA Mohamud and NN Isak, 'Reforming the Tax System of the Federal Government of Somalia', 5(2) *Journal of Tax Administration* (2019), pp 125–137.

29 *Ibid.* Some economic sectors cannot be taxed properly due to corruption and security problems.

30 *Ibid.*

31 World Bank (n 27).

32 See G Anderson, *Fiscal Federalism: A Comparative Introduction*, Ottawa, ON, Oxford University Press, Forum of Federations (2010); G Brosio, 'The Assignment of Revenue from Natural Resources' in A Ehtisham and G Brosio (eds), *Handbook of Fiscal Federalism*, Cheltenham, Edward Elgar (2006), pp 431–458.

33 Suberu (n 1).

34 Anderson (n 33) mentions that while ownership, management, and principal access to revenue go together in some federations, there are also variations. For instance, in Brazil, the federal government owns and manages but states get most of the revenue; in India, states own but the centre manages and gets most of the revenue; and in Russia, the federal government manages and gets all the revenue. Ownership and share of resources sometimes vary depending on whether the resource is offshore or onshore. See also G Anderson (ed), *Oil and Gas in Federal Systems*, Oxford, Oxford University Press (2012); G Anderson, *Natural Resources in Federal and Devolved Countries*, Ottawa, ON, Forum of Federations (2020).

35 Anderson (n 32).

36 *Ibid.*

37 S Bryan and B Hofmann, *Transparency and Accountability in Africa's Extractive Industries: The Role of the Legislature*, Washington, DC, National Democratic Institute for International Affairs (2007), p 10.

38 Suberu (n 1), p 35.

39 *Ibid.* The experiences of Nigeria and Ghana support this argument. Nigeria still faces challenges related to a lack of effective institutions, whereas Ghana continues to benefit from having instituted an appropriate democratic system prior to generating natural resource revenue.

40 World Bank (n 27).

41 *Ibid.*

42 *Ibid.* p 47.

43 A Shah, 'A Practitioners Guide to Intergovernmental Transfers', *Working Paper* 4039, Washington, DC, World Bank (2006).

44 Similar issues could be raised in the process of intra-state transfer of revenue; likewise, the solutions adopted at the federal level could also be used at the state level.

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46 L Schroeder and P Smoke, 'Intergovernmental Fiscal Transfers: Concepts, International Practice, and Policy Issues' in P Smoke (ed), *Intergovernmental Fiscal Transfers in Asia: Current Practice and Challenges for the Future*, Manila, Asian Development Bank (2003), pp 20–59.
47 Data gathered from the Ministry of Finance of Somalia at http://mof.gov.so/fiscal/indexx.html; see also World Bank (n 27).
48 The Kenyan Constitution guarantees county governments at least a share of 15 per cent from the national revenue (article 203(2)); the Ethiopian Constitution empowers the House of Federation to determine the share of joint revenue as well to design a formula to determine the share of states from the federally determined grant subsidy (article 62(7)).
49 World Bank (n 27), p 13.
50 *Ibid*.
51 T Gebre-Egziabher, 'Decentralization and Regional and Local Development: Trends and Policy Implications' in D Rahmeto, et al. (eds), *Reflections on Development in Ethiopia: New Trends, Sustainability and Challenges*, Addis Ababa, Forum for Social Studies (2014), pp 133–168.
52 Dafflon (n 17), pp 18–19.
53 For detail on the civil service, see chapter 11 (articles 115–119) of the Provisional Constitution.
54 Shah (n 43), p 46.
55 Watts (n 20), p 53.

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