



Institute of Public
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IPF POLICY PAPER

FISCAL DECENTRALIZATION IN SOMALIA:

COMPARATIVE INSIGHTS AND A POLICY
FRAMEWORK FOR EMPOWERING LOCAL
GOVERNANCE

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ABSTRACT

This paper examines Somalia's evolving fiscal federalism with a focus on enhancing the decentralization of fiscal responsibilities to improve local governance and service delivery. Drawing on official Somali government strategy documents and international comparisons from Germany, Ethiopia, Kenya, and Nigeria, the study analyses the constitutional basis, institutional arrangements, and revenue assignment practices in Somalia. It reviews both domestic and international literature, presents a detailed methodology of policy analysis, and discusses empirical findings on intergovernmental fiscal relations, functional assignments, and transfer mechanisms. A case study of Puntland's Local Development Fund is used to illustrate successes and challenges. The paper concludes with policy recommendations for the Federal Government, Federal Member States, local governments, and international donors. These recommendations aim to guide legal reforms, build institutional capacity, and establish transparent fiscal coordination for a more equitable and sustainable decentralization framework.

01 | INTRODUCTION

Somalia's provisional constitution, adopted in 2012, established a federal system intended to distribute power and resources among a central government and multiple subnational entities. Fiscal decentralization—the allocation of revenue sources and expenditure responsibilities across government tiers—is considered pivotal for bringing governance closer to the people, improving public service delivery, and mitigating long-standing grievances from centralized rule [1].

However, the constitutional framework provides only broad guiding principles and leaves many details—such as revenue assignment, intergovernmental transfers, and borrowing authority—to be negotiated by the Federal Government of Somalia (FGS) and Federal Member States (FMS) [1][2]. This paper examines the current state of fiscal decentralization in Somalia and, by incorporating comparative insights from Germany, Ethiopia, Kenya, and Nigeria, proposes a policy framework to support a more structured and effective system.

02 | Overview of Fiscal Decentralization in Somalia (Current State)

Somalia's fiscal federalism remains in an emergent stage. The Provisional Constitution outlines a basic federal structure with two levels of government (FGS and FMS) and implies that local governments should play a role in service delivery. However, key fiscal responsibilities—including tax collection and expenditure management—are not clearly divided by law. As a result, fiscal powers have been negotiated on an ad hoc basis through periodic intergovernmental forums, such as the Finance Ministers' Fiscal Forum and the National Economic Council [3].

Legal and Policy Framework

The constitution reserves certain exclusive federal functions (e.g., defence, foreign affairs) while implying that other responsibilities are devolved to states or shared. Yet, the absence of a comprehensive fiscal federalism law means that assignments and revenue-sharing remain largely informal. Recent policy initiatives (e.g.,

the Fiscal Decentralization Strategy and the MoIFAR Framework) are designed to clarify these arrangements, but final legislative action is pending [4].

Institutional Arrangements

Intergovernmental fiscal coordination is managed through temporary forums rather than permanent bodies. The FGS and FMS convene regularly to negotiate revenue-sharing arrangements, but no binding transfer mechanisms exist. Local governments, where they function, have limited capacity and are not fully integrated into the fiscal system. Pilot projects in Puntland, for example, demonstrate progress in local revenue mobilization and the potential for district-level budgeting, yet these remain isolated successes [5].

Revenue Assignments and Transfers

Currently, the FGS retains the majority of revenue through central collection of customs duties, income taxes, and donor funds, while FMS generate revenue through localized taxes (e.g., port fees, market taxes) in their territories. However, formal rules to share these revenues systematically with local governments are missing. Existing transfers are often informal and subject to political negotiation. Table 1 (see below) provides a simplified overview of the revenue flows among the FGS, FMS, and local governments.

Table 1. Stylized Overview of Revenue Sources and Fiscal Transfers in Somalia

Level	Key Revenue Sources	Transfers Received	Transfers Given
Federal Government	Customs duties; federal sales taxes; donor grants; telecom fees; income tax on federal employees.	Occasional donor-based budget support; nascent formula-based transfers to FMS (pilot stage).	Limited ad hoc support to FMS (e.g., security sector payments).
Federal Member States	Port charges; sales taxes; business licenses; checkpoint fees.	Some federal transfers via negotiated agreements; donor-funded grants in specific sectors.	Generally, no formal transfers to local governments; occasional ad hoc subsidies.
Local Governments	Property taxes; market fees; business license fees; minor user charges.	Very limited, often donor-driven support; irregular state subsidies.	N/A

Table 1: Overview of current fiscal flows (adapted from government strategy documents [4][5]).

Ongoing Policy Initiatives

Key initiatives include efforts to develop a comprehensive National Decentralization Policy and pilot fiscal transfer mechanisms. The Federal Government, in collaboration with FMS and donor partners, has begun designing a formula-based transfer system intended to equitably distribute revenues among states. Additionally, donor-funded projects such as the World Bank's RCRF and the UN Joint Programme on Local Governance are supporting capacity building and system harmonization at all government levels [6].

This section draws on experiences from Germany, Ethiopia, Kenya, and Nigeria to provide context and lessons for Somalia's fiscal decentralization.

3.1 Germany



Federalism in Action: Germany's Balanced Tax System

Germany's federal system is characterized by a well-defined division of tax powers and robust intergovernmental transfers. The Basic Law (Grundgesetz) guarantees local self-government and delineates shared responsibilities between the federal government and the Länder (states) [7]. Revenue-sharing is highly formula-driven, with major taxes such as income tax and VAT split between federal and state governments, and an elaborate equalization mechanism ensures that disparities are minimized. Municipalities also benefit from state-level equalization funds. These institutional arrangements have successfully reduced regional inequalities following reunification and serve as a model of solidarity and legal clarity [7][8].

3.2 Ethiopia



Block Grants and Regional Autonomy: Ethiopia's Fiscal Experience

Ethiopia's ethnic-based federalism provides an instructive contrast. The 1995 Constitution grants substantial autonomy to regional states, which depend heavily on federal block grants due to limited own-source revenues. Ethiopia uses a formula-based block grant system (incorporating population, poverty, and revenue effort indicators) to address both vertical and horizontal fiscal imbalances. Although this approach has contributed to regional development, it has also been a source of political tension, as states sometimes contest the fairness of the allocations. Ethiopia's experience underscores the need for a balanced and transparent formula that accounts for both capacity and needs [9].

3.3 Kenya



Devolution and Fiscal Empowerment: Kenya's County Experience

Kenya's devolution, established by the 2010 Constitution, created 47 county governments with significant fiscal autonomy.

Counties receive an equitable share of national revenue – guaranteed to be no less than **15%** – through a formula that incorporates population, land area, poverty, and other factors. Additionally, counties have legal authority to levy certain local taxes and benefit from conditional and unconditional grants. Strong constitutional protections and independent institutions, such as the Commission on Revenue Allocation (CRA), have ensured the sustainability of county finances. Kenya’s experience demonstrates how well-designed fiscal rules and robust oversight can empower local governments and promote inclusive development [10]

3.4 Nigeria



Revenue Sharing and Local Fiscal Struggles: Nigeria’s Lessons on Decentralization

Nigeria’s revenue-sharing system is complex due to its oil-dependent economy. The Constitution allocates revenues among the federal government (**approximately 52.7%**), **states (26.7%)**, and **local governments (20.6%)**, with additional derivation funds (about 13% of oil revenues) earmarked for oil-producing states. Despite these statutory allocations, in practice, local governments have long struggled to access their funds due to state-level control and weak institutional mechanisms. Recent judicial interventions have sought to enforce local fiscal autonomy by mandating that funds allocated to local governments be released directly, without undue state interference. Nigeria’s experience highlights the challenges of enforcing decentralized fiscal rights in a politically centralized environment, offering lessons on the importance of clear legal frameworks and independent oversight [11].

04 | Methodology

This study uses a qualitative policy analysis approach based on document analysis and comparative review. Primary data were drawn from Somali government documents (e.g., the Fiscal Decentralization Strategy, MoIFAR Framework, Puntland policy papers) and supplemented by international sources from Germany, Ethiopia, Kenya, and Nigeria. Content analysis was applied to extract themes such as legal frameworks, institutional arrangements, revenue assignments, and intergovernmental transfer mechanisms. Comparative analysis further illuminates similarities and differences, with visual aids (tables and charts) created to summarize data across the different systems. This methodology provides a comprehensive understanding of both the domestic context and international best practices in fiscal decentralization.

05 | Empirical Findings

5.1 Intergovernmental Fiscal Relations in Somalia

Somalia's current system relies on periodic intergovernmental forums, such as the Finance Ministers' Fiscal Forum, to negotiate fiscal arrangements. While informal practices dominate, recent initiatives indicate a move toward formalization. For example, pilot formula-based transfers have been introduced to share federal revenues with FMS, though local governments remain largely excluded from such arrangements. This ad hoc system, while effective in maintaining dialogue, lacks the legal force of a comprehensive fiscal federalism law [2][3].

How inter-governmental fiscal transfers (IGFT) actually work in Somalia today

Level / Instrument	How the money is shared	Legal/Policy basis	Most recent practice (FY 2023-24)	Key issues noted by MoF & IMF
Vertical split – between the Federal Government of Somalia (FGS) and the six Federal-Member States (FMS) plus Banadir Regional Administration (BRA)	60 % FGS – 40 % FMS/BRA of all on-budget donor budget-support grants (mainly World Bank, EU BS & AfDB TSF). Deducts agreed fiduciary fees first.	2016 Inter-Ministerial Finance-Ministers’ Forum communiqués; reconfirmed in successive Budget Framework Papers (most recently FY-2025)	US \$90 m transferred in 2023/2024 (FGS→FMS/BRA). Transfers are released ad hoc basis through the Treasury Single Account.	Heavy reliance on external grants; domestic-revenue based transfers still ad-hoc for port less states.
Horizontal formula – how the 40 % is divided among Puntland, Jubbaland, Southwest, Galmudug, Hirshabelle & BRA	The five-parameter performance-linked formula below (Table 1).	First set out in 2019 and codified in MoF Financial Governance Report 2023 & the FY-2025 Budget Strategy Paper	Applied without change in FY 2021-24 disbursements. A joint FGS/FMS technical team scores each parameter annually; results are endorsed by FMFF published on MoF portal.	Formula only covers donor budget-support. PEFA self-assessment report is not all the time used where sharing the budget support grants
Special-purpose transfers	(i) BRA receives 15 % of Mogadishu port revenues ; (ii) natural-resource sharing deals under 2020 Petroleum Act & 2023 Fisheries Act; (iii) project-specific World Bank programmes routed through FGS.	Individual resource-sharing agreements & sector laws.	BRA port-share averaged US \$18 m/yr (2021-23). Petroleum shares not yet material due to early production stage & fisheries licenses fees are shared based formula agreed FGS/FMSs.	Execution highly uneven; Transfers are not timely reporting from some FMS-run ports & fisheries.
Fiscal-gap top-ups	3 % fiscal gap allocation pool inside the formula reserved for Galmudug, Hirshabelle & Southwest (the lack of operational ports, low-revenue states).	Same MoF guidance as horizontal formula.	Disbursed proportionally to the three eligible states each year.	Very small envelope – does little to offset structural imbalances.

What this means in practice

Consensus on Transfer Formula – The Federal Government of Somalia (FGS) and the Federal Member States (FMS) have agreed to shift from the informal gentleman’s agreement on transfer-sharing to a structured transfer formula. As a result, Intergovernmental Fiscal Transfers for both FGS and FMS are now incorporated into the annual budget allocation. Performance incentives are modest – Budget support is shared based individual FMS performance on the indicators resulting to PFM reform agenda and a 2-point swing in the ranking moves at most 0.3 % of the total pool; MoF notes limited behavioural change so far.

Equity questions remain – port-owning states (Puntland, Jubbaland) still enjoy far higher own-revenue; the 3 % equalisation parameter is too small to close horizontal gaps.

Next reform steps under discussion (2025-27)

1. Broaden the vertical pool to include a share of domestically mobilised taxes like (Income Taxes) once collection passes US \$400 m/yr.

2. Add needs-based variables (population, poverty headcount, service coverage) alongside performance scores. **ipsum**

3. Institutionalize Inter-governmental Fiscal Forums to Commission: to replace the ad-hoc Finance-Ministers Forum and arbitrate formula reviews.

4. Publish transfer scorecards on the MoF portal in Somali and English to raise transparency and citizen oversight.

5.2 Revenue Assignments and Transfer Mechanisms

The FGS collects the majority of revenue from customs duties, income taxes, and donor funds, while FMS generate revenues from localized taxes. However, formalized revenue-sharing mechanisms are minimal, and transfers are largely ad hoc. Table 1 (above) illustrates these imbalances. Recent efforts to design formula-based transfers—using criteria such as population, developmental needs, and fiscal capacity—signal progress toward more equitable distribution, though implementation remains at a pilot stage [4][6].

5.3 Institutional and Legal Frameworks

The constitutional and legal framework is provisional. The 2012 Constitution sets broad principles but leaves detailed assignments to be negotiated. As a result, intergovernmental fiscal coordination is managed by temporary forums and donor-supported initiatives. FMS have enacted Local Government Laws that theoretically empower districts; however, in practice, fiscal control is centralized at the state level. Efforts are underway to draft a comprehensive Fiscal Federalism Law and to create permanent institutions (e.g., a National Fiscal

5.3 Institutional and Legal Frameworks

Donor-funded projects such as the UN Joint Programme on Local Governance (JPLG) and the World Bank's RCRF have been pivotal in piloting new models of fiscal transfers and capacity building. In Puntland, the Local Development Fund (LDF) has successfully channeled funds to local projects, demonstrating the potential benefits of a well-structured fiscal decentralization system. These pilots serve as important examples for broader application across Somalia [7][8]. (Commission) that will manage revenue-sharing and dispute resolution [4][5].

5.4 Donor and Pilot Programs

Donor-funded projects such as the UN Joint Programme on Local Governance (JPLG) and the World Bank's RCRF have been pivotal in piloting new models of fiscal transfers and capacity building. In Puntland, the Local Development Fund (LDF) has successfully channeled funds to local projects, demonstrating the potential benefits of a well-structured fiscal decentralization system. These pilots serve as important examples for broader application across Somalia [7][8].

06 | Comparative Analysis: Lessons from Germany, Ethiopia, Kenya, and Nigeria

The international cases provide instructive contrasts:

GERMANY

Germany demonstrates how a constitutional commitment to local autonomy, combined with well-established equalization mechanisms and formula-driven transfers, can create a robust fiscal federal system [7][8].

ETHIOPIA

Ethiopia shows that even in fragile contexts, formula-based block grants can be used to address regional inequities, although political tensions may arise if allocations are perceived as unfair [9].

KENYA

Kenya's devolution underscores the value of strong legal guarantees and independent oversight in ensuring that sub-national governments receive a fair share of national revenues. Kenya's experience also highlights the benefits of public participation in budgeting and transparency in fiscal transfers [10].

NIGERIA

Nigeria illustrates the challenges of implementing constitutional revenue-sharing in a resource-rich yet politically centralized environment. Despite statutory allocations, practical challenges persist in ensuring local governments receive their rightful share, though recent court rulings have begun to enforce these rights [11].

Key Lessons for Somalia:



- 01** Establish clear legal provisions for revenue assignments and a formula-based transfer system
- 02** Create permanent institutions for intergovernmental fiscal coordination.
- 03** Guarantee sub-national autonomy by protecting local government fiscal rights and integrating them into the decision-making process.

- 04 Incorporate equity and conflict-sensitivity into transfer formulas to ensure marginalized regions receive adequate support.
- 05 Gradually build local capacity while aligning donor programs with national policies.

07 | Discussion

The comparative analysis reveals a clear imperative for Somalia to move from an ad hoc, negotiation-based system to one grounded in clear legal frameworks and institutionalized fiscal processes. While Germany's model emphasizes constitutional guarantees and robust equalization, Ethiopia and Nigeria show that even in fragile contexts, a well-designed transfer formula can promote equity – though with challenges related to political influence. Kenya's devolution offers an example of how legal empowerment and public accountability can ensure that local governments have the fiscal capacity to deliver services. Somalia's current system, by contrast, is characterized by centralization at both the federal and state levels, with local governments receiving insufficient funds. The ongoing policy initiatives (e.g., the Draft Fiscal Decentralization Strategy and MoIFAR Framework) aim to address these issues, but progress depends on finalizing constitutional reforms and building the necessary institutional capacity. Ultimately, the success of fiscal decentralization in Somalia will hinge on the willingness of all stakeholders to embrace a rules-based, transparent system that aligns incentives and ensures accountability across all levels of government.

8.1 For the Federal Government (FGS)

Legal Codification: Finalize and enact a comprehensive Fiscal Federalism Law that clearly delineates revenue assignments and establishes a formula-driven transfer system.

Institutional Development: Establish a permanent Intergovernmental Fiscal Commission to oversee revenue sharing and dispute resolution.

Enhanced Coordination: Strengthen intergovernmental forums (e.g., Finance Ministers' Fiscal Forum, NEC) and integrate them into the national budgeting process.

8.2 For Federal Member States (FMS)

Harmonization of Laws: Align state-level revenue and local government laws with the national framework to reduce overlaps and ensure consistency.

Fiscal Transfer Systems: Develop and implement formal, formula-based transfers to local governments.

Capacity Building: Invest in upgrading local financial management systems and administrative capacities.

8.3 For Local Governments

Revenue Mobilization: Enhance local taxation systems (e.g., property taxes, market fees) and modernize collection methods.

Governance and Accountability: Establish transparent budgeting and financial reporting mechanisms and actively participate in intergovernmental dialogues.

Service Delivery: Prioritize essential services using available resources while building capacity for future responsibilities.

8.4 For International Donors

Alignment of Programs: Ensure donor-funded projects align with national decentralization policies and support the transition to government-led fiscal transfers.

Technical Assistance: Provide sustained technical support to build local and state-level fiscal capacity.

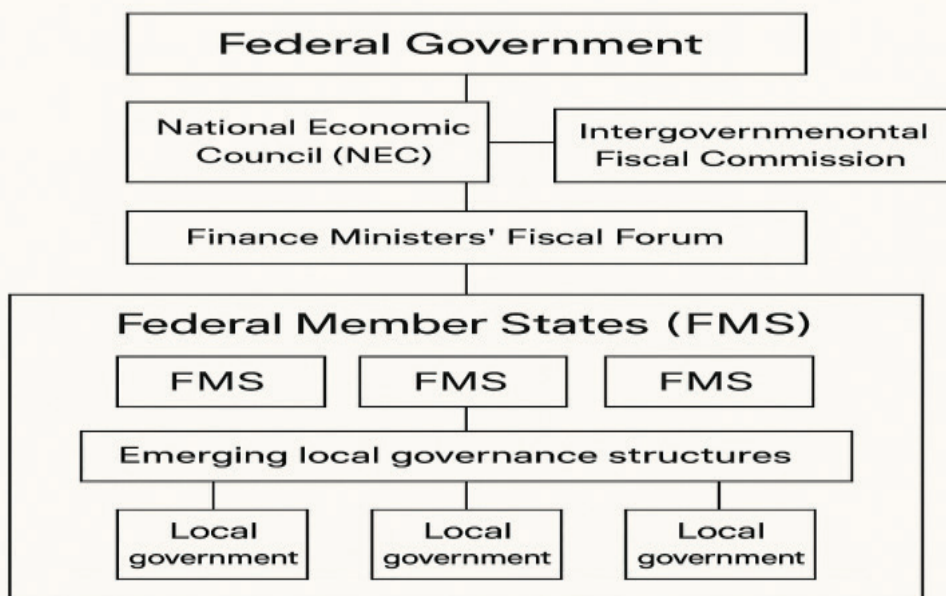
Conditional Funding: Link continued funding to demonstrable progress in implementing fiscal reforms.

09 | Conclusion

Somalia's journey toward effective fiscal decentralization is marked by significant progress amid persistent challenges. The provisional constitutional framework provides guiding principles, but the lack of detailed legal provisions and institutional capacity has necessitated an ad hoc approach to revenue sharing. Comparative experiences from Germany, Ethiopia, Kenya, and Nigeria offer valuable lessons on the importance of clear legal frameworks, formula-driven transfers, and robust institutions to ensure that all levels of government can fulfill their responsibilities. By finalizing constitutional reforms, establishing dedicated fiscal commissions, and aligning donor efforts with national policies, Somalia can develop a fiscal decentralization system that promotes equity, improves service delivery, and strengthens national unity. The path ahead requires political will, technical capacity, and sustained commitment to building a transparent and effective federal system.

Figure 1. Institutional Framework of Intergovernmental Fiscal Relations in Somalia

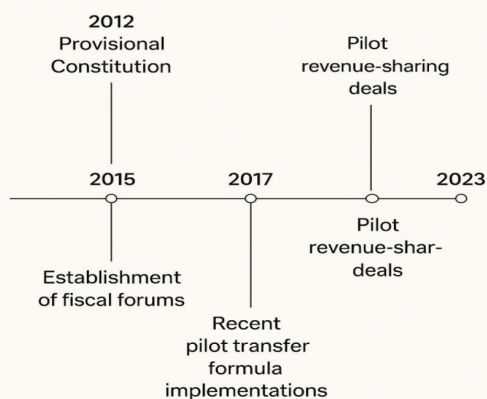
Figure 1. Institutional Framework of Intergovernmental Fiscal Relations in Somalia



(A diagram illustrating the relationships among the Federal Government, FMS, and local governments. Key bodies include the National Economic Council (NEC), the Finance Ministers' Fiscal Forum, the proposed Intergovernmental Fiscal Commission, and the emerging local governance structures.)

Figure 2. Timeline of Key Fiscal Decentralization Milestones in Somalia (2012–2023)

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(A timeline marking major events such as the 2012 Provisional Constitution, formation of FMS, establishment of fiscal forums, pilot revenue-sharing deals, and recent pilot transfer formula implementations.)

Table 2. Stylized Overview of Revenue Sources and Fiscal Transfers in Somalia

Level	Key Revenue Sources	Transfers Received	Transfers Given
Federal Government	Customs duties; federal sales taxes; donor grants; telecom fees; income tax on federal employees.	Occasional donor-based budget support; nascent formula-based transfers to FMS (pilot stage).	Limited ad hoc support to FMS (e.g., security sector payments).
Federal Member States	Port charges; sales taxes; business licenses; checkpoint fees.	Occasional federal transfers via negotiated agreements; donor-funded grants in specific sectors.	Generally, no formal transfers to local governments; occasional ad hoc subsidies.
Local Governments	Property taxes; market fees; business license fees; minor user charges.	Very limited, often donor-driven support; irregular state subsidies.	N/A

Table 2: Adapted from Somali government strategy documents [4][5].

Table 3. Comparative Fiscal Decentralization Overview

Country	Governance Structure	Revenue Mechanism	Transfer	Local Autonomy Features
Germany	Federal republic with 16 states and numerous municipalities	Formula-based sharing of joint taxes; extensive equalization system ensuring fiscal balance.		Constitutionally guaranteed local self-government; robust municipal equalization funds.
Ethiopia	Ethnic-based federal republic; regional states and woredas	Block grants based on a formula (population, poverty, revenue effort) from the federal budget.		Regional autonomy enshrined in the constitution; however, woredas often face administrative constraints.
Kenya	Devolved unitary state; 47 counties	Equitable share guaranteed by the Constitution; additional conditional grants; Equalization Fund for marginalized counties.		Counties have distinct corporate status with legal autonomy and strong oversight bodies.
Nigeria	Federal republic; 36 states plus local governments	Constitutional revenue sharing (52.7% federal, 26.7% states, 20.6% local), with additional derivation funds for oil-producing states.		Local governments face challenges due to state control; recent court rulings reinforce local fiscal rights.

Table 2: Synthesized from international and regional experiences [7][9][10][11].

11. Footnotes

1. The provisional Somali Constitution provides broad federal principles but leaves detailed fiscal arrangements to be negotiated between FGS and FMS.
2. Intergovernmental fiscal forums in Somalia have been instrumental in piloting revenue-sharing agreements, albeit on an informal basis.
3. The fisheries revenue-sharing deal in 2019 and the recent pilot transfer formula represent initial steps toward formalizing fiscal transfers.
4. **German fiscal federalism** is characterized by a robust equalization system and constitutional protection of local government rights.
5. **Ethiopia's block grant system** is designed to compensate for regional disparities but is often a source of political contention.
6. **Kenya's devolution model** has significantly empowered counties through a constitutionally mandated equitable share and independent oversight institutions.
7. **Nigeria's constitutional revenue-sharing system** is detailed and formulaic; however, local governments have historically struggled with fiscal autonomy.

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