

Unpacking Decentralization

Decentralization is defined as the transfer of authority, responsibility and resources through deconcentration, delegation or devolution – from the centre to lower levels of administration. Theoretically, decentralization is neither good nor bad for efficiency and equity in terms of public service delivery. It needs to be recognized however that decentralization across countries has been predominantly a political process and not an economic one. The effects of decentralization depend on institution-specific design, which relates to the degree of decentralization and how decentralization policy (in terms of functions, finance and functionaries) and institutions interact. Despite the growing recognition across countries that decentralization can play a pivotal role in the economy for efficient delivery of public goods and services, especially in the countries of sharp regional disparities and heterogeneous population, there is few related literature – both theoretical and empirical – on the topic especially in the context of India.

This book discusses the theoretical and empirical evidences related to the effectiveness of decentralization on specific public services, viz. education and health in India. Apart from an extensive review of literature, the study incorporates fresh analysis of decentralization, both in the Indian and global contexts. It undertakes the analysis of the benefit incidence of decentralized public service delivery with respect to health and education – an area which has not seen much attention in the past. The specific objective of this book is to provide a comprehensive review of research relating to the effectiveness of decentralization on education and health within the broad framework of institutional set-up, the degree of financial autonomy and accountability, and benefit incidence of decentralized public expenditure on health and education.

The study assumes relevance in the context of India for two important reasons. The first and foremost is the legal fiat, i.e. the 73rd and 74th constitutional amendments giving recognition to the local self-governments. The second issue is the fiscal fiat, where there is asymmetry in functions and finance at the local level where functional responsibilities far exceed the revenue resources of local bodies leading to the problems of ‘unfunded mandates’. At the same time, there are efforts from the higher levels of governments to use the institution of local self-governments for the provisioning of various public services through various specific

purpose transfers.¹ Our objective is to examine how effective is decentralization on service delivery with respect to health and education given the constraints of unfunded mandate.

Decentralization: From theory to process

Conceptually, decentralization assumes importance in the light of the *principle of subsidiarity* which argues that for the most efficient public provisioning of goods and services, government activities should be located at the level of government closest to people² (Oates, 1972). However, operationalizing decentralization is not simple, it may involve conflicts and trade-offs. In its simplest form, decentralization is the transfer of both authority and responsibility for public functions from the central government to subordinate levels of government (provincial and local) or, in some special cases, even to the private sector within four broad areas of government activities (World Bank, 1999):

- (i) Political decentralization – Focuses on the transfer of the responsibility and authority for political self-determination from the central government to subordinate levels of government in particular for the formulation and implementation of policies.
- (ii) Administrative decentralization – Seeks to redistribute authority, responsibility and financial resources for providing public services among different levels of government.
- (iii) Market decentralization – Privatization and deregulation are the core elements of market decentralization that is directed toward the creation of a free-market in which government and industry cooperate to provide public services or infrastructure.
- (iv) Fiscal decentralization – The core component of decentralization is fiscal decentralization by which the government transfers revenues or allows the subordinate government levels to raise their own funds.

Thus, the prerequisite for effective functioning of decentralization is the functional autonomy of the local governments supported by appropriate devolution of financial resources. Otherwise there will be horizontal and vertical imbalances between the expenditure needs and the available

¹ Many centrally sponsored schemes are being implemented by the local governments.

² Oates Theorem explains that the responsibility for providing a particular service should be assigned to the smallest jurisdiction whose geographical scope encompasses the relevant benefits and costs associated with the provision of services.

resources of the decentralized layer of the governance, which may hinder the developmental functions at local level. The first generation theory of decentralization talks about efficiency gain, and second generation theories talks about responsiveness and accountability through decentralization. As argued by Oates (2005), second generation theories “are moving beyond a purely static view of the incentive structure and potential performance of federal institutions to a broader consideration of the evolution of federal structure over time with attention to the stability of institutions and their capacity of be ‘self-enforcing’” (p. 368).

Voice and exit

The theoretical underpinnings of the link between decentralization and service delivery are accountability (‘voice’ and ‘exit’), information symmetry, transparency and appropriate size of government at local level. The degree of accountability (‘voice’) in a federal set-up is based on dual conjecture: (i) accountability of sub-national government to higher tier of government and (ii) to the electorate. The former limits the latter, especially in cases where financial decisions are centralized, but the provision of public goods is decentralized. The dichotomy of finance from functional assignment can lead to inefficiencies, the most oft-cited problem being of *unfunded mandates*. On the other hand, the real autonomy of the governance plays a crucial role in efficient public service delivery; however, their accountability to the electorate gets constrained if the flow of funds is through *deconcentrated* intermediate levels with accountability to the Central government. However, it is established that fiscal policy in a federal setting promotes government accountability, particularly in geographically or demographically large nations (Stern, 2001). In a federal set-up, monitoring and control of governance by local communities is easier in principle. At the sub-national level, elected governments can be expected to be generally more accountable and responsive to the human development concerns. Decision at the sub-national level gives more responsibility, ownership and thus incentives to local agents, and local information can often identify cheaper and more appropriate ways of providing public goods (Stern, 2001 and Bardhan, 1997).

The axiom of ‘exit’, which provides yet another mechanism for accountability, refers to the mobility of population. Theoretically, citizens who are dissatisfied with the public provisioning of services by one local government can ‘vote with their feet’ by moving to another jurisdiction that better meets their preferences. Interjurisdictional labour mobility may be an instrument of local accountability, when citizens reveal their preferences by strengthening ‘exit’.

Elite capture

One of the risks of decentralized public service delivery is the dominance of elite groups within the jurisdiction and their influence in control over financial resources and in the public expenditure decisions related to the provisioning of public goods and governance. There is growing evidence that power at local level is more concentrated, more elitist and is applied more ruthlessly against the poor than at the centre (Griffith, 1981). This is referred to as *elite capture* in theoretical literature. In such a setting, the 'voice' of poor may get neutralized by political pressure groups. The benefits of decentralized socio-economic programmes would be captured by local elite, which in turn would result in under investment in public goods and services for poor. This is particularly true in the context of heterogeneous communities and underdeveloped rural economies (Bardhan, 1999 and Ravallion, 2000). The aberrations in 'voice' may induce possibility of greater corruption at local levels of government than at the national levels. Corruption in turn deepens capability deprivation. There is empirical evidence indicating that decentralization increases corruption and reduces accountability (Rose and Ackerman, 1997 and Tanzi, 2000).

Asymmetric federalism and intergovernmental competition

A centrally determined 'one size fits all decentralization policies' cannot be a solution to redress inequities in a country with vast population and heterogeneity across jurisdictions. Given the heterogeneity in the efficiency of public service provisioning across jurisdictions, it may be timely to consider the scope of 'asymmetric federalism'³ in incorporating human development into decentralized fiscal policies; and one way of looking at this is the process of accreditation where the sub-national governments which pass minimum standards in service and product delivery and specific attributes of governance could be given greater autonomy in functions and finance. This requires benchmarking the governance of sub-national governments, which may catalyze horizontal competition among the states. It can ensure gains in efficiency and increase in productivity through the 'Salmon mechanism' in which intergovernmental competition is activated by benchmarking the performances of other governments

³ 'Asymmetric federalism refers to federalism based on unequal powers and relationships in political, administrative and fiscal arrangement spheres between the units constituting a federation. Asymmetry in the arrangements in a federation can be viewed in both vertically (between Centre and states) and horizontally (among the states). If federations are seen as *indestructible union of indestructible states*, and Centre and states are seen to exist on the basis of equality; neither has the power to make inroads into the defined authority and functions of the other unilaterally' (Rao and Singh, 2004).

in terms of levels and quality of services, of levels of taxes or more general economic and social indicators (Salmon, 1987).⁴ The voters and opposition parties compare the supply performance of their governments with the benchmark performance and influence supply decisions.⁵ This benchmarking of local governance can empower poor to compare the relative performance of their governments in terms of the tightness of 'wicksellian connections'⁶ and influence supply decisions of their jurisdictions to design and implement appropriate policies and programmes to ensure equity.

Intergovernmental competition and the mechanism of exercising choice by the citizen-voters either through 'exit' or by 'voice' helps to reveal preferences of public services (Rao, 2002). The theoretical literature elaborated that competition results in innovations in the provision of public services and in respect of public goods, it helps to identify the beneficiaries and impose user charges on them. However, the efficiency in the service delivery and welfare gains accrued and the enhancement of accountability depends on the nature of intergovernmental competition and political institutions (Breton, 1996).

Asymmetric information

Information symmetry is one of the important factors to hold sub-national government accountable. The proximity of policymakers to people has high probability of better information on needs and demands of citizens as they participate effectively and exercise their 'voice' in terms of revealing preferences and also the accountability of local governments towards the public provisioning of the services. It is argued that higher the information symmetry, higher the accountability and transparency of the local government. Information symmetry can reduce the transaction costs on both sides, provider's side and the citizen's side. In this context, the size of the local government is also an important issue. The

⁴ As cited by Albert Breton and Angela Fraschini, 2004 and Rao, 2006.

⁵ Breton, 1996 and Salmon, 1987.

⁶ A *wicksellian connection* is a link between the quantity of a particular good or service supplied by centre of power and the tax price that citizens pay for that good or service (Breton, 1996). Knut Wicksell (1896) and Erik Lindahl (1919) showed that if decisions regarding public expenditures and their financing were taken simultaneously and under a rule of (quasi) unanimity, a perfectly tight nexus between the two variables would emerge (Breton, 1996). Breton (1996) argued that competition between centre of power, if it was perfect and not distorted by informational problems, would also generate completely tight wicksellian connections. In the real world, competition is, of course, never perfect and informational problems abound and, as a consequence, wicksellian connections are less than perfectly tight. Still, as long as some competition exists, there will be wicksellian connections (Albert Breton and Angela Fraschini, 2004).

size of the lowest tier of the government varies significantly across countries. It is often argued that lower the size of the local government, higher the inefficiency in public service delivery. It is often because of lack of capacity to manage all the functions assigned to them. On the other hand, lower the size of local governments, greater the participation and accountability. The real challenge at this point is a judicious structure of local government, which is not only politically acceptable, but can also provide efficient delivery of public services. The appropriate scale for key services should be an important element in the governance structure at the local level.

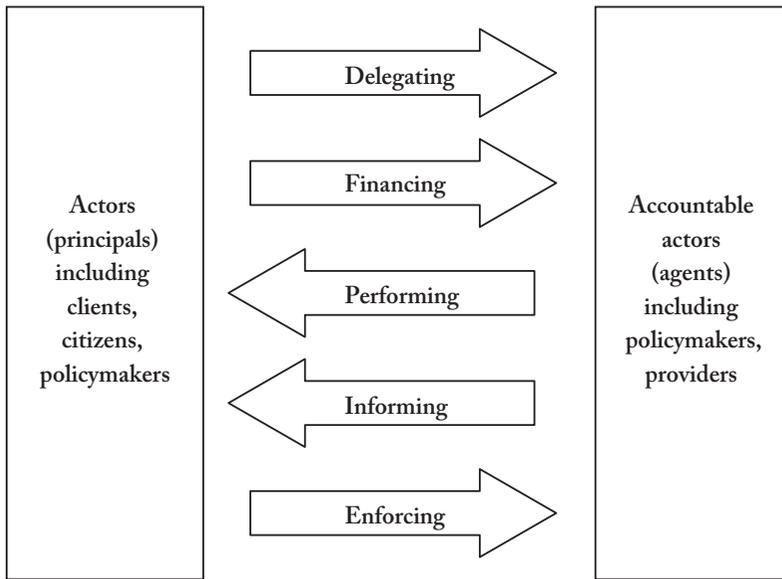
Accountability framework of decentralized service delivery

The analytical framework of effectiveness of decentralization on public service delivery can be traced to 2004 World Development Report (hereafter WDR 04), *Making Services Work for Poor People* (World Bank, 2004). WDR 04 provides the link between decentralization and public service delivery in an accountability framework. The core of the argument in WDR 04 is that the effectiveness of public service provisioning for the poor has its roots in institutional mechanism in which agents in service provisioning are accountable to each other and the process is transparent.

Five facets of accountability framework of decentralized service delivery

The five facets of accountability provided in WDR 04 are illustrated in Figure 1.1. This comprises: (i) delegation, (ii) finance, (iii) performance, (iv) information and (v) enforceability. In this analytical framework, it is impossible for each of the facets of accountability to operate in watertight compartments. For instance, lack of flexible financial resources at the decentralized levels thwarts the agents from being accountable for their performance. Secondly, if the functional delegation is not clearly defined and not linked to quantitatively measurable desired objectives, the enforceability from the service providers would be ineffective.

Thirdly, reversing the sequence of decentralization, from ‘functions precede finance’ to ‘finance precedes functions’ to avoid ‘unfunded mandates’ might also encounter the problems related to accountability, if there is elite capture of funds devolved or any corruption which creates disequilibrium at the decentralized levels (Chakraborty, 2010). It is also equally important to ensure information symmetry for enforceability.

Figure 1.1: Five facets of accountability

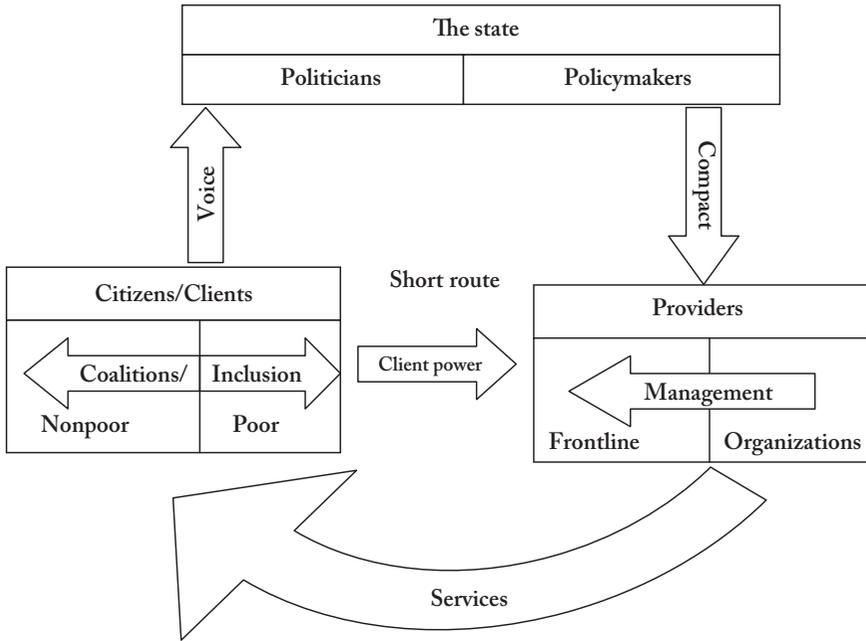
Source: World Bank (2004).

Three pillars of accountability in service provisioning

WDR 04 suggests that there are three sets of actors involved in effective provisioning of decentralized service delivery. They are: (i) citizens or clients, (ii) policymakers (inclusive of politicians) and (iii) service providers (Figure 1.2). Through exercising adult franchise, citizens exercise ‘voice’ over politicians. The policymakers work in concomitance with the service providers. The clients/citizens exercise client power through transactions with the service providers, including monitoring the service providers. The interlinkages are illustrated in Figure 1.2.

There are two routes of accountability – short route and long route (these routes have been discussed in greater detail in Chapter 9). WDR 04 argued that when markets alone are involved and all decisions rest directly with citizens who can enforce them through competition, we have a short route of accountability – citizens holding providers directly accountable. But where the state and the public sectors are involved, voice and compacts make up the main control mechanism available to the citizen or client in a long route of accountability. However, it is a subject matter for debate whether market mechanism is the short route of accountability than state. The failure in service provisioning arises from the drawbacks in either the short or the long route of accountability.

Figure 1.2: Accountability framework: The long and the short routes

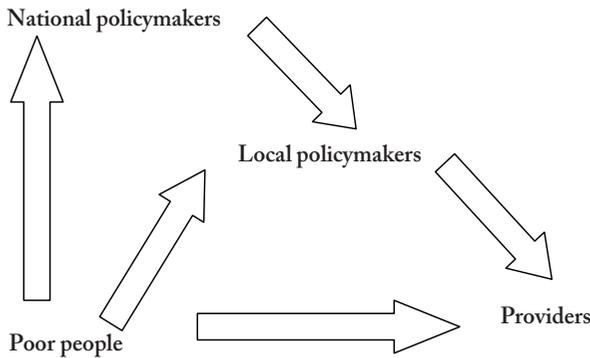


Source: World Bank (2004).

Decentralization and accountability link

Decentralization introduces an additional element into the framework of accountability, that is, sub-national or local government. This introduces two new links between decentralization and service delivery: (i) between national and sub-national governments and (ii) between citizens and sub-national governments (Figure 1.3). These links could be interpreted differently under different components of decentralization (reference to Rondinelli's threefold classification of decentralization: (i) deconcentration, (ii) delegation and (iii) devolution).

For instance, 'deconcentration' primarily affects the compact relationship between national level policymakers and their local frontline service providers, but may have little influence on voice at the local level. On the other hand, devolution is an effective mechanism of accountability as it implies transfer of greater resources from the national level. Though the power to allocate these resources across different uses would be ultimately decided by the local politicians, devolution may provide greater scope for strengthening local voice, their compact with local providers and local client power.

Figure 1.3: Links between decentralization and accountability

Ideally, the intergovernmental fiscal system works well when (i) there is capacity at different levels of government, (ii) there is strict monitoring system of public bureaucracies and (iii) the sub-national government could also collect taxes and spend untied/discretionary funds on service delivery. In these situations, WDR 04 argued that the local political accountability is strong because citizens associate performance with the spending decisions made, implemented and monitored by their local governments. Under these conditions, the accountability of national and local policymakers to citizens is strong.

Partial decentralization

Partial decentralization can occur if local governments remain dependent on fiscal transfers from central government and are less accountable to their electorates. When local governments are not held accountable for a complete set of budgetary allocations and their outcomes, it is 'partial decentralization'. In other words, decentralization is partial when national governments have not given the local government discretion over all aspects of budget. Interpreting within the framework of Figure 1.3, partial decentralization means that the accountability between citizens and local policymakers ('local voice') is weak. But when decentralization is partial, citizens continue to expect that their national governments would provide service delivery. In such situations, it is argued that citizens are more likely to vote in or vote out national political representatives than their immediate local political leaders. In partial decentralization framework, the short and long routes to decentralization get ineffective due to lack of accountability.