Part IV: Post-Conflict Recovery and Policy Reforms

Intergovernmental Transfers: A tool for Conflict Resolution in Sudan

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Abstract

In an attempt to put an end to the conflicts that had prevailed in Sudan for a long time, three different peace agreements were signed between 2005 and 2007. The first was the comprehensive peace agreement (CPA), which ended the north-south armed conflict. The second was the Darfur peace agreement (DPA). It was meant to settle the conflict in Darfur region. The third was the East Sudan peace agreement (ESPA) aimed at resolving the conflict in the Eastern part of the country.

A major pillar of these agreements is the wealth sharing arrangements (WSAs), which provide a model for fair and equitable distribution of financial resources between the central government and the states (regions). The WSAs rely heavily on the principles of fiscal federalism.

The adopted system proved to be fairly effective in transferring substantial resources to the concerned states. Transfers accounted for about four percent of GDP on average during the 2005-2007 period. The system also marked a positive move in the intergovernmental fiscal relations. However, some obstacles confront the implementation of this system, and will most likely reduce its effectiveness in eradicating the symptoms of conflict. The system depends heavily on the flow of oil revenues, which are unpredictable. The weak institutional capacity at the state level adds to these challenges. There should be robust fiscal reforms, mainly in the area of expenditure control and cash management, for a sustainable transfer system to exist.

Keywords: Fiscal policy; Intergovernmental transfers, Revenue sharing, post-conflict.

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1. Background

The Republic of the Sudan is an independent, sovereign state governed through a federal system, in which power is effectively devolved. Responsibilities are distributed between the national and other levels of government according to the provisions of the constitution.

Sudan started to suffer internal conflict in the South soon after independence in the fifties. Conflict also erupted in other regions at latter periods, particularly in the Darfur area and in the Nuba mountains (Southern Kordofan).

A common factor in the eruption of these conflicts is the state of underdevelopment and discontentment among some of the rural communities in the affected regions. Lack of development and the poor provision of basic services were stated as some of the main causes of conflict. It therefore became clear to the government that any peace negotiations should address the question of marginalisation of some areas.

Allocating resources to finance development is a genuine demand from the side of the armed movements. This demand found support from a wide range of persons and institutions, who took part in the peace negotiations.

By combining both political federalism and fiscal federalism, Sudan started to put in place fiscal arrangements that were supposed to assist in ending these conflicts and to provide direct support to the peace-building process. These fiscal arrangements were centered around creating a system of intergovernmental financial transfers, whereby the national government would transfer financial resources to the sub-governments of the different states. The state governments would then take the responsibility of spending these resources to finance different activities, including the provision of basic services.

The objective of this paper is to picture intergovernmental transfers as a tool for containing armed conflict and as support to the peace-building process. The paper is organised as follows: Section two gives a conceptual framework of the intergovernmental fiscal transfers and the role these transfers can play in reducing conflicts. It discusses the methodology used and the sources of data and information. Section three reflects on the significance of fiscal decentralisation and intergovernmental transfers. The fiscal components of the wealth sharing agreements signed between the central government and the armed movements are highlighted in section four, while section five describes the nature of the current fiscal arrangements that were adopted by the government of Sudan to adhere to the various wealth-sharing agreements. The section also proposes a simple rules-based method of calculating these transfers. Section six highlights the challenges and the constraints to the system. Section seven suggests some policy changes necessary for reforming and improving the system. The conclusion is drawn in section eight.

This paper will be the first step in developing a framework that could be applied and used to design and evaluate the efficacy of wealth-sharing agreements.

2. Conceptual framework, methodology, and sources of data

Intergovernmental transfer system is the process of transferring funds from the central government to the sub-governments of the states or regions. The basic objective of this transfer is to close a fiscal gap at the state level. The rationale is to: a) Address vertical fiscal imbalance to assist state governments and empower them financially to pursue the provision of basic services in their respective regions; b) address horizontal fiscal imbalances by raising the capacity of local governments to raise own resources and consequently reduce horizontal inequality among regions; and c) ensure minimum level of services is provided, and that the services reach all the people in the regions at the same quality. It is important to note that intergovernmental transfer systems have redistribution implications, since they entail a flow of resources from the central government to the sub-governments.

For the above objectives to be achieved, it is crucial to consider the appropriate design of the mechanism through which the transfer funds should be channelled. Three different but related policy choices should be considered: i) How to determine the total amount of the resources to be shared among the regions; ii) how to allocate the resources pool across the eligible sub-governments; and iii) how to make these transfers conditional on the implementation of specific development programmes. These transfers can take different forms, but generally we can identify the following types:

a) Conditional transfers, which include transfers made for specific purpose. The recipient sub-government has no power to allocate them for different purposes.

b) Unconditional transfers, which include funds that were transferred to sub-governments. The latter is to decide on how these funds should be spent.

The concept of intergovernmental transfers could be used as a tool for the resolution of armed conflicts, given the fact that most of the conflicts in Sudan erupted as a result of underdevelopment and inadequacy of services provision, in addition to other political factors. The funds being transferred from the center to the sub-governments will be used mainly for the provision of basic services, such as education, health, and safe drinking water.

The methodology used in this paper is based on the analysis of secondary data. The main sources of the data and information are the Ministry of Finance and National Economy, and the Fiscal and Financial Allocation Monitoring commission. No econometric methods are used as a tool of analysis for the simple reason that the adoption of this intergovernmental transfers is very recent, and that the data available covers only three years, which is not enough to model the effectiveness of the transfer practice.

3. The significance of fiscal decentralisation and intergovernmental transfers

Promoting fiscal decentralisation will assist in achieving multiple objectives. Improving efficiency and better responsiveness to local conditions will contribute to improving the well-being of the rural communities (Tanzi 1996). Another objective is to highlight key policy options for addressing the fiscal and financing constraints affecting the service delivery by state governments.

It is of crucial importance that the national governments should fully define the institutional arrangements necessary to guarantee a reliable fiscal decentralisation and effective systems of revenue sharing between the central governments and state governments (Alhiraika 2007, Ehtisham 2004). It is hypothesised that while regional or local authorities always rely on transfers from the central government, their effectiveness in planning and service delivery depends crucially on the nature of the system of transfers and on their ability to mobilise own-revenue (including from tax), borrowing from domestic financial capital markets, and public-private sector partnership.

The transfer systems or the intergovernmental systems that exist between the central government and the state or regional governments in a post-conflict country play a crucial role in financing various activities at regional levels. These transfers can be used in financing various activities that can heal the wounds of conflict.

Intergovernmental transfers have a role in supporting regional stabilisation and equalisation, such that they correct for fiscal deficits at the regional governments, especially when regional expenditure levels are too high, relative to their levels of own resources and revenues. The transfers are also useful in reducing disparities among regions and may be used to insure against asymmetric shocks. They could also be used as a tool to provide for fiscal capacity equalisation, which involves transfers from regions with high per capita revenues and low per capita expenditure needs to those with low per capita revenues and high per capita expenditure needs. In such cases, these transfers will enable regional governments to provide comparable levels of own revenue collection.

Although there are considerable variations among countries in the importance of transfers, countries design them according to the objectives of their development strategies. Some countries adopt such transfer systems to redistribute income from rich to poor regions. Others apply transfer systems to provide insurance against asymmetric shocks, such as devastating floods, crop failure, or livestock market disruptions. In most cases, these transfers account for much of the local governments resources. Intergovernmental transfer systems include:

1. The sharing of tax revenues between the central government and sub-national governments;

2. Financial subsidies provided by the central government to sub-national governments;
3. The sharing of the oil revenues between the central government and the oil-producing areas.

Transfer systems suffer from different weaknesses that may lead them to be less effective. There are institutional deficiencies and technical deficiencies, which will impact the design and the operation of these systems. They are designed primarily to support operating expenses, and rarely to support acquisition of real assets. If these transfers are substantial, they impose disincentive hazards on the sub-governments and discourage the enhancement and mobilisation of local revenues. They provide unpredictable and uncertain flow of funds. Few of the transfer systems work to develop a market-based credit system.

There is a sizeable collection of literature on intergovernmental transfer systems in developing countries, but relatively little has been written on the subject as a tool for consolidating peace-building processes in conflict and post-conflict countries.

4. Wealth sharing agreements: Their fiscal components

The Government of Sudan started to negotiate with the various armed movements in the South in 1989, followed by negotiations with similar groups in the eastern part of the country, and in the west. The government was successful in reaching peace agreements with the Sudan People Liberation Movement (SPLM) in Nairobi, Kenya, in January 2005, and with the armed movements in Darfur in Abuja, Nigeria, in July 2005. In October 2006, the government also reached an agreement with the armed movements in the East of the country. The deal was arrived at in Asmara, Eritrea.

Although a comprehensive peace agreement has not been arrived at yet, since not all the armed movements signed the outlined peace deals, what has been achieved so far is a necessary step to mark the beginning of solid peace-building in the entire country.

An important complement to the signed three peace agreements is the wealth sharing agreements with their various fiscal and economic clauses. The different wealth sharing agreements converge on the understanding that the wealth of Sudan shall be looked at as a composure of natural and human resources, historical and cultural heritage, financial assets including credit and public borrowing, and donor assistance and grants. The understanding around wealth sharing also brings on board all the means, institutions, policies, and opportunities that contribute to the generation and distribution of wealth, which should be used to achieve economic development in Sudan. The aim is to eradicate poverty and achieve equitable distribution of wealth, while ensuring reasonable quality of life, dignity, and good living conditions for all the citizens.

The generation and distribution of wealth is critically affected by government policies, programmes and institutions. The definition of wealth therefore extends to the means, institutions, policies, and opportunities that affect its creation and distribution. It also includes the physical resources and government revenues. A key dimension of wealth is fair participation of the various stakeholders in the decision-making process, which affects its generation and the allocation of resources.

The authorities recognise that to get rid of the cumulative effects of underdevelopment compounded by the destructive effects of the conflict in Sudan, it is essential to establish an effective, transparent, and accountable system for the distribution of wealth. In this regard, effective and strong measures should be taken to remedy the situation through affirmative action in economic policy.

Negotiations on wealth sharing took considerable time and effort before conclusions on how to implement a fair and equitable intergovernmental transfer system. Each of the three agreements has a wealth sharing understanding and components. In brief, the fiscal components of each agreement are summarised below:

1. Naivasha wealth sharing agreement:

This agreement was signed in Naivasha, Kenya, on January 2005, between the Government of Sudan and SPLM. It is a major part of the comprehensive peace agreement (CPA). A complement to the wealth sharing agreement is the agreement on the implementation modalities of the framework. These two documents set out a comprehensive scheme for sharing common wealth, so as to enable each level of government to function and to ensure the quality of life, dignity, and living conditions of all citizens without discrimination. This wealth sharing arrangements functions on the following principles:

a) The wealth of the Sudan shall be shared equitably.
b) All parts of Sudan are entitled to development and wealth sharing.
c) Revenue sharing should show a commitment to the devolution of power and decentralisation of decision-making.
d) Development will be transparent and accountable.
e) Best-known practices for utilising natural resources will be followed.

A distinctive feature of wealth sharing under the CPA is the sharing of oil revenues. The CPA defines a national system for the management and sharing of the entire oil revenues in Sudan. A national petroleum commission was established to formulate and monitor public policies and to set guidelines for the oil industry, including developing strategies for the future development of the petroleum sector. The wealth sharing agreement developed a formula for sharing the oil resources as follows:

a) Two percent of oil revenue will go to the oil producing states in proportion to their output.
b) The remaining net revenue will be distributed as follows:
   i. 50 percent of the net oil revenue from the wells developed in the south of Sudan will go to the government of Southern Sudan.
   ii. 50 percent of the net oil revenue from oil wells developed in southern Sudan will go to the central government and the governments of the states in Northern Sudan.

The Government of National Unity (GNU), the Government of Southern Sudan (GOSS), and the governments of the other states, can develop and collect revenues from various sources including taxes, licenses, service charges, and loans. State governments and the Government of Southern Sudan should have exclusive control of income collected under their own taxation powers. Some institutional arrangements were created to support the allocations of these resources. They included:

a) The establishment of a national revenue fund (NRF). This fund should host all the collected national revenues and have an account in the Central Bank of Sudan (CBOS). It is administered by the Ministry of Finance and National Economy.
b) A special account in the Bank of Southern Sudan (BOSS) was opened to host all the revenues collected by the national government in the south of Sudan. 50 percent of these revenues should be transferred to GOSS and the rest be deposited in the (NRF).
c) A Fiscal and Financial Allocation and Monitoring Commission (FFAMC) was established by the government of national unity (GNU) and GOSS. The main function of FFAMC is to ensure fairness and transparency in the allocation of nationally collected funds to GOSS and to the governments of the states. The FFAMC is considered the most important institution for facilitating the implementation of the CPA clauses. This same institution is assigned the responsibility of monitoring the allocations mandated by the Darfur and the East peace agreements.
d) The Southern Sudan reconstruction and development fund: This fund receives resources from GOSS and other donors, and is used mainly for the reconstruction, resettlement, and re-integration and development in Southern Sudan.
e) The national reconstruction and development fund: This fund was established by the federal Ministry of Finance and National Economy and the joint national technical team (JNTT) for the purpose of assisting the war-affected areas. 75 percent of the resources of this fund will be used for the benefit of the war-affected areas in the Nuba Mountains (Southern Kordofan), and the Blue Nile states. The remaining 25 percent will be allocated to the other least developed states in order to reduce state or regional disparity.

2. Abuja Agreement:

The conflict in Darfur has been over natural resources, mainly water and pastures. Given the lack of readily exploited oil or mineral resources within Darfur region, the Darfur agreement calls for direct financial transfers from the GNU to the three states of Darfur. The major wealth sharing agreement provisions consist of the following:

a) The establishment of a Darfur Reconstruction and Development Fund (DRDF), whose responsibility is to solicit, raise, and collect funds from domestic and international donors and to disburse such funds for the resettlement, rehabilitation, and re-integration of the internally and externally displaced people. The agreement also requires the GNU to make regular contributions to the fund, which also aims to address the past development imbalances and provide adequate and sustainable development strategy for Darfur in an accountable way.

b) A joint assessment mission supported by multilateral organisations, similar to the one for Southern Sudan, should determine the development and reconstruction needs and should adjust the sums allocated to the DRDF.

c) The establishment of a fiscal and financial allocation monitoring commission, whose responsibility is to monitor and manage the financial transfers from the GNU to Darfur three states[2]. In the meantime, the wealth sharing agreement establishes a panel of experts to develop a formula for allocation of funds from national revenue account to Darfur.

d) The wealth sharing agreement of Darfur also provides for a compensation commission to develop and adopt mechanisms for reviewing and enforcing the commission's decisions. The GNU agreed to transfer US$30 million to cover these compensations. These compensations are mainly for the people who were affected by the conflict.

It is highly commendable that the Abuja Agreement stresses the importance of preserving the macroeconomic stability in the country. The agreement states that the national macroeconomic policy framework provides an important vehicle for combating poverty and eliminating the sense of marginalisation in Sudan during the post-conflict period.

That way, the agreement called for the formulation of the macroeconomic policies in such a way that it should ensure the quality of life, living conditions, and dignity of all the citizens in Sudan are promoted without discrimination on grounds of geographical location, race, ethnicity, religion, language, political affiliation, or gender. Fiscal and monetary policies should accordingly be formulated to meet the requirements of sustained growth and equitable development.

2. The three states of Darfur are Northern Darfur state, Southern Darfur state and Western Darfur state.

Abuja Agreement specified the strategic objectives of post conflict economic recovery and development of Darfur states as follows:

1. Integrating the economy of Darfur's three states into the national economy.
2. Rehabilitating the basic services, mainly access to safe drinking water, education, and health.
3. Eradicating poverty and creating adequate employment opportunities.
4. Building institutional capacities and developing human capacities to improve accountability and governance.
5. Encouraging the development and production of alternative energy sources and addressing causes of environmental degradation.

A noticeable issue in the discussions of Abuja is that the armed combatants wanted greater financial commitment to compensate victims. They also wanted clearer engagement of GNU to transfer wealth to Darfur. These demands increased the financial obligations of the GNU budget and could only be met within a medium term programme.

3. Eastern Sudan Peace Agreement (ESPA):

The Eastern Sudan Peace agreement (ESPA) was signed in Asmara, Eritrea, in October 14, 2006. By signing this agreement, an end was put to the conflict in Eastern Sudan. The fiscal arrangements that shape this agreement are centred around two issues: The first is the direct transfers from the federal government to the eastern states. The second is the transfers to the Eastern Sudan Development Fund.

The FFAMC should assure proper transfer of the assigned amounts to the eastern state. The Eastern Sudan Reconstruction and Development Fund (ESRDF) should serve as the principal organ in the planning, monitoring, and follow up of the reconstruction and development programme. The ESRDF should receive the following allocations from the central government: USD 100 million as an initial payment in 2007, and USD 125 million in 2008, 2009, 2010, and 2011 respectively.

5. The current nature of fiscal transfers

The design and adoption of an intergovernmental transfer system is highly influenced by non-economic factors, such as political, social or cultural. Therefore, the purely economic analysis of the system of transfers has limitations (Ter-Minassian 1997). In that sense, the adoption of a system of intergovernmental transfers serves multiple purposes, especially if these transfers were meant to resolve armed conflicts and sustain peace processes.

To fully adhere to the implementation of these WSAs, the federal Ministry of Finance and National Economy adopted a system of intergovernmental transfers to ensure that the different regions of Sudan will get their share of the exploited wealth and exercise their fiscal freedom in putting the transferred resources to best use. These transfers were made out of a pool of national revenues deposited in the National Revenue Fund (NRF). The main sources of revenues to the NRF are the oil proceeds and direct and indirect taxes.

We can observe three categories of intergovernmental transfers in Sudan. They are:

1. *Conditioned current transfers:* In this category the central government enforces certain rules and guidance over the recipients by specifying certain spending arrangements. An advantage of this system is that it provides protection to certain vulnerable groups and assists specific economic purposes. Conditioned transfers consist of various components that include:
   a) Transfers to cover wages and salaries of national institutions, mainly the wages and salaries of the police, higher education employees, the judiciary, and the cost of recruitment of the graduates at the states.
   b) Transfers to cover the purchases of goods and services for the police, higher education, and wages and salaries of the judiciary employees at the state levels.
   c) The transfers of social subsidy to meet social requirements of certain vulnerable groups. In a way, these transfers provide direct support to poor students in the states. They cover the cost of feeding the prisoners at all the prisons across the states, and meet the cost of free health care and health insurance.

2. *Unconditioned current transfers:* The recipients of these transfers exercise their powers over the money they receive. This category comprises: a) Transfers to the Government of Southern Sudan; b) transfers to oil producing states; c) transfers Abyei, Blue Nile, and Nuba Mountains; d) Compensation for the states which were affected by the elimination of the agricultural taxes[3]; e) VAT transfers; and f) Transfers to the reconstruction and development funds for the war affected areas.

3. *Transfers to state development.*. This category of transfers comprises development projects financed by local currency and by foreign loans, and classified under acquisition of non-financial assets in the national budget.

Other channels of fiscal transfers are the allocations made to the various development and reconstruction funds. The wealth sharing agreements called for the establishment of the following Funds:

1. Southern Sudan Reconstruction and Development Fund (SSRDF).
2. Darfur Reconstruction Development Fund (DRDF).
3. Eastern Sudan Reconstruction and Development Fund (ESDRF).
4. National Reconstruction and Development Fund (NRDF).

3. Agricultural tax exemption is a policy for giving incentives to small farmers.

Table 1. ***Evolution of conditioned and unconditioned transfers***

Item	2005	2006	2007
C.C.T	501.7	512.9	705
U.C.T	1130.9	2199.8	2246.8
Devlp. Transf.	537	866.5	1090.3
Total	**2169.6**	**3579.2**	**4042.1**
Nominal GDP	66714	79046	93200

* *Source:* Ministry of Finance and National Economy - Sudan
** Figures are in million Sudanese pounds (1US dollar is equivalent to about 2 Sudanese pounds).
*** C.C.T.: conditional current transfers.
*** U.C.T.: Unconditional current transfers.

Table 1 shows the transfers that were mandated by the various wealth sharing agreements during the 2005-2007 period. The total intergovernmental transfers totalled on average, four percent of GDP. This allocation is considered to be substantial by all proportions.

There is a tendency to increase the unconditional transfers more than the other allocations. Unconditional transfers represent 57 percent of total transfers on average, during the period under consideration. Unconditional transfers are very difficult to monitor by FFAMC, since the FFAMC has no authority to put guidelines for utilising these resources and to assess their impact.

Transfers to development represent an average of 25.4 percent of total transfers. This category of transfers could be considered as conditional in the sense that it is directed at financing specific capital expenditure activities. Although these transfers are assumed to have the biggest allocations, in reality, their allocations have a ceiling.

The conditioned current transfers represent only 17.6 percent of the total allocations. A drawback of this allocation is its direct support to cover wages and salaries of certain groups of employees and its support of current expenditure. This type of transfers is prone to boosting consumption at the state level and adding to the pressures on prices.

A balance should be drawn among the three categories of transfers to ensure that vulnerable groups are not subject to marginalisation so that all communities taste the dividends of peace on equal basis in terms of adequate service provision, adequate infrastructure, and conducive living environment.

Table 2 shows that substantial resources were allocated to the various reconstruction and development funds. For these allocations to be effective in realising development at the state levels and in the war affected areas, efficient expenditure planning is required to avoid wastage of these resources.

The strengths of this transfer system could be reflected in the point that it is well integrated within the budgetary process and well defined along the budget classification. These transfers are transparent when allocated, transferred, and monitored. Beneficiary states participate at different levels of the process.

Table 2. ***Allocations of the development and reconstruction funds***

Item	2006	2007	2008
SSRDF	300	300	-
DRDF	300	200	200
ESDRF	-	100	125
NRDF	250	250	125
Total	850	850	450

Source: Ministry of Finance and National Economy (Sudan) and the wealth sharing agreements. Figures are in million US dollars.

For conditioned transfers, the state institutions know the amounts of their allocations in advance. For unconditioned transfers, the state governments know the volume of their allocated transfers during the year. The advantage of this prior information is that the state governments are able to plan their priority expenditures and how to allocate the budgeted transfers to finance their activity.

On the basis of these strengths, GOSS, Darfur, and East of Sudan were able to get substantial financial resources to start various development activities and programmes that could:

a) Reduce disparity among regions and the states.
b) Create employment at the regional and state levels and subsequently reduce poverty.
c) Soften the severe impact of war and enable the rural communities to feel the dividends of peace.
d) Provide regions and the states with adequate infrastructure to stimulate and attract local and foreign investment.

In order for these to be truly achieved, there should be strong commitment from the sub-regional governments to put the received transfers to efficient use. Also the GNU must commit to timely delivery of the mandated transfers.

To be more effective, the adopted system of current transfers should be moved towards more rules-based mechanism instead of negotiated transfers. This will allow much better redistribution of resources among regions and better resource allocation within the economic activities. We can distinguish four types of formulas for equalisation transfers:

1) Formulas that consider revenue capacities and expenditure needs of the regions.
2) Formulas that consider the equalisation of revenue capacity only.
3) Formulas that are based on some expenditure needs indicators.
4) Formulas that distribute transfers on an equal per capita basis.

Since all armed movements in the conflict areas are calling for equal share of the available financial resources, we can consider the first type of formulas as the most sensible mechanism of transfer. Following earlier studies (e.g., Ahmed *et al*. 2004), a general model for intergovernmental transfer could be suggested. A simple method of calculating the transfers to each beneficiary state could be illustrated to show how to implement an equalisation transfer system with a minimum data requirement. Although full equalisation is not easily attainable, this formula could be looked at as a mechanism for the redistribution of fiscal resources.

Let:

$$TR_i = (N_i - C_i) - OTR_i \tag{1}$$

where TR total transfers to the state, N_i is the expenditure needs of the ith state, and C_i is the revenue capacity of the ith state. The value $(N_i - C_i)$ measures the fiscal deficit in the ith state. OTR_i represents other transfers that the ith state receives from the central government. The other transfers embody the share of the state from the oil revenues.

This formula states that the central government transfer will cover the fiscal deficit in the ith state, i.e. the difference between the expenditure needs and the revenue capacity.

The transfers that the total states can get should be adjusted proportionally according to the volume of the revenues available in the NRF, such that:

$$ATR_i = \left(\frac{TT}{\sum TR_i}\right).TR_i \tag{2}$$

ATR_i is the actual transfers that the ith state receives, and TT is the total size of the transfers.

There are two issues of important considerations when making the calculations of the transfers using the revenue capacity expenditure needs formula:

a) The first issue is how to measure the revenue capacity of each state. The revenue capacity is defined as the ability of the state government to raise revenue from its own resources. In many developing countries, this capacity is measured by using data on major tax bases and tax rates applied within the boundaries of that particular state. Another method to assess the revenue capacity is by employing some income or output indicators. Frequently used indicators comprise: i) Gross domestic product calculated for the particular state; ii) the disposable personal income of the residents in each state; and iii) total purchases and sales of commodities in the state.
b) The second issue is how to measure the expenditure needs. This could be done by formulating an expenditure plan that reflects the costing and estimates of the development objectives of the state government. Seven categories are most likely to comprise these expenditure needs for a typical conflict-affected state or region. There are expenditure needs for education, health service provision, social welfare, government administration, securing law and order, rehabilitation of infrastructure, and securing safe drinking water.

6. Challenges and constraints of the system

The currently adopted system of intergovernmental transfers has many strengths and benefits. However, it also faces many challenges and obstacles, which, if not corrected, will affect the effectiveness and the efficiency of implementing the transfer process and threaten the peace-building process. The system also assigns too much responsibility to the state governments. This poses new challenges for public expenditure management by the sub-national governments. The challenges are as follows:

1. The need to co-ordinate the budgetary policies of the national and the sub-national governments in order to ensure the full consistency with the macroeconomic objectives of the entire Sudan.
2. The need to promote the degree of responsiveness of the sub-national governments to the requirements of the citizens in both the allocation of budgetary resources and the delivery of goods and services assigned to them, in an efficient and cost-effective way.
3. The need to have in place sound financial management of the operations of each level of government.
4. Each of the three agreements should reflect the particular development problems of that region and should propose a guideline to development. The south is endowed with oil and livestock. Darfur is endowed with livestock and agricultural production. Eastern Sudan is endowed with agricultural and livestock production. The main challenge is to gear these resources to the development of the endowed resources of each region and provide employment for the population.
5. Developing the institutions in these regions is a serious challenge. Efficient institutions should back suitable policies to develop the economies of the conflict regions.
6. An important element in building these institutions and monitoring the implementation of the various clauses of these agreements is the human development through training and education. Education is a national issue. The central government should increase investment in education and further invest in raising the management capacity at the regional level to ensure efficient resource management. Most of the conflict regions and war-affected areas suffer from brain-drain. In some regions, there is acute shortage of well-trained human resource.
7. The three agreements should be well integrated within a macroeconomic framework that cares for the stabilisation of the national economy and aims at high economic growth. Integrating the three agreements is not an easy job. The economies of the states are not well organised and measured. Neither is the contribution of the regional economies into the national economy well documented. Regions and the states have different levels of monetisation. A detailed account of the economies of

the various regions in terms of the levels of GDP, consumption, private sector contribution and financial intermediation is an essential task.

8. The financial components of the wealth sharing agreements were based on the volume of the national revenue flow. The oil revenue constitutes more than 70 percent of the resources. The problem here is that oil prices are volatile and unpredictable, beside the fact that oil is an exhaustible resource, which will wither away in a finite time. This will complicate long-run expenditure planning and prioritisation. In the short-run, these resources will be put to finance short-term obligations, but will increase the level of current expenditure rather than increasing capital expenditure. Current expenditure may not be productive, hence there is the possibility that the recipient states may not benefit from these transfers in real terms. This will most likely put pressure on the overall price level, and could lead to inflation and affect the stability of the economy.

7. Suggested issues to improve the system

The beauty of any agreement rests in the ability of the parties to honour its clauses. If fiscal transfers are designed well, then they will realise benefits of a genuine central-regional government relationship in basic service delivery, poverty reduction, and the accomplishment of broader national macroeconomic objectives of economic stability and growth. Ultimately, this will put an end to the tendencies of the emergence of armed movements.

Poorly designed systems will erode the government's ability to provide basic services, and lead to collapse of the social safety nets. Corruption will emerge and conflicts could re-erupt.

The essence of the system depends on the scope of the reforms incorporated and implemented. Given the current system of transfers, more reforms could be suggested to increase its efficiency and effectiveness. They include the following:

1. The rules and the procedures of the system should be flexible enough to allow the parties to take frequent assessment and evaluation and adopt changes as necessary.
2. Some of the unconditioned transfers should be conditioned. This is necessary to ensure that at least a minimum level of development is achieved. There should be concentration on the provision of the basic needs and services, such as health, basic education, and access to safe drinking water.
3. An important element in the effectiveness of this system is the efficient management of the bulk of the resources. The FFAMC should allocate resources to build human capacity at the state level to improve monitoring and evaluation. Efficient monitoring and evaluation will enhance

the effectiveness of the transfer system in achieving the development goals and objectives.

4. The bulk of the resources should be modelled within a national budgetary macroeconomic framework. The transfers should also be built within a medium term national development strategy.

8. Conclusion

The signed three peace agreements to resolve the conflicts in southern, western, and eastern Sudan forced the GNU to adopt fiscal arrangements that embody a system of intergovernmental transfers. The main objective is to allocate and transfer adequate resources to these conflict areas so that they realise genuine development and mobilise human resources in a way that will consolidate peace-building, reduce poverty, and increase the standard of living among the rural communities through the provision of basic services.

The system proved to be quite effective in availing substantial resources to serve these objectives, and empowered the state governments to exercise some degree of fiscal freedom in the sense that they obtained more power to plan and allocate resources according to their specific needs.

The current transfer system provides the necessary but not sufficient elements of effective fiscal arrangements that could serve as an effective arm in putting an end to the armed conflicts in Sudan. It will redirect substantial resources for the benefit of the people of Sudan.

More reforms were required to strengthen the system, especially in the areas of fiscal and financial management, expenditure control, and cash management.

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