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# **SOMALILAND CUSTOMS REVENUES AND STATE-BUILDING: THE IMPACT OF LOCAL GOVERNMENTS' REVENUE COLLECTION AND SHARING**

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## EXECUTIVE SUMMARY

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- Debate about local government revenue collection and sharing has persisted since the 1990s, and intensified in the last couple of years. On 27 June 2022, members of the Somaliland house of representatives submitted a motion to amend the Regions and Districts Self-management Law, No. 23/2019 law. The amendments aim to correct inequalities in revenue sharing. Other MPs and sections of society are against the motion.
- While the debate about revenue sharing, notably of local government revenue, has broader implications for national cohesion, state-building and state-society relations, there is little documentation and understanding of this debate. The overall objective of this study was to deepen the understanding of the Somaliland local government customs revenues, notably the controversial 12.5% and 10%, by documenting and analysing the different rationales behind and politics surrounding it. By doing so, the study will contribute to an informed debate on revenue sharing.
- At the policy and practical levels, there is a misunderstanding between the local and central governments on the local government supplementary budget/ *Kabka Dawladaha hoose* (KDH) , also known as the 12.5%. Moreover, the policy rationale and objective behind the municipality tax (10%) are not transparent and are not aligned with current Somaliland ambitions, including the government's presence in the Eastern regions.
- The debate about the KDH and the municipality tax has become more political and divisive and requires more informed and open discussion than rushed parliamentary majority approvals.
- Considering that Somaliland hugely relies on trade taxes, continuous dependence on revenues from circulating imported goods may prolong and intensify the current contestations and controversies surrounding the trade circulation and customs revenue.
- Some debate whether existing custom points are organic, based on a geographic endowment, or man-made, influenced by political decisions. However, the real debate should be on why some areas of some economic activity (mid-sized cities across the country) are not generating or receiving as much revenue as they think they should. It is also important to note that even if customs are organic, decisions such as where to tax, what to tax, who should tax and how tax revenue is allocated are political.

## 1. BACKGROUND

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The Somaliland territories have historically been characterised by long-distance import-export trade (Pankhurst, 1965). Behind this has been the control of key seaports such as Zeila, Berbera, Heis, Meit and Bulhar along the Red Sea and the Gulf of Aden which served the Somaliland hinterlands and landlocked territories such as Ethiopia. This import-export trade took place along historic trade corridors such as the Zeila-Harar corridor (Pankhurst, 1965; Musa et al., 2021). Since the colonial period, revenues from the import-export trade remained the main source of revenue for governments, capturing revenues in the ports, markets and customs (Pankhurst, 1965; Raballand & Knebelmann, 2021; Musa et al., 2021). Moreover, government policies shaped the significance of some trade corridors over others. For example, the opening of the Ethio-Djibouti Railway in 1917 changed the significance of the Zeila corridor. This infrastructure drew trade away from nearby Zeila port under the British to Djibouti under the French, while the establishment of a British military garrison in Aden across the Red Sea in Yemen at the beginning of the second quarter of the twentieth century cemented Berbera's significance (Dua, 2013; Musa, 2020).

After 1991, the volume of import trade through Berbera port and the main corridor connecting Berbera to the west and east directions increased. At the same time, cross-border trade between Ethiopia and Somaliland at the Togwajale border resumed and intensified. The increase in import trade has enabled the government of Somaliland to generate custom tariffs and tax revenue that was used to finance state-building from 1993 (Balthasar, 2013; Phillips, 2020). During this period, local authorities were formed in cities and districts along the trade hubs and corridors. Since revenue collection and allocation is the centre of the contemporary state-building literature, in Somaliland, at central and local levels, 'the process of interactions between 'state' and 'the economy' has become increasingly relevant and complex' (Tobias & Finn, p.8, forthcoming).

The discussion on "who pays taxes, how they are collected, and how the governments use the revenues" are important factors that shape state-society relations (Moore et al., 2018). This is evidenced by the persisting debate about customs revenue collection and distribution in Somaliland which has intensified recently and mainly focused on the tax revenue the

central government collects and disburses to the local governments, i.e., the 12.5% (Kabka Dawladaha Hoose/local governments budget supplements) and 10% (municipality tax). In contexts like Somaliland, the debate about the collection and disbursement of domestic revenues is more pertinent due to the absence or limited external funding sources.

Discussing how ‘Somaliland’s foundational state-building [after 1990] based on circulation ‘ of commodities and shifting customs regimes and strategies to capture revenues from cross-border, import, export and transit goods, Finn Stepputat and Tobias Hagmann coined the concept of ‘politics of circulation,’ i.e., the politics surrounding the everyday economy of goods on the corridors and economic hubs (Stepputat & Hagmann, 2019). According to them, “the shifting flow of goods can underpin, change, or undermine political orders and therefore change relations between competing political elites” (Hagmann & Stepputat, p. 10, forthcoming). The debate about revenue sharing has persisted since the late 1990s, and intensified since the last 2021 elections. On 27 June 2022, members of the Somaliland house of representatives submitted a motion to make amendments to Law No. 23/2019 law that repealed Law No.12/2000. They argue that inequalities from customs revenues the central government collects for the local governments should be corrected. However, other MPs and sections of the society are against the motion to make amendments to Law No. 23. Strong state-society relations underpin ‘durable’ and ‘positive peace’ as the citizens see the state as acting in the collective interest (DFID, 2010). The discussion about local government revenue sharing has broader implications for national cohesion and equitable revenue redistribution.

It is against this backdrop of public contestation over commodity circulation (flows of commodities) and customs regimes (custom points, revenue collection and allocation) and the absence of well-documented references that we undertook this exploratory study to have a better understanding of local government tariffs and the politics surrounding this issue. By 2035, it is expected that Berbera will facilitate [75%](#) of Somaliland’s trade. Considering that Somaliland hugely relies on trade taxes, continuous capture of revenues from circulating imported goods may prolong and intensify the current contestations and controversies surrounding the trade circulation and customs revenue. Therefore, the overall objective of this study was to deepen the understanding of the Somaliland local government customs revenues, notably the controversial 12.5% and 10%, by documenting and analysing the

different rationales behind and politics surrounding these revenues. By doing so, the study will contribute to an informed debate on revenue sharing. The specific objectives included:

- To document the logic (organic or man-made) behind Somaliland's custom points and revenues.
- To analyse the references/rationale (economic, political, historical) behind the debates for and against the current customs regimes and revenue sharing arrangements.
- To highlight shortcomings in the local governments' revenue sharing
- To suggest policy options to inform policy debates on local government revenues sharing

To answer these objectives, APD researchers conducted ten days of fieldwork in Hargeisa, Gabiley, Zeila, Berbera and Burao in May 2022. These areas were selected because the debate on the local government revenues, especially the 12.5% and 10%, centres around these cities. Berbera, Gabiley, Hargeisa and Zeila districts host the main Berbera, Kalabyadh, Hargeisa and Lawyado customs, respectively. These areas have been the centre of the local government customs revenues debate since the 1990s. In Burao local authorities have argued against local government customs revenue sharing, which they believe has been designed to benefit specific districts over others. In order to bring out the voices of the research participants, the analysis will stay closer to the views expressed by the research participants.

The study notably focuses on customs revenue that the central government collects and disburses to the local governments, i.e., the 12.5% and 10%, known as local governments' budget supplements and municipality tax, respectively, due to the controversies surrounding these revenues. The report is arranged in three main sections: (1) the context and rationale of the unified local government tariffs in late 1990 and early 2000; (2) the influence of state-building logic on Somaliland custom regimes and (3) the effects of local government tariffs on state-society relations. The last section is further arranged into four sub-sections (1) the debates over local municipality customs revenue, including whether customs points are organic or man-made (2) arguments for entry versus destination point taxation (3) ambiguities in sharing local governments revenues and (4) accountability in the local government customs revenue.

## 2. LOCAL GOVERNMENT TARIFFS: CONTEXT AND RATIONALE

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Customs revenue has been central to state-formation in Somaliland since the early 1990s. The contestation of who should control key revenue infrastructures such as ports, airports, and main customs points had implicitly or explicitly contributed to the 1992 and 1994 civil wars (Balthasar, 2013; Tahir, 2021). According to Phillips, in 1992, a violent power struggle ensued over control of public infrastructure and revenue at Berbera port and in 1994, in a reflection of the Berbera conflict in 1992, another local clan began agitating for control of Hargeisa airport and the revenue that passed through it, causing the 1994 conflict that had spread to Burao and continued until 1996 (Phillips, 2020, xv-xiv).

Commenting on how tax collection has been an integral component of state building in Somaliland, a senior local municipality official in Berbera interviewed for this study recounted, *“when Egal was establishing the state, he was successful in the disarmament, demobilisation and reintegration of clan militias that controlled different revenue sources...for this to happen Law No.12/2000 of Local Government Unified Tariffs was passed by the parliament. This law mandated the central government to collect 12.5% taxes for all local municipalities and 10% tax for cities that hosted the custom points.”*<sup>1</sup> According to Balthasar, it was easy for President Egal’s administration to levy customs duties because Berbera and Kalabaydh, the two most profitable sources of revenue, were largely under the control of militias who supported Egal due to clan affiliation (2013). Therefore, “Egal put particular emphasis on removing the roadblocks between Kalabaydh, Hargeysa and Berbera, the country’s main economic corridor” (Balthasar, 2013, 224) and started to tax commodities along this route which he controlled.

The contestation over custom points and revenues started with the post-1991 state formation. From the start, Somaliland's customs regimes were marked by ambiguities on who should collect customs revenues and where they should be collected. In the absence of established laws and regulations, such as a constitution, multiple local authorities and militias competed with the central government for the collection of customs and tax revenues on

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<sup>1</sup> Senior local government official, Berbera, 22 Maya 2022



commodities at the customs and ‘control’ points located at the entry points (Musa et al., 2021). In early 2000, two important laws were established: the constitution and the Local Government Unified Tariffs law (*xeerka tacriifada midaysan*), also known as Law No.12/2000. Before this law, local governments had tax collection desks at the checkpoints and custom points. After the formulation of this law, the central government took the mandate to collect two customs revenues, municipality tax (10%) and local government supplementary budget (the 12% or *Kabka Dawladaha hoose/KDH*), for the local authorities. It is unclear why the central government gave itself the mandate to collect customs revenues for the local governments when the latter could still have tax collection desks in the customs as was the case before 1991. However, some plausible explanations suggested by those interviewed were that by then there were no elected local governments and the government wanted to have leverage over the appointed local authorities. The first post-1991 local council elections were held only in December 2002. It may also have been because there are logical economies of scale and scope for the central government to administer some types of revenue.

### 3. THE INFLUENCE OF STATE-BUILDING ON SOMALILAND CUSTOMS REGIMES

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A customs regime is understood as a set of operations and practices that specify how customs duties/taxes are collected, how much duties/taxes are levied on imported and exported commodities, and where are these commodities in circulation are taxed. As mentioned, the state-building logic greatly influenced the current customs regimes in Somaliland. Explaining this, a key informant in Berbera recounted, *“the government of President Egal designed that imported and exported commodities were taxed at Berbera and Kalabaydh customs points. These were two customs the government fully controlled and the revenues from these two custom points were important for Egal’s government”*.<sup>2</sup> Balthasar argues that the Egal administration was able to secure Berbera, Gabiley and Berbera corridor because they were largely under the control of militias from his clan who supported him (2013). Tax collection was effectively carried out in these areas that came under Egal’s administration (Bryden & Farah, 1995). The collection of customs taxes, including the local government tariffs i.e., local

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<sup>2</sup> Key informant, Berbera, 22 May 2022

governments' budget supplements (12.5%) and municipality tax (10%), was, in part, built on the same logic of capturing revenues in customs where Egal's administration had full control.

The rationale for the central government collecting revenues for the local authorities was also, in part, tied to state-building logic. To control revenue collection, the central government *"abolished the numerous controls [checkpoints] and custom points along the trade corridor. The government also wanted to capture revenues at custom points where it had full control"*.<sup>3</sup> There were numerous 'controls' and customs points along the main trade corridor that levied different tariffs on moving commodities and the local authorities had desks in these controls and customs points where their officials levied tariffs alongside the central government. Therefore, with the formulation of Law No.12/2000, the central government not only unified local government tariffs but also authorized itself for the collection of all customs duties including local government tariffs and effectively captured revenues where it held most control. A pertinent question is why the clans operating the historic checkpoints agreed to cede responsibility of revenue collection to the Egal administration. One explanation is that the Egal administration monopolised violence at a time when different actors challenged state authority; the administration then provided protection, including safer, more predictable, and monopolistic economic activities, to the business communities who operated along this corridor. Egal monopolised violence and in exchange the businessmen from the areas that ceded revenue collection to Egal monopolised and created long term market control in the trade between Berbera, Hargeisa, Ethiopia and Djibouti (Bradbury, 2008; Renders & Terlinden, 2010).

Article 14 (XIV) of Law No.12/2000 is on custom duties of the imported commodities (*cashuurta badeecadaha debedda*) and stipulated that the Ministry of Finance Development (MoFD) collects customs revenues on behalf of cities containing custom points and provides 10% of these revenues to the local governments of these cities. The law also stipulated that, the MoF collects 12.5% of customs revenues (*Kabka dolwada hoose/local government budget supplement*) on behalf of local governments, including those hosting customs points.<sup>4</sup> The

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<sup>3</sup>Former local councillor, Berbera, 22 May 2022

<sup>4</sup> It is also important to note that the 10% and 12.5% were based on imported commodities not exported commodities such as livestock.

original districts that were mentioned by the law to benefit from the 12.5% were Hargeisa (51.26%), Burao (21.39%), Gabiley (9.87%), Borama (9.86%), Sheikh (3.75%), Zeila (2.18%), and Baki (1.69%). This shows that only seven districts, including those that already received revenues from the 10%, exclusively benefited from the 10% and 12.5%. The laws also stipulated that the 10% and 12.5% were based on general custom duties. However, a later presidential decree clarified that the 10% and 12.5% were based on specific heads instead of the general custom revenue.<sup>5</sup> In any case, this indicates ambiguities in the distribution of the 12.5% revenues.

The findings show interwoven rationales behind the Somaliland customs regimes established in the 1990s. While the main rationale was state-building, political and economic rationales were not absent from establishing the customs regimes. In the state-building process, the motive of the national leaders was that the government should monopolise the customs regimes by levying of tariffs and duties on imported and exported commodities in cities and trade corridors where it had full control;

*The government was not strong, and it could not protect or had full control of all cities and areas. Therefore, the government decided to levy tariffs and duties on imported and exported commodities in the cities where it had full control. For example, the current Haleeya checkpoint was located at Da'ar Buduq but it was relocated in the late 1990s after Da'ar Buduq checkpoint came under attack by armed militias who looted the coffer.<sup>6</sup>*

The negotiations between the central and local governments over the local government tariffs and taxes started in the wake of the formulation of Law No.12/2000. The appointed Mayors vocally negotiated with President Egal and President Rayale administrations, “during the President Rayale era; different Mayors compiled a list of all the municipal taxes that the central government collected. We submitted the list to the Minister of Finance, who then

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<sup>5</sup> There are 13 subheadings that the Ministry of Finance taxes at customs. Three subheadings (harbour tax, sales tax, value tax) are charged 10% of local municipality tax and two subheadings (sales and value tax) are charged the 12.5% of budget supplement’ (Kabka Dawladaha hoose). The 2% of Eastern Regions development tax is charged value unit of imported commodities.

<sup>6</sup> Key informant, Berbera, 22 May 2022

*informed the Minister of Defence who said if the local municipalities collect all these taxes how shall we pay the salary of the army?”<sup>7</sup> This indicates that the revenue collection was closely tied to national security. However, the elected mayors are less vocal in negotiating with the central government over local government tariffs and taxes. One plausible explanation for this is that “the appointed Mayors had equal access to President as those of the Ministries since they were both appointed by the President. However, the elected Mayors do not have access to the President; instead, the Ministry of Interior has oversight and administrative roles which they cannot bypass.”<sup>8</sup> This could explain why the debate about the local government tariffs and taxes has become public since the elected local government officials communicate through the media due to the communication barriers, “we cannot even access the Ministers, let alone the President, we do not know whom to talk to about our complaints on revenues.”<sup>9</sup>*

A long-term serving local government official in Gabiley said, “when Law No.12/2000 was new, we complained. We especially complained about the 12.5% which we did not want to be called *Kabka Dawladaha hoose* because it is revenue that the central government collects for us, not a supplement we receive from the national government revenue. We also wanted its period of disbursement to be reduced to 10 days. In fact, during this time, the central government released the revenues every month, but now it releases quarterly. Appointed Mayors led the districts, but they were more experienced than the current elected Mayors who cannot overstep Ministry of Interior”.<sup>10</sup> This indicates the policy and practical misunderstanding between the local and central government on what the 12.5% tax is and what it is for or how it works.

Since mid-2000, the state-building has become increasingly strong and the government controls reached most Somaliland territories. However, the customs regimes that were influenced by temporary and contextual realities in the 1990s have remained permanent. Commenting on this, one interviewed key informant said, “the current taxation regime is

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<sup>7</sup> Former Mayor, Burao, 24 May 2022

<sup>8</sup> Informal interviews, intellectual, Hargeisa, 27 May 2022

<sup>9</sup> Senior local government official, Burao, 26 May 2022

<sup>10</sup> Former local government official, Gabiley, 21 May 2022

*based on collecting revenues where the state has a full control since it was formulated at a time when state building was in early stage and the security was weak”.*<sup>11</sup> Similarly, a former Mayor said, *“It is not 1990 when militias controlled checkpoints and customs. Today, checkpoints and customs are under the jurisdiction of districts led by elected local councillors that are responsible and willing to assist the central government in raising revenues”.*<sup>12</sup> Similarly, a senior local government official in Burao stated, *“the collection and allocation of the 12.5% and 10% customs duties were not designed to be a temporary solution that lived for 22 years but to find a temporary solution for an administrative challenge at the time when these taxes [were] designed”.*<sup>13</sup> These voices indicate the contextual and temporary nature of the current customs regimes and the need for a discussion on customs reforms that reflect the post-2000 realities and priorities in Somaliland.

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#### 4. THE EFFECTS OF LOCAL GOVERNMENT CUSTOMS REVENUE ON STATE-SOCIETY RELATIONS

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State-society relations have been defined as ‘interactions between state institutions and societal groups to negotiate how public authority is exercised and how it can be influenced by people. State-society relations can be peaceful or contested (and at times, violent). They are focused on issues such as defining the mutual rights and obligations of state and society, negotiating on how public resources should be allocated and establishing different modes of representation and accountability’ (DFID, 2010, p. 15). In Somaliland, the discussion on revenue collection and allocation has lingered since the 1990s but has taken centre stage in the last decade. On 27 June 2022, members of the Somaliland house of representatives submitted a motion to make amendments to Law No. 23/2019 that repealed Law No.12/2000. Their argument is to correct inequalities from customs revenues that the central government collects on behalf of the local governments. However, other MPs and sections of the society are against the motion to make amendments to Law No. 23. Strong state society relations underpin ‘durable’ and ‘positive peace’ as the citizens see the state as acting in the collective interest (DFID, 2010). As the *“discussion about the 12.5% and 10% has broader implications for the national cohesion and equitable revenue distribution”*,<sup>14</sup> this section takes stock of the debates and views on the local government’s customs revenues.

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<sup>11</sup> Key informant, Berbera, 22 May 2022

<sup>12</sup> Former Mayor, Burao, 24 May 2022

<sup>13</sup> Senior local government official, Burao, 26 May 2022

<sup>14</sup> Member of parliament, Hargeisa, 14 May 2022

#### 4.1. Debates over local government customs revenue

Law No.12/2000 of Local Government Unified Tariffs Law was repealed by the Regions and Districts Self-management Law, No. 23/2019. However, the contested article on the 12.5% and 10% local government tariffs has not been amended. Policy and practical ambiguities relating to these laws stoke the debate on the local government customs revenues. The Ministry of Finance Development (MoFD) collects customs revenues for the local governments; however from the start of the enactment of the Local Government Unified Tariffs law, the local authorities were displeased with the MoF collecting what they believed to be municipal tariffs that they should have collected and naming the 12.5% as Kabka dolwada hoose/local government budget supplement. In addition, when this law was enacted, most districts were not consulted as the state was not present in parts of the country, while key districts such as Hargeisa and Burao were against the Unified Tariffs law from the very start. They believed that the 10% disfavoured them (see figure 1). The current debate on local government customs revenues has different layers. These debates can be categorised into general debates about the customs regimes and more specific debates about the local government revenues, i.e., the 12.5% and 10%.

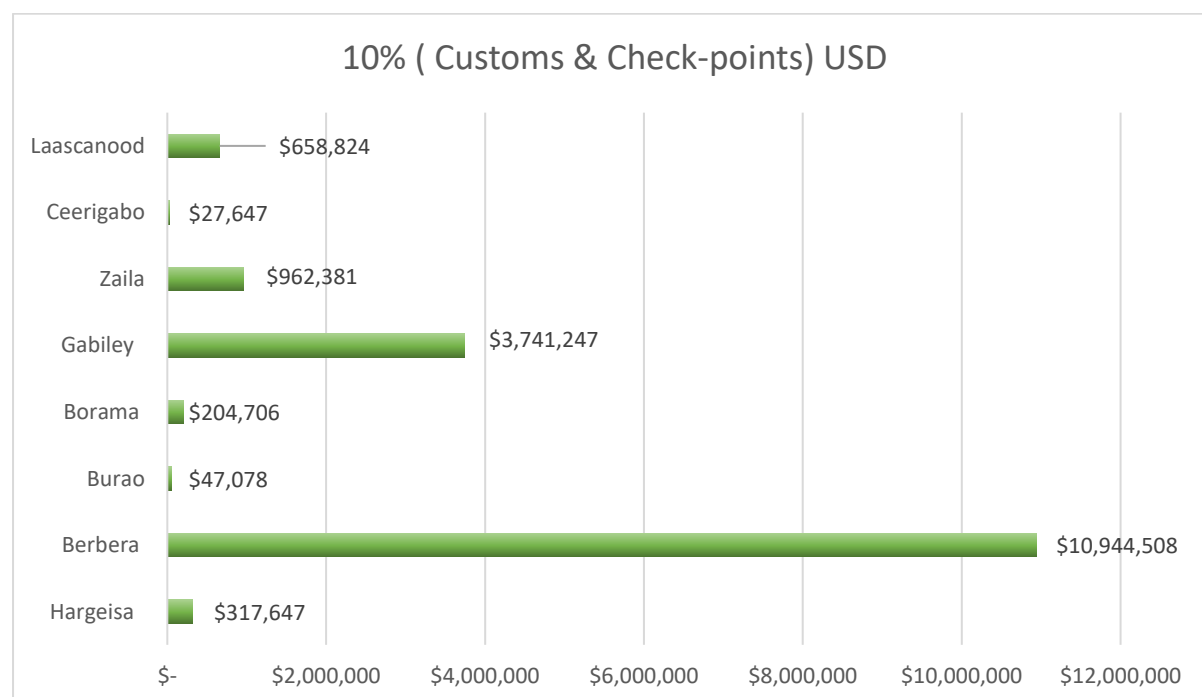


Figure 1: the annual revenues that selected districts generated from the 10%

Source: an analysis based on MoF 2022 budget

#### 4.1.1. Arguments for Entry versus Destination point taxation

Some debate whether existing custom points are organic, based on a geographic endowment, or man-made, influenced by political decisions. However, the real debate should be on why some areas of some economic activity (mid-sized cities across the country) are not generating or receiving as much revenue as they think they should. It is also important to note that even if customs are organic, decisions such as where to tax, what to tax, who should tax and how tax revenue is allocated are political.

One general debate centres around whether the MoF should tax commodities at the entry points or at the destination, i.e., the customs of cities where commodities are destined. The proponents of the view that import commodities should be taxed at the entry point, including interviewed customs officials and Gabiley and Berbera local government officials, gave operational and legal explanations.

Operationally, collecting revenue at the entry points is cost-effective and makes revenue collection easier. Commenting on this, a former Berbera local councillor argued, *“the reason why commodities are taxed at the entry point is not to lose revenues and to control tax evasion”*.<sup>15</sup> A senior customs official in Berbera also stated, *“taxing at the destination customs is technically difficult because our traders do not like tax; they are forced to pay. For example, we stopped to collect 0.5% profit tax at the point of entry and decided that it is collected at the destination, but this revenue has substantially reduced”*.<sup>16</sup> He added, *“Somaliland customs taxation is a triangle: traders are the taxpayers, the government is the tax collector and the traders transfer the tax to the consumers, but if the traders do not pay tax at the point of entry it will be difficult to collect at the destination”*.<sup>17</sup> This debate reflects that taxpayers play games with the taxing authorities including ‘tax negotiations, bargaining, avoidance, and other practices with different degrees of agency of the taxpayers’ (Musa et al., forthcoming 2022). These tax games are motivated when the taxpayers cannot see the link between tax and service delivery i.e., lack of or weak social contract. A senior local government official in

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<sup>15</sup> Former local councillor, Berbera, 22 May 2022

<sup>16</sup> Customs official, Berbera, 23 May 2022.

<sup>17</sup> Customs official, Berbera 23 May 2022.

Burao said, *“it is not true that Somalis inherently dislike tax; they only dislike it when they do not receive service delivery in return. The tax compliance has increased in areas of Burao where we constructed roads”*.<sup>18</sup>

Legally, any changes in terms of No. 23/2019 law, notably the revenue sharing percentages, should be done through a discussion in parliament with input from the government. Commenting on this, a local government official in Gabiley stated, *“the 10% and 12.5% are legal and has been approved by the parliament and it applies to all the existing 22 customs of which Berbera is one of them”*.<sup>19</sup> On 27 June 2022, members of the Somaliland house of representatives submitted a motion to make amendments on Law No. 23/2019; however, this debate has become a more political and divisive issue that might require discussion and consensus building than rushed parliamentary majority approvals.

Those suggesting that imported commodities should be taxed at the destination presented two related arguments. One, customs taxation should be decentralised. It is not the 1990s when the state was weak and did not fully control the whole country; today, the government fully controls all customs, and there are elected local councils. Therefore, it is (operationally) practical that MoF taxes customs at destination instead of at entry. A former Mayor said, *“what difference does it make for the Ministry of Finance to tax-exclusive customs when it could have taxed at different customs to distribute resource sharing”*.<sup>20</sup> The MoFD has started to gradually establish or operationalise new customs points including Baligubadle and in Guuxa but has not yet begun to decentralise the taxation of main imported commodities that contribute to the 10% which are still taxed at main entry points. Two, if the current revenue sharing percentages, i.e., the 10% and 12.5%, is retained, the revenue sharing formula must be revised. A senior local government official in Burao stated, *“if the current customs regimes remain intact, then 5% of the 10% revenue for the local governments that host main customs should be allocated for other districts or the 12.5% and 10% should be combined and distributed to all local government equitably”*.<sup>21</sup> The formula for revenue sharing is technical

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<sup>18</sup> Senior local government official, Burao, 26 May 2022.

<sup>19</sup> Local government official, Gabiley, 21 May 2022.

<sup>20</sup> Former Mayor, Burao, 24 May 2022

<sup>21</sup> Customs official, Berbera 23 May 2022.



and might require the establishment of an independent commission. For example, Kenya established the Commission on Revenue Allocation (CRA) after 2010 which is mandated to [‘make recommendations concerning the basis for equitable sharing of revenue raised by the national government; between the National and County Government; and among counties Governments’](#). The commission regularly reviews data on the population and marginalisation and submits recommendations to the Senate.

#### **4.1.2. The ambiguity in sharing local government revenues**

A more specific debate focuses on the the sharing of the revenues among the local governments, notably, the 12.5% and 10%. Regarding this, there are several issues. One, the administrative criteria are not clear; the central government disburses the revenues from the 12.5% on a quarterly basis with the approval of the Ministry of Interior (MoI) while the 10.5% is disbursed on a daily basis and is not approved by the MoI. Moreover, the 12.5% is fraught with ambiguities in its sharing; it is now shared by all districts instead of the original seven districts named in Article 14 (XIV) of Law No.12/2000, while the 10% is less ambiguous and limited to customs containing cities. These criteria of revenue sharing and disbursement affect the revenue in the local governments’ coffers which also affects local government planning and service delivery. Cities such as Gabiley and Berbera that host main custom points receive timely windfall revenues. Table 1 shows the total budget of selected districts and the percentage of the local government budget generated from the 10%, 12.5%, and inland revenues. It indicates that when central government customs revenues to the local governments, i.e., the 12.5% and 10%, are combined, Berbera and Gabiley receive the highest customs revenues, \$ 11,124,508 and \$ 4,070,659, respectively, compared to, for example, Hargeisa and Burao, the two largest and most populous districts that received \$ 3,141,176 and \$ 1,223,548, respectively.

**Table 1: Local Government Budget 2022 - selected Districts**

| Local government Budget 2022 - selected Districts |            |                                  |                                     |                                       |                           |                       |
|---|------------|----------------------------------|-------------------------------------|---------------------------------------|---------------------------|-----------------------|
| No  | Districts  | 10% (Customs & Check-points) USD | 12.5% - (Grants from CG capita) USD | Total Central Gov subsidy (10%+12.5%) | Other Inland revenue -USD | Tot - 2022 Budget USD |
| 1   | Hargeisa   | 317,647                          | 2,823,529                           | 3,141,176                             | 15,066,139                | 18,207,316            |
| 2   | Berbera    | 10,944,508                       | 180,000                             | 11,124,508                            | 2,661,280                 | 13,785,788            |
| 3   | Burao      | 47,078                           | 1,176,471                           | 1,223,548                             | 4,119,178                 | 5,342,727             |
| 4   | Borama     | 204,706                          | 663,529                             | 868,235                               | 3,573,059                 | 4,441,294             |
| 5   | Gabiley    | 3,741,247                        | 329,412                             | 4,070,659                             | 540,673                   | 4,611,332             |
| 6   | Zeila      | 962,381                          | 371,626                             | 1,334,007                             | 545,294                   | 1,879,301             |
| 7   | Ceerigabo  | 27,647                           | 529,412                             | 557,059                               | 857,059                   | 1,414,118             |
| 8   | Laascanood | 658,824                          | 470,670                             | 1,129,494                             | 1,098,929                 | 2,228,423             |
|   |            | 16,904,037                       | 6,544,649                           | 23,448,686                            | 28,461,612                | 51,910,299            |

Source: analysis based on the MoF 2022 budget.

The reported ambiguities in the practice of revenue sharing and disbursement is, in part, influenced by ambiguities in the policies. As stressed by the research participants, the central government understands the 12.5% (*Kabka Dawladaha hoose*, i.e., a budget supplement) as a revenue that the central government donates to the local governments, while the local governments see it as its revenues that the central government collected on their behalf. This, however, has administrative implications including that sometimes the central government allocates the revenues from the 12.5% for national projects. Commenting on this, a local government and public revenue expert said, “sometimes, the central government allocates revenue from the 12.5% for national institutions. For example, in 2013, 50% of the 12.5% revenue was used to construct the presidential palace road and in 2018, the office of the auditor general requested that 5% of the 12.5% revenue be allocated to them, the president approved for them but later, the Ministry of Finance revised this decision”.<sup>22</sup>

The distribution of revenues from the 12.5% tariffs between districts is clearly stipulated in the Regions and Districts Self-management Law, No. 23/2019 law and the central

<sup>22</sup> Local governments and public revenue expert, Hargeisa, 9 May 2022

government has no powers to decide how to distribute the 12.5% revenues as article 89 details the allocation of the revenues from 12.5% which is based on the size of the population of the districts (Table 2). Table 1 shows that Hargeisa and Burao receive the highest revenues from the 12.5%, \$ 2,823,529 and \$ 1,176,471, respectively.

**Table 2: 12.5% Distribution**

| 12.5% Distribution ( Article 89(2)) |       |                     |
|-------------------------------------|-------|---------------------|
| District grade                      | Share | Number of districts |
| A                                   | 6%    | 7                   |
| B                                   | 2%    | 5                   |
| C                                   | 3%    | 11                  |
| D                                   | 1.5%  | 78                  |
|                                     | 12.5% | 101                 |

Source: No. 23/2019

Article 14 (XIV) of Law No.12/2000 mentioned only seven districts to benefit from the 12.5%. These were Hargeisa (51.26%), Burao (21.39%), Gabiley (9.87%), Borama (9.86%), Sheikh (3.75%), Zeila (2.18%), Baki (1.69%). However *“since then all grade A districts were included, then from 2007 all grade B districts and then all grade C districts and now even grade D districts, the number has increased to over 100 districts”*.<sup>23</sup> The inclusion of new districts to benefit from the 12.5% revenues took place when the 12.5% revenue was not increased to accommodate the new districts while numerous new districts were created by the Ministry of Interior. This has reduced the share that A-grade districts receive from the 12.5%. For example, the annual revenue from the 12.5% is \$6,544,649. Considering the original Article 14 (XIV) of Law No.12/2000, Hargeisa should have received \$3,272,324 but instead has received \$ 2,823,529.

According to article 7 and 11 of Law no 23, the Mol was supposed to assess grade D districts within 2 years, but no such assessment was carried out and the boundaries between grade A and D districts remain not demarcated, creating administrative and revenue collection challenges for the local governments.

<sup>23</sup> Former Mayor, Burao, 24 May 2022

With the creation of many districts, mostly Grade-D, Somaliland now has 101 districts of which over 70 are grade D districts. This has compounded the revenue disparity in at least three ways; first the new districts share the 12.5% with the existing districts which affects the share of the districts from this revenue. Second, since the Ministry of Interior has the decision to approve the allocation of the 12.5% to different districts, the creation of new districts has contributed to the ambiguities in the way this revenue is allocated. Third, the new districts compete with the A-grade districts for revenue collection, *“D districts have started to tax livestock; they tax 2000 shillings per head of small ruminant instead of the 3000 we tax in Burao”*.<sup>24</sup> These administrative challenges, however, do not affect the 10% which is limited to only the cities that host customs. Moreover, while there are 23 customs in Somaliland, four customs monopolise custom duties of imported commodities, making customs hosting cities receive relatively large revenues which they do not share with other districts in Grade B, C and D in the same region. Commenting on this a research participant in Berbera noted, *“the 10% is limited to Berbera city, Grade C and D districts in Sahil region do not benefit from this revenue. These districts remain underfunded. For example, Sheikh district does not benefit from the 10% and it complains about the allocation of the 10%”*.<sup>25</sup>

#### **4.1.3. Accountability in the local government customs revenue**

The discussion of accountability emerged as an important topic during the data collection. Taxation is the core of how governments and their citizens relate as low accountability reinforces low trust between the government and its citizens (Tellander & Hassan, 2016). Lack of transparency, proper feedback, public dialogue, and enforcement mechanisms are challenges to accountability within the taxation system in Somaliland (ibid). The research participants stressed lack of transparency between the central government and local governments in the collection and allocation of the local government budget supplement (the 12.5%) and municipality tax (the 10%). One interviewed senior local municipalities official said, *“we do not know the actual revenue from the 10%, we only receive what the Ministry of Finance provides since it is the we do not see the documentations such as receipts that have*

<sup>24</sup> Interview, Senior local government official in Burao, 24 May 2022

<sup>25</sup> Interview, key informant, Berbera, 22 May 2022

*been used to collect the taxes.”.*<sup>26</sup> Similarly, long-term serving local councillor said, *“we have been complaining about Kalabaydh customs, we asked them to show us the revenues from the 10% and 12.5% but they did not. We then placed local government officials at the customs to document Khat trucks, they complained to the Ministry of Finance, and we were told to back off”.*<sup>27</sup> While the customs and the Ministry of Finance Development (MoFD) might have their internal control systems and it might not be practical for the local governments to have direct insights into daily or monthly revenues collected by the Ministry, the production of audited revenue reports by the Ministry and Accountant General offices could improve the transparency of the local government customs revenues.

There has also been a strong perception of a lack of transparency on the local government budget utilisation, notably the municipality tax (the 10%) which generates relatively significant revenue for some cities. An interviewed customs official said, *“ Berbera receives over a million monthly revenue from the 10%; this money would have transformed Berbera but such transformation is not happening so there must be something wrong”.*<sup>28</sup> The perception among some research participants has been that a substantial chunk of the revenue from the 10% is used for political reasons including lobbying against parliamentary reviews of this law, buying political loyalty and sponsoring campaigns during elections.

It is also important to note that domestic revenue collections are relatively less important to the local government budgets of cities that receive substantial revenue from the municipality tax, i.e., 10% (figure 2). A fairer redistribution of the local government customs revenue would likely incentivise cities such as Berbera, Gabiley and Zeila to collect more inland taxes. A senior Zeila local government official said, *“ 80% of Zeila revenue is from the customs and 20% from inland revenue collections and the 12.5% [KDH]. We are very dependent on customs revenue”.*<sup>29</sup>

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<sup>26</sup> Senior local government official, Berbera, 22 May 2022

<sup>27</sup> Long-term serving councillor and local government official, Gabiley, 21 May 2022.

<sup>28</sup> Customs official, 23 May 2022

<sup>29</sup> Senior Zeila local government official, Hargeisa 29 May 2022

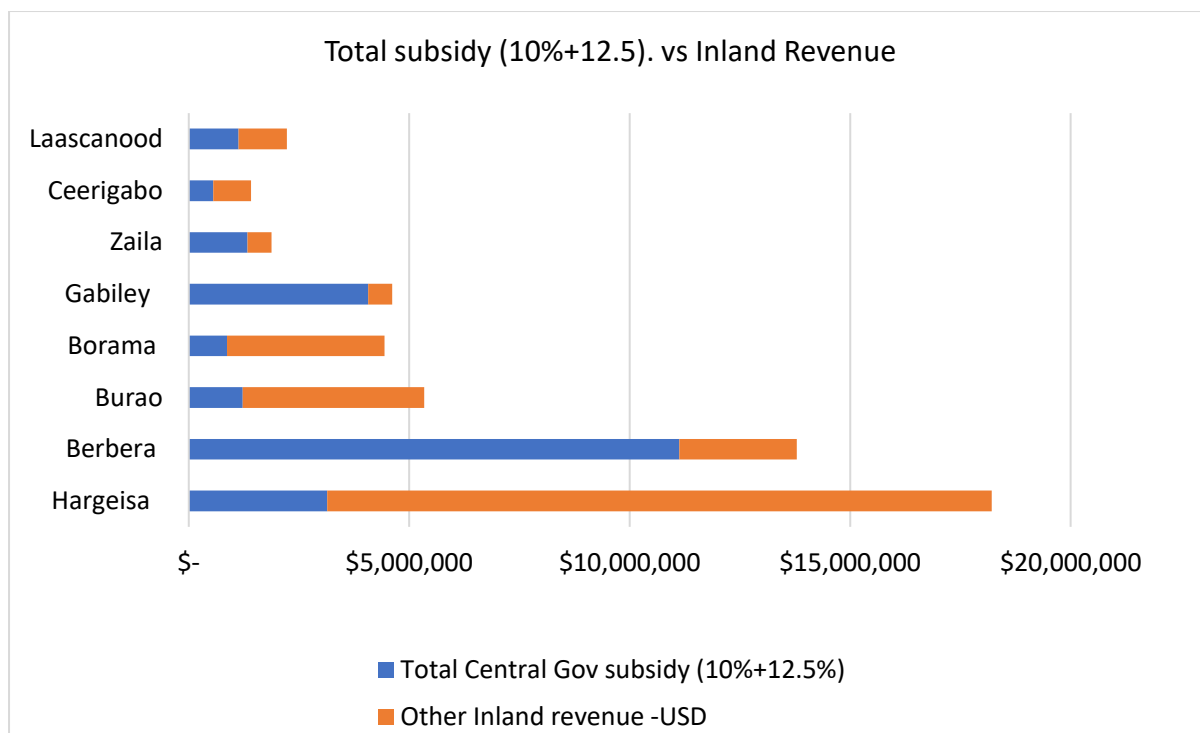


Figure 2: *Total subsidy (10%+12.5). vs Inland Revenue*

Source: *an analysis based on MoF 2022 budget*

The fact that some local governments have to collect more inland revenues and the amount of effort and cost this requires while other local governments receive revenues with less effort and cost also ignites the perception on inequality in revenue sharing. A senior local government official in Burao stated, *“every day, we fuel our cars and send off different teams to collect revenues while other local governments receive a windfall of revenue without effort, there is inequality. We are not saying that Gabiley and Berbera local governments should not receive revenues we are saying we also need revenues to serve the 800,000 population in Burao and the many villages and communities that fall under its jurisdiction.”*<sup>30</sup>

Last year Burao local government budgeted 45 billion shillings (around US \$ 5 million) after increasing inland revenues by 30% but raised 27 billion (US \$ 3 million). Drought and livestock export ban due to Covid-19 have affected the local government’s revenue collection. Interviewed local government officials stressed that while they are not envious of other districts’ revenues, they demand fair distribution of revenue and resources, *“the reality is that*

<sup>30</sup> Senior local government official, Burao, 24 May 2022

*Burao is not env[ious] of other districts, but Burao does not have revenue and it needs fair distribution of resources”.*<sup>31</sup> The central government recognised the revenue disparity in the country in 2007 when the president issued a decree to collect 2% of customs revenue for the ‘development’ of the eastern regions. But this revenue is not well managed, and it has problems similar to the local government budget supplement (the 12.5%) and municipality tax (the 10%) as argued by one informant.

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## 5. CONCLUSION

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Revenues from trade taxation, notably duties on imported commodities, have become central to Somaliland's revenue collection since the 1990s. However, this has not been free from the ‘politics of circulation,’ as the debate on where to levy tariffs, who should levy tariffs, and how the revenue from customs tariffs is allocated has lingered and intensified in recent years. This debate has implications for state-society relations. There are political, economic, and administrative grievances regarding the collection and sharing of local government customs revenues.

A combination of economic and political factors have contributed to the intensified debate about local government customs revenues. These include the exclusiveness of local government customs revenue, the so-called municipality tax or the 10%, to customs containing cities, the ambiguous allocation of the revenues from the local government budget supplement (the 12.5%), the monopoly of a few custom points to levy duties on imported commodities, the increased volume of trade and custom revenues that increase revenues for the ‘monopolistic’ customs, and the citizen’s increased expectation from local governments to deliver services. The monopoly, whether organic or man-made, of a few customs points over the collection of import duties and the disparity in the sharing of customs duties primarily ignite and sustain the debate on the local government customs revenues.

For the interest of improved social cohesion and state-society relations which are central to state-building, the issue of revenue collection and sharing between the central government and local governments, and among the local governments, can benefit from open discussion to refresh the policy rationale and objectives of the revenue sharing. This study informs this

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<sup>31</sup> Senior local government official, Burao, 24 May 2022

discussion as it takes stock of the political-economy factors and informed views on the local government revenues. Some debate whether existing custom points are organic, based on a geographic endowment, and therefore, custom containing cities should enjoy special rights; or man-made, influenced by political decisions, and therefore how customs revenues are shared should be debated. However, the real debate should be on why some areas of some economic activity (mid-sized cities across the country) are not generating or receiving as much revenue as they think they should. It is also important to note that even if customs are organic, decisions such as where to tax, what to tax, who should tax and how tax revenue are allocated are political.

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## 6. RECOMMENDATIONS

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1. The central government, parliament, and local governments should open a discussion on the local government customs revenues (the 12.5% and 10%). This is necessary to refresh the policy rationale and objective of these revenues and to support state building and security. Refreshing this policy will be in line with Somaliland's current priorities including the government's ambition to be more present in the Eastern regions.
2. The Regions and Districts Self-management Law, No. 23 should be revised so that it becomes sufficiently clear on how revenue collection responsibilities are divided between central and local governments. A comprehensive list of all municipal taxes should be generated, and the collection of these revenues should be fully decentralised to the local governments in line with Law No. 23.
3. The stakeholders should find a simple, transparent, agreed and evidence/formula-based mechanism for sharing (local and national) revenues. Revenue sharing should be administered by an independent commission.
4. There should be a legal framework to allow key agencies in national government (Ministry of Finance Development and Ministry of Interior) to work with local governments to decide and implement revenue sharing arrangements annually or bi-annually.
5. To improve the transparency of either the current or future arrangements, the Ministry of Finance Development and the Accountant General should produce more



regular audited reports for local governments to assure them of what is being transferred to them on what basis.

6. The creation of new districts and regions not ratified by parliament has brought administrative challenges in taxation, service delivery, and revenue sharing. The created but not ratified districts and regions should be assessed so that their existence becomes legal and approved by the parliament, and these administrative areas are considered in the revenue sharing.

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