THE TITLE: FEDERALISM AND POLITICAL STABILITY IN SOMALIA

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ABSTRACT

Federalism is by far the most complicated system of governance that has ever been used anywhere in the world. Whereas power emanates from one source in a unitary system of governance, there are two competing power centers in a federal system. Political Stability can be used to describe a government that is functioning well.

Nearly 30 years after the collapse of the Siad Barre regime, Somalia has made considerable progress in defining a new relationship between the federal government and the member states. But key agreements on the allocation of functions and revenues between the two tiers of government have yet to materialize. This paper considers three options: (i) maintaining the status quo; (ii) shifting most revenue raising powers to the federal government while assigning responsibility for major functions to the states and financing those functions through intergovernmental transfers; and (iii) concentrate both revenue-raising powers and expenditure responsibilities at the federal level.

This paper endorses the second option, as it responds to the desire of states to maintain substantial autonomy, while establishing a federal government that can provide security against external threats, ensure a basic level of public services available to all Somalis regardless of where they live; and facilitate the free movement of people and goods throughout the country.

Methodology: The data for this study paper was both primary and secondary in nature. An effort has been made to study the Federalism and Political Stability in Somalia. Data has been collected from several newspapers, journals and websites related to Federalism and Political Stability

Finally, the study found out that there is a positive correlation between Federalism and Political Stability (at r. Value of 0.895; Beta value 0.895 and a significant value of 0.000). In summary the findings, it was discovered that were similar to those of Swaleh et al. (2008), (2010) and 2015; believe that federalism seem to be more appropriate in the political stability and this is attributed to clan influence because most of clan leaders in the region hold or have much influence to the political stability.

1. INTRODUCTION

Somalia continues to develop its own form of Federalism in response to its unique history, culture, and socio-economic needs. The objectives of this paper on the Federalism and Political Stability are to:

(i) Explain federalism and its relevance to the Somali context;
(ii) Provide a stocktaking exercise of where Somalia is in its journey toward fiscal federalism and political stability, with the objective of informing multiple audiences of the current status and gaps remaining with reference to international examples; and
(iii) Present some forward looking options to inform the policy dialogue and stimulate wider debate among the various stakeholders in Somalia

Somalia is emerging from decades of conflict, with the signing of the Provisional Constitution in 2012 paving the way toward a political settlement. Whereas the Provisional Constitution defines the boundaries of Somalia based on the country's former (pre-1991) frontiers, the 'government' effectively consists of five member states, a federal government, and the self-declared Republic of Somaliland. Since the onset of the civil war in 1991, the member states and Somaliland have been largely autonomous. The authority of the federal government is largely confined to the city of Mogadishu. The agreement of the Provisional Constitution marked substantial progress. However, key issues related to the distribution of functional assignments and the sharing of resources still need to be agreed upon.

2. Materials and Methods

Federalism and Political Stability with its Application to Somalia (

Federalism is conventionally defined as a structure of governance in which two or more governments share sovereignty over the same territory. In this context, the federal government's mandate extends over the entire national territory and the subnational governments' mandates extend over the individual parts of it. Some countries in fragile and conflict-affected settings have adopted federal structures to accommodate regional political interests within a single political entity.

There are 25 officially designated federal countries in the world, accounting for 40 percent of the world's population. Many federations have large populations (Brazil, India, Nigeria and the United States), but some may be small, such as Bosnia and Herzegovina (with a population of 3.5 million). Federal structures arise from a variety of different historical circumstances. However, for purposes of this chapter, federal structures are considered as having three key characteristics: a guarantee of political autonomy for first-tier subnational governments (states); explicit limitations on the powers and functions of the federal government; and provisions to ensure that first-tier subnational governments have the resources required to perform the functions assigned to them.

Regarding political autonomy, each member state has an independently

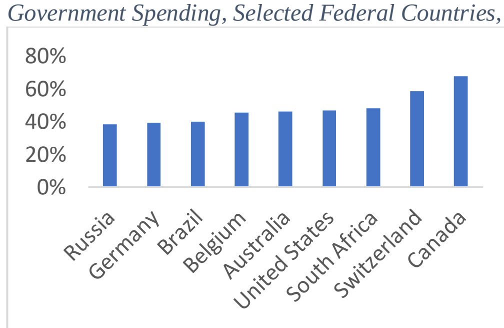
elected government, with a parliament and an executive chosen by the citizens of each state. Many non-federal countries have multiple tiers of territorial administration, including some with elected parliaments, but would not necessarily be considered federal under this definition.

In a federal structure, the constitution limits the functional responsibilities of the federal government. Typically, federal functional responsibilities are limited to national security, foreign affairs, the regulation of the monetary and banking systems, and certain modes of transportation. The assignment of functional responsibilities to states can take two forms. Some constitutions simply authorize states to perform any function that is not assigned to the federal government. Others list the functional responsibilities of state governments, with varying degrees of generality. Typically, federal constitutions only outline the aspects of the relationship between the federal government and the states that are intended to be permanent, leaving details that may be frequently revised to ordinary legislation.

Importantly, the delimitation of federal powers in federal constitutions does not imply that a federal government can have no role whatsoever in functions that are not explicitly assigned to it. Federal governments typically regulate the functions performed by states. In fact, federal constitutions do not prevent a federal government from expanding its role into new fields. For instance, Figure 1 shows that state and local governments typically account for only 40 to 60 percent of total public spending in the federal countries for which internationally comparable data is available. This is partly due to central government spending on social insurance a function that was not contemplated when most of their respective constitutions were first drafted.

Figure 1: In Federal Countries, Subnational Governments Play a Large Role in Public Spending

(Subnational Spending as a Percentage of General Government Spending, Selected Federal Countries, 2017)



Source: International Monetary Fund

To ensure that states have the resources to perform the functions assigned to them, federal constitutions typically assign certain taxing powers to them. In assigning taxes Federal constitutions typically make a distinction between taxes that have a localized incidence and those that do not. Taxes that do not have localized incidence include taxes on international trade and transactions, value-added taxes and corporate income taxes. These taxes do not have localized incidence because their burden falls not on the firm or person that pays the tax, but rather on people who buy the firm's products, or those who work for the firm or own it. Those people may not live in the jurisdiction where the tax is collected. Allowing a state to impose a corporate income tax, for example, would generate substantial revenues for the jurisdiction where corporations are headquartered, while the burden of those taxes would ultimately fall on employees, consumers, or stockholders throughout the country. For this reason, states and their subordinate local governments are typically assigned only taxes that have localized incidence such as retail sales and property taxes. States are also permitted to impose personal income taxes, although this power may be shared with the federal government. Box 1 illustrates selected country examples.

Federal constitutions often also call for a system of fiscal transfers from the central government to the states. These take a variety of forms. Some are discretionary, that is, states can use the transfers for any (legal) purpose they wish. Countries also provide transfers earmarked for specific purposes. These are intended to encourage states to spend more on certain functions than would otherwise be the case. Governments often provide earmarked funding for education, for example, to ensure that states devote sufficient funding to this function. Central supervision is required to ensure that states spend these funds as directed.

Whereas every federal country is unique, the federal model appears well suited to Somalia. The key characteristics of federalism (state-level political autonomy, significant functional responsibilities and allocation of revenue raising powers) respond well to the desire of states to maintain substantial autonomy, while establishing a viable federal government for the territory as a whole. As such, federalism can aim to prevent military conflict among states; ensure a basic level of public services available to all Somalis regardless of where they live; and facilitate the free movement of people and goods throughout the country.

Box 1: Revenue Assignment: Selected Country Examples

The process of assigning revenues to subnational governments and designing intergovernmental transfers is highly political, where different federal systems have their own idiosyncrasies.

In Ethiopia, states are granted exclusive power to impose taxes on farmers and individual traders, rental incomes, transport services within their respective territories and the incomes of their own employees. However, the states are largely reliant on central government transfers. The main federal transfer is an unconditional grant, which is distributed among the states according to a complex assessment of the revenue potential and specific expenditure needs of each state.

In Nigeria, state governments are permitted to impose personal income taxes, as well as various minor taxes on entertainment, hotels, and so on. However, the principal sources of state revenues (except in Lagos state) are transfers—including shares of the value-added tax (VAT) and shares of oil revenues which form part of a so-called federation account. The VAT is administered by the central government, which retains 15 percent of the proceeds. States and local governments receive 40 percent and 30 percent, respectively. Of the total assigned to states and local governments, 40 percent is distributed in equal amounts per state, 30 percent is distributed on the basis of population, and 20 percent on the basis of origin. The Nigerian Constitution prohibits one state from taxing citizens of another state.

In Brazil, the federal constitution authorizes states to impose a VAT, as well as taxes on property transactions. Local governments are authorized to impose taxes on property. To supplement state revenues, the Brazilian Constitution requires the federal *government to distribute 21.5 percent of the revenues from the federal income and industrial products to the states. Funds are distributed on the basis of population and per capita income, with poorer states receiving a proportionately larger share. Another 24 percent of revenues from those two taxes are distributed directly to local governments.*

The Canadian Constitution restricts provinces to taxes that are considered 'direct,' a term which has been subject to much debate. At present, 'direct taxes' include the personal income tax, the corporate income tax, and the harmonized retail sales tax. These taxes are administered by the federal government (except in Quebec) and are shared between the two tiers. Each province's share is based on the amount collected in the province, which in turn reflects the size of its tax base and the tax rate it chooses to impose. The provinces also benefit from several central government transfer programs, including a large equalization program which supplements the revenues of the poorer provinces.

Source: Author's compilation from various federal constitutions

The details of any such federal arrangement will need to be worked out among the relevant parties in Somalia, who have various interpretation of federalism, and its potential benefits. Some parties may prefer a more centralized approach, holding on to the legacy of the Siad Barre regime. Other parties may prefer a loose confederation of largely independent states, reflecting in certain states how governance arrangements evolved during the period of state collapse. Others may prefer something in between. What is critical is that the relevant parties arrive at an agreement on key components of a federal structure that they are willing to buy into and stick with.

3. Results

The Status of Somalia in its Journey towards Federalism and Political Stability.

A. Drafting the Constitution

It was not until August 2012 that a new Constitution was provisionally adopted by a National Constituent Assembly (NCA) comprising 825 members representing various parts of Somali society. The Constitution has several key provisions. First, it declares that the territory of the federal republic corresponds to the boundaries of the former republic as defined in the 1960 Constitution (thus including Somaliland). Second, it defines the political structure of the federal government. It consists of a federal Parliament comprised of an upper house of no more than 54 members, with an equal number of representatives for each region (based on the 18 regions that existed in Somalia before 1991) and a lower house consisting of 275 members 'representing all communities of the federal republic in a balanced manner.' Together the two houses are to elect a president, who among other duties, serves as commander in chief of the armed forces, approves legislation drafted by the federal parliament, and appoints a prime minister. The prime minister, in turn, serves as the head of the federal government, and appoints and dismisses members of the Council of Ministers.

The process of reconstituting a central government in the territory of the former republic is underway. It began in 2000 when the Djibouti Peace Conference established a Transitional National Government (TNG) and a power-sharing arrangement based on a so-called 4.5 formula. Under this formula, Somalia's four main clan families each received an equal stake in political representation, and the other 'minority' clans together shared a 0.5 stake. In 2004, the Nairobi Conference led to the creation of a Transitional Federal Government (TFG). In the same year, the president of Puntland was elected President of the TFG. Before the voting, the 25 Presidential candidates signed a declaration, pledging to support the elected president and demobilize their respective militias. However, the demobilizations never occurred.

The Provisional Constitution defines the structure of the state but leaves the division of responsibilities for several major functions undefined. The state is to consist of two levels: the federal government and the federal member state (FMS) levels. The Provisional Constitution goes part way toward assigning functions to each of the two levels. It identifies four functions that are exclusive to the federal government: foreign affairs, national defense, citizenship and immigration and monetary policy. It also states explicitly that the 'Federal Government shall guarantee the peace and … national security of the Republic through its security services, including the armed forces and the police force.' At the same time, it acknowledges that the FMSs may have their own police forces, stating that the 'police forces established by the FMS have the mandate to protect lives and property and preserve peace and security locally, alone or in cooperation with the federal police force.' However, the Provisional Constitution does not define the functional responsibilities for a wide range of other functions such as education, health, and transport, stating that 'power (shall be) given to the level of government where it is likely to be most effectively exercised.'

Likewise, the Provisional Constitution does not provide for a division of resources or a system of intergovernmental transfers, stating only that the distribution of resources is to be 'fair', and that responsibility for the raising of revenues shall be given to the level of government 'where it is likely to be most effectively exercised'. It states that 'the allocation of natural resources shall be negotiated and agreed upon between the Federal Government and the FMS.' Also, 'in the spirit of intergovernmental cooperation, the federal government shall consult the FMS on negotiations relating to foreign aid and commits the Federal Parliament to enact a 'framework for financial management'. The framework is to define the procedures and timetable that FMSs are to use in preparing their annual budgets.

The 2012 Provisional Constitution therefore leaves some key elements of the federal structure undefined, and is in the process of being reviewed. Unlike the constitutions of other federations, it does not constrain the functions of the federal government or define the revenues of the states. As the Constitution was intended to be provisional, procedures are defined for making amendments and adopting a final version. Schedules C and D of the Constitution include the specific list of issues to be addressed through amendments. The task of drafting these amendments was assigned to an Independent Constitutional Review and Implementation Commission

(ICRIC), overseen by a high-level Provisional Constitutional Review and Implementation Oversight Committee (OC). At the time of writing (March 2020), the constitutional review process is currently underway, spearheaded by the United Nations. As part of the Mutual Accountability Framework, agreed at the 2019 Somalia Partnership Forum, a commitment was made to adopt a reviewed Federal Constitution by June 2020. Pending adoption of such a permanent constitution, further legal procedures may be followed to allow the Provisional Constitution to continue. In the case of Puntland, the Constitution of Puntland was adopted before the Provisional Constitution, and so Puntland is allowed to function on the basis of its own State Constitution until such time that the Provisional Constitution and the Puntland State Constitution are harmonized.

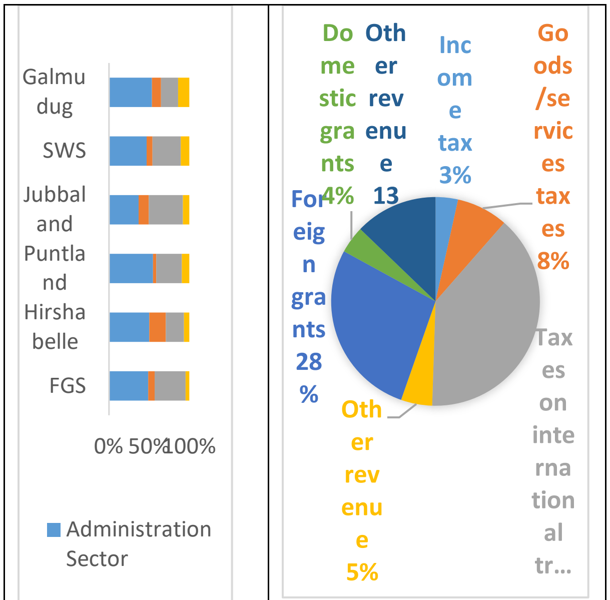
B. Current Situation

In the meantime, the federal government and the member states continue to operate as quasi-autonomous jurisdictions. Although the Provisional Constitution grants the federal government exclusive power over foreign affairs and immigration, as well as monetary policy, for example, some states have taken these powers into their own hands. Each member state supports itself from its own tax revenues, supplemented by small ad hoc transfers from the federal government and direct foreign aid.

The expenditures of the federal government and the member states are dominated by two functions: administration and security. Figure 2 shows the functional breakdown of their respective expenditures based on the Appropriation Acts for 2018. As indicated, roughly half the spending of both the federal and member state governments was allocated to administration, a category that (for the FGS) includes the operations of Parliament and the Ministries of Finance and Interior. At the federal level, 40 percent of spending was allocated to security. Among the member states, that proportion varied from 21 percent (Galmudug) to 43 percent (Jubbaland.)

Very little spending is devoted to economic activities, which include transportation, public utilities, and support for agriculture, as well as social services, such as education, health and social protection (Figure 2). The FGS devoted eight and four percent of its budget to economic activities and social services, respectively. State allocations to economic activities ranged from four percent (Puntland) to 21 percent (Hirshabelle). State spending on social services ranged from six percent (Hirshabelle) to 14 percent (Galmudug). The low level of state spending on economic activities and social services is particularly striking when expressed in per capita absolute terms. In Galmudug, for example, allocations for economic activities totaled US$ 0.13 per capita, and allocations for social services totaled US$ 0.15 per capita.

Figure 2: Budget Allocations are Dominated by Administration and Security Sectoral Allocation of FGS and Member State Budgets, 2018	**Figure 3: International Trade Taxes and Foreign Grants are the most Significant Sources of Revenues** Sources of Total FGS and State Revenues, 2018



Source: Abyrint Monitoring Agent (2018); FGS, and FMS Budgets (2018)

The federal government and the five member states are largely dependent on two sources of revenue: taxes on international trade and foreign aid (Figure 3). Taxes on international trade accounted for roughly 40 percent of total revenues in 2018 and official development assistance (ODA) accounted for nearly 30 percent. The federal government collects the highest share of revenues from international trade taxes (at 72 percent) and is the largest recipient of ODA (at 94 percent.

C. Recent Developments

Since the Provisional Constitution was adopted, some progress has been made on the political front as well as on specific issues. In the last three years, in particular, there have been several meetings signaling an intention to continue dialogue. These include meetings in London, UK (May 2017), Baidoa, Somalia (June 2018), Kampala, Uganda (November 2019), Kismayo, Somalia (December 2019), and another meeting is planned for this year in Baidoa, Somalia (March 2020).

On the political front, elections for the lower house of Parliament were successfully held in 2016 using a multi-stage process, starting with the selection of traditional elders from each of the main clans. The new parliament and government convened with the leadership in 2017, promising to finalize the process before the 2020 elections. To this end, the National Security Council, comprised of the leaders of the federal government and the federal member states, met several times in 2017 and 2018, culminating in a meeting in Baidoa in June 2018. They reached a political agreement in principle on an electoral model based on proportional representation and a closed party list system. Nevertheless, the situation remains fluid and a broader political agreement still needs to be reached.

There has been some progress in defining the respective functions of the federal and state governments, particularly for the security and education sectors.

(i) **Security**. The 2017 (London) agreement on Somalia's national security architecture represented a first step in defining the respective responsibilities of the federal and state governments. The agreement calls for a Somali National Army (SNA) and a Somali police force, divided into Federal and State Police forces. The existing regional forces are to become part of the SNA or the State Police.

(ii) **Education.** Some progress has been made in defining the respective functional responsibilities of the federal and member state governments. In August 2019, the federal Ministry of Education, Culture and Higher Education (MoECHE) and representatives of the education ministries of the five member states signed a memorandum of understanding (MOU). The MOU calls for the federal ministry to develop national education policies and standards in collaboration with the states. The states are required to finance education at the state level, establish and manage the schools, and manage school personnel. At this time, only Puntland provides some form of public education. Instead, education has been provided by a multitude of institutions ranging from non-governmental organizations (NGOs), religious groups, the United Nations Children's Fund (UNICEF) and governments at various levels, including the federal, state and local authorities, as well as the private sector.

An interim agreement on the division of functions and assignment of revenues was reached in November 2019 in Kampala, which while marking a step forward, leaves several issues unresolved. Consistent with the Provisional Constitution, the agreement calls for the federal government's exclusive responsibilities to include national defense, foreign affairs, citizenship/immigration, and monetary policy. However, key functions such as education and internal security (police) are allocated concurrently to the federal government, the member states, as well as (undefined) regional governments, leaving the specific division of responsibilities in these sectors undefined. With respect to revenues, the agreement calls for 60 percent of 'shared revenues' to be allocated to the federal government, with the remaining 40 percent to be transferred to the states to finance development projects.

Several important steps have been taken to improve specific tax legislation and administration. The Revenue Administration Law, enacted in October 2019, states that laws governing the major taxes (including taxes on international trade) should be made at the Federal level, and 'the Ministry (of Finance) is to be responsible for the administration and the implementation of the revenue laws in line with the articles of the National Revenue Law.' Although the law does not stipulate which level of government will administer or retain any given tax, it nonetheless provides a legal basis for the federal government to work with the member states to harmonize tax policies across the country. It also calls for an additional law that would designate which level of government would collect the revenues from each source, keeping in line with Article 125 of the Provisional Constitution.

The enactment of the Revenue Administration Law and supporting measures to improve tax administration are expected to boost revenue collection, albeit from a low base. Revenues from taxes and fees were equal to 10.3 percent of gross domestic product (GDP) in 2018 (including the federal government, the five member states and Somaliland. This figure compares unfavorably to revenue performance in neighboring countries, such as in Kenya (18 percent) and Ethiopia (14 percent).

There are multiple challenges to raising revenues in Somalia, including tax competition amongst ports. Revenues from taxes on international trade are impeded by competition among ports, which encourages member states to reduce the customs duties at their ports in order to divert trade from Mogadishu. The result is a lose-lose situation, in which both the federal government and the member states impose rates that are lower than would otherwise be the case. Federal personal income taxes are levied only on government and selected private sector employees.

The quality of tax administration is also extremely weak. The federal inland revenue department is short of qualified staff and equipment. As such, it is reliant on manual, rather than electronic, processes. As a result, significant discretionary power is given to tax collectors. Several actions can be undertaken to increase tax revenues. On the policy front, the rate of customs taxes can be increased, and the coverage of the personal income tax can be extended to include wage and business income for all employees (public and private), with more attention to service sectors such as telecommunications and financial services. On the administrative front, better trained staff should be recruited, and processes should be automated, such as the electronic sharing of customs documentation.

Although revenues from natural resources are not large at the present time, there is some prospect that such revenues (particularly from petroleum) could become important in the future. How these revenues should be shared among the jurisdictions that comprise Somalia is controversial. The Provisional Constitution evades this issue, stating only that 'the 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.' At the aforementioned Baidoa National Security Council meeting in June 2018, an agreement was reached between the FGS and FMS regarding the division of oil and other mineral revenues between the federal government, producer FMS, producer districts and non-producer FMS.

The revenue-sharing arrangements vary depending on whether the source of oil is on-shore or off-shore, as well as according to the source of revenue (see Table 1.) In the case of offshore oil, for example, the federal government would receive 55 percent of the government's share of profits from oil, with 25 percent going to the FMS adjacent to where the oil was extracted offshore, ten percent to the district adjacent to where the oil was extracted offshore, and the remaining ten percent being shared between all other non-producer FMS (that is, two percent to each non-producing FMS). Revenue shares from on-shore oil extraction would differ with a greater share of the profit going to the producing FMS and districts, as would shares for rents, signing bonuses, and so on. Amendments to the 2008 Petroleum Act recently passed by the House of the People require petroleum revenues to be shared in line with the Baidoa Agreement.

Table 1: Proposed Distribution of Oil Revenues among Governmental Tiers (%)

Details	FGS	P*. FMS	P*.District	NP FMS
Investment Fund				
Offshore	55	25	10	10
Onshore	30	30	20	20
Royalties	40	40	10	10
Signing Bonus	40	60		
Surface Rents	30	50	20	10
License fees	50	50		
Production Bonuses	30	50	10	10
Corporate Income Taxes	100			
Export Taxes	60	40		
Capital gains	50	30	20	
Seismic Data	50	50		
Capacity Building	50	50		
Local Community	?%	30	70	

Source: Baidoa agreement. Note: FGS= Federal Government of Somalia; FMS= Federal Member States; NP=non-producer; P= producer.

4. Discussions

At present, the former Somalia functions, in most respects, as seven separate political jurisdictions: the 'federal government' whose authority is largely confined to Mogadishu, the five member states, and Somaliland. Despite 20 years of effort, the various regional interests have not managed to reach definitive agreements regarding the division of expenditure responsibilities between the federal and FMS governments, the assignment of revenues between them, and/or the design (if any) of a fiscal transfer system. Indeed, goods imported from one FMS are taxed in another FMS as part of revenue-generating activities.

Looking ahead, different governance options can be envisioned. Theoretically, the former Somalia could be permanently divided into seven independent countries, linked to each other only through a customs union along the lines of the European Economic Community from 1957 to 2009. Or it could become a defensive pact along the lines of the North Atlantic Treaty Organization (NATO). Both types of options are inconsistent with Somalia's efforts to reconstitute the nation-state. At the opposite extreme, Somalia could be reconstituted as a unitary state. This option is inconsistent with demands for some degree of regional autonomy. This chapter therefore rejects both extremes and instead focuses on intermediate, federal solutions that combine varying degrees of federal and state power.

The governance options presented below presume that the immediate, overriding objective of any solution is the prevention of further military conflict. A second objective is the creation of a stable structure of government that can provide internal security and a minimum of government services on a reasonably efficient basis. Given the extreme poverty of some member states, this latter objective would imply the provision of such services either directly by a central government or through a system of transfers from the federal government to the poorest member states. Another objective is freer trade to facilitate the free movement of people and goods throughout the country, which would help to raise incomes and enhance economic growth.

When considering the options, it is important to recognize that the context in Somalia is still evolving. Firstly, the overall size of the resource envelope is likely to increase over the short-to-medium term. Reforms to tax policy and tax administration are expected to result in enhanced revenues from customs duties and personal income taxes. Somalia's reengagement with the international community facilitated through debt relief as part of the Heavily Indebted Poor Countries (HIPC) initiative is most likely to result in higher budgetary grants. The potential exploitation of natural resources, particularly oil, would also increase revenues. Secondly, the increase in these revenues means that the capacity of the public sector (in the FGS, FMS and Somaliland) to increase expenditures on national priorities — such as education, health and transport infrastructure — will increase.

In the short term, though, any reform scenario should begin by addressing two pressing issues. The first is the division of responsibility for financing and managing internal security. As noted, both the federal government and the states perform this function, which appears to consume most of their respective budgets. No rational progress on the assignment of revenues between the two tiers can be made until the division of responsibilities for financing this function can be determined. There are many ways to resolve this issue. In theory, the federal government could be granted sole responsibility for defense against both external and internal threats.

Another issue concerns the administration and allocation of tax revenues from international trade. While states that derive most of their revenues from taxes on international trade taxes would want to retain them, there is a strong case for assigning this revenue source solely to the federal government. First, it would allow Somalia to implement a common tariff policy, avoiding a race to the bottom whereby each member state (despite federal legislation to the contrary) is free to offer lower rates to attract trade. Second, it would remove the random element of geography from the determination of each state's tax revenues, where access to ports, airports, or a border with a foreign trading partner generates taxes from international trade.

<u>Discussion One</u>: No Reform

If no progress is made on these governance issues, then Somalia would be left in its current situation, in which each jurisdiction finances whatever functions it can afford from its own revenues. In the short term, the federal government's principal function (other than 'administration') would continue to be limited to national security, which would be financed with taxes collected in the Benaadir District as well as donor support. Similarly, outside of Mogadishu, the individual member states would spend most of their budgets on internal security, and would be reliant on their own tax bases, donor support, and a trickle of grants from the federal government. Over the longer term, as the yield of domestic taxes increases, the member states could increase spending on non-security-related functions including education, transport and health. The states with stronger tax bases would expand spending in these sectors relatively quickly; however, those without such tax bases would fall further behind. The federal government, for its part, could increase spending on these functions, either in Mogadishu and/or in the member states.

The current status option has several drawbacks. First, it does not resolve the ambiguities in the division of functions between the federal government and the member states. Second, it does not resolve the problems associated with what is, de facto, a decentralized tax on international trade. However, most importantly, in leaving each jurisdiction to fend for itself, it would leave several states with very limited resources. As shown in Figure 6, Galmudug, Hirshabelle and Southwest have virtually no tax revenues of their own. Because these jurisdictions lack major ports, their revenues from taxes on international trade will continue to be minimal, even as the national economy grows. Furthermore, because most growth in the formal economy will presumably occur in Mogadishu and larger cities of Puntland and Jubbaland, revenues from the personal income taxes (PIT) or other domestic taxes will be limited in the other member states as well.

A much preferable option would be to fundamentally restructure the relationship between the federal government and the member states. This would entail centralizing the tax on international trade, clearly delimiting the respective responsibilities of the federal and state governments. It would also involve organizing a system of transfers to ensure that all member states have the wherewithal to provide the functions assigned to them. Two functional decentralization options bear consideration.

<u>Discussion Two:</u> Functional Federation

Under the functional federation approach, the majority of public sector functions would be assigned to the states. This would include responsibility for internal security, primary and secondary education, primary health care and intra-state transportation. (The individual states, for their part, could delegate some of these functions to their respective local governments.) The federal government's functions would be limited to national defense, along with foreign affairs, international and interstate transport (for example, international airports, highways and railroads), monetary and fiscal policy, and the regulation of the banking system. If such an approach was followed in Somali, the permanent Constitution would resemble those of many other federations including Brazil, Ethiopia, and Nigeria.

There are multiple fiscal implications of option 2: With the majority of functions assigned to the state level (and the Mogadishu local government) and the absence of strong tax bases in the three poorer member states, option 2 would require a large-scale transfer system. Centralized revenues from taxes on international trade could be used to finance a transfer system, supplemented with resources from grants. Over the longer term, there could be additional revenues from federal corporate income tax or a production-based value-added tax (VAT). In the short term, any attempt to centralize taxes from international trade would reduce the revenues generated by the states that have ports. Experience with similar reforms in other countries suggests that, at the outset, the transfer will have to compensate them for this loss. For example, in the first year, the transfer to each state might be equal to the amount of revenues generated from taxes on international trade in the year prior to the reform. While such an approach would not reduce disparities, an equalization formula could be introduced over time. A hold-harmless provision could be specified, such that the amount of the transfer would always be at least equal to the amount the state collected in the year prior to the reform.

There are innumerable ways to implement a large-scale transfer system. The most complex and ambitious form of an equalization transfer is one that attempts to fill the gap between the expenditure needs of each jurisdiction, based on the costs of particular service standards, as well as the ability of each jurisdiction to finance those needs from its own tax bases. Although this approach is used in several former members of the Soviet bloc (as well as Ethiopia), it has several drawbacks. First, it is extremely difficult to calculate expenditure needs, as the costs of meeting service standards for individual functions varies across jurisdictions. Moreover, the costs of meeting any uniform set of national standards is likely to far exceed the available resources, requiring some arbitrary form of rationing.

Alternatively, the federal government could calculate the education sector transfer based on enrollment, transferring a fixed amount per pupil to each state based on the number of pupils attending classes. In the case of health, the transfers could cover both the salaries of health care workers and basic medicines and supplies. Again, the distribution of such funding could be based on authorized inputs (for example, the number of authorized health care workers) or on an indicator of demand (for example, the number of registered patients).

Either of these transfer approaches to the social sectors would require close supervision by the federal government, since they contain perverse incentives. Under the first option, states would have an incentive to pressure the federal government to authorize more staff than they need. Under the second option, states would have an incentive to overstate enrollment (in the case of schools) or registered patients (in the case of health care). In this context, any attempt to establish earmarked transfers should be held off until the federal government has the administrative capacity to limit such behavior.

Possible tax sources for the states: In theory, even with the federal government monopolizing customs taxes, states (and the Mogadishu local government) would have a wide range of options. These would include personal and corporate income taxes, broad-based taxes on goods and services (for example, a VAT or a retail sales tax), taxes on the sale of specific goods and services), and various forms of property taxation. However, the range of options is in fact more limited for two reasons.

<u>Discussion Three:</u> Centralization of Major Functions

Another option would entail having the federal government assume direct responsibility for a wider range of services. In addition to national security, this might include education, health care, and transport infrastructure. The federal government, for example, could assume direct responsibility for primary and secondary education, recruiting and managing teachers and paying their salaries. This is a common approach in unitary countries (such as France) where the responsibilities of local governments are limited to operating and maintaining school buildings. As in discussion 1, this would require most taxing power to be concentrated at the federal level. However, unlike discussionsz1, this would not require a major system of intergovernmental transfers. Instead, spending on centralized services would be financed directly by the federal budget. In choosing between the options, states would have to decide whether they would prefer to give up management responsibility for these functions in return for escaping the burden of paying for them.

5. Conclusion

Effect of federalist debates on Political Stability

The study concludes that federalism is considered as a comprehensive system of political

relationships which emphasizes the combination of self-rule and shared rule within a matrix

of constitutionally dispersed powers

Without basic consensus on some form of federal principles and processes it is likely that the

concept could become too flexible and any regime could call its system 'federal' on the basis

of the mere existence of the structures alone

The study concludes that federalism not only embraces individual citizens, with an equal

entitlement to vote, but also individual territories or states or provinces, which also enjoy

some form of equal influence at the federal center'

Effect of international interventions on federalism on Political Stability

The study also concludes that diplomatic mediation in Somalia has sometimes confused these

episodic processes with moving to the next stage of the resolution, which is the establishment

of a transitional government.

The haste to create a central government is perhaps informed by what Moller describes as the

"relentless quest for state building" because the entire international system is constructed

around states to such an extent it is unable to handle stateless territories inhabited by people

who cannot be classified as citizens of any state.

The study concludes that at times, diagnosing the Somali conflict has been influenced by

external factors and interests not relevant to the conflict.

Effect of failed federal government on Political Stability

The study concludes that the fall of a government does not necessarily signal the collapse of a

state in democratic societies. The basic assumption is that the threat of state collapse

unsurprisingly arises in countries in which the preconditions for state formation and

maintenance was most uncertain in the first place and derives from the relatively recent

assumption that the entire world should be divided into states.

It also concludes that the collapse of the Somali state was not a chance event, but a process, which began at the time of independence in 1960. Thus, it can be stated that the state

“collapse was triggered when the Siad Barre government fell in 1991.

When the Somali state collapsed in 1991, there was no formidable political formation capable

of filling the vacuum left by the weak government of Siad Barre. The country was

fragmented in terms of clan lineage and patronage and the devastating drought and ensuing

famine introduced food security as a source of conflict.

The study furthermore concludes that another element consistent with, the concept of an

intractable conflict concept was introduced: the changing goalpost in the life cycle of such a

conflict.

6.Summary and Recommendations

Nearly 30 years after the collapse of the Siad Barre government, the regional interests governing separate parts of Somalia have yet to devise a workable governance arrangement for the country as a whole. Although there has been progress in the form of the 2012 Constitution and certain agreements on specific issues, critical decisions about the role of the federal government vis-a-vis the states have yet to be reached.

A federal approach, consisting of (1) a central government whose powers and resources are deliberately constrained and (2) member states, with a wider mandate and guaranteed access to federal funding, would appear to be a promising way of gaining the benefits of a national government while also accommodating regional demands for autonomy.

The federal approach would require a definition of the functions and resources of each of the two tiers of government. In the short term, this involves two issues. The first is the division of responsibility for security. At present, while the federal government is nominally responsible for national security, the member states also maintain their own armed forces. Under the terms of the 2017 London Agreement, the federal government would be responsible for national defense, but both tiers would play a role in maintaining internal security. In working out the details of such an arrangement, Somalia could consider the examples of Brazil and Ethiopia.

Another immediate issue concerns tax revenues from international trade. There are strong arguments for giving the federal government exclusive power to impose customs taxes. In the short term, states that are reliant on customs taxes would have to be compensated. This could be accomplished through a federal transfer, funded in part from the federal government’s newly-expanded customs revenues. Such a compensation transfer should be considered temporary, however.

Over time, as revenues from customs taxes and domestic taxes increase, along with possible revenues from oil, the ability of the public sector to expand spending on non-security related functions will increase. These functions would include education, transportation, and health care. This will again require a definition of the respective responsibilities of the federal and state government in these sectors. One option is to assign responsibility for managing these functions to the state level, but assign responsibility for financing them to the federal level.

To this end, the federal government could establish a transfer aimed at ensuring that even the poorest states have the wherewithal to provide a minimum level of the services for which they are responsible. This could be phased in as the compensation element of the transfer is phased out. In designing such a transfers, elaborate formulas should be avoided. There is a strong case for allocating transfers to the states solely on the basis of population, at least until such time as the federal government is able to accurately monitor the functional allocation of state expenditures. Even afterward, attempts to fine-tune distribution formulas to reflect supposed variations in unit costs or revenue potentials should be avoided.

In this connection, there is a case for re-visiting the Baidoa Agreement regarding the distribution of revenues from the exploitation of oil and other mineral resources. Consideration could be given to reducing the share of oil and gas revenues allocated on the basis of derivation and increasing the proportion that is used to reduce disparities in the per capita revenues of the member states.

In order to supplement federal transfers and fund discretionary expenditures, individual states should be authorized to impose direct taxes. Given the informal nature of state economies, the options for raising significant revenues through such taxes are limited. However, there are two promising candidates: the personal income tax, which would be largely imposed through withholding from the employees of governmental organizations and large enterprises, and a retail sales tax.

Some of the agreements on these issues should be enshrined in the revised Constitution; others in ordinary law. Apart from establishing the structure of the state (the organization of Parliament, the role of the head of state, the federal election system), a federal constitution typically provides the broad outlines of the relationship between the central government and the states. These provisions are intended to be permanent—or at least difficult to change. To this end, the rules for amending a constitution typically establish a much higher threshold than is the case for ordinary legislation. Somalia's 2012 Constitution is typical. It requires a two-thirds majority in both houses of Parliament to amend the constitution. Ordinary legislation requires only a majority vote in both houses and the signature of the president.

Regarding the relationship between the federal government and the member states, the constitution should include only those provisions that are not intended to be frequently revised. This would include, for example, a broad definition of the functional responsibilities of each of the two tiers, recognizing that ordinary legislation may permit the federal government to regulate functions nominally assigned to the states. By the same token, the constitution should define the respective tax instruments assigned to the federal and state governments, while leaving the details governing tax rates and tax administration to ordinary law.

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