

COMBATING THE CRISIS IN GOVERNMENT ACCOUNTABILITY

A Review of Recent International Experience

Dilip Mookherjee¹

December 26, 2001

*R.C. Dutt Memorial Lectures, Center for Studies in Social Science, Calcutta, December
27-28, 2001*

¹Department of Economics and Institute for Economic Development, Boston University; dilipm@bu.edu

1 Introduction

It is exactly one hundred years since the publication of Romesh Dutt's monumental *Economic History of India*. As is well known, this treatise dealt principally with the role of British colonial taxation, land and administrative policies on India's economic development. Dutt's perspective is remarkably balanced and fair-minded: giving credit where it was due, while identifying key areas of neglect, weakness and oversight. A century later, including a half century of Independence, the role of colonial taxation, tariff and land policies is now mainly of historical interest. But his discussion of administrative reforms continues to be highly pertinent.

Within this area, Romesh Dutt dwelt on separation of powers, representation by Indians, judicial and police administration, devolution of powers to local village communities, education, and the public press. A hundred years later, development economists and multi-lateral institutions are becoming increasingly preoccupied with government accountability to its citizens, which depends on many of the same institutions: the democratic process, devolution to local governments, empowerment of minorities and the spread of education. The focus on government delivery of infrastructure and social services has been increasing throughout the developing world amidst the general trend towards privatization and deregulation in the 1990s. Disparate literatures in economics — e.g., both macro cross-country growth regressions and micro institutional analyses — now recognize that growth and poverty reduction rely critically on provision of infrastructure, education, health and social security, and that this is where reforms are most urgently needed.

It is becoming equally well recognized that the top-down state-led pattern of development planning in vogue in earlier decades paid insufficient attention to institutional context within which these services were provided by government. The result was widespread failure to maintain cost-effectiveness, match investment to local needs or limit corruption in implementation of government programs. The development landscape is now littered with stories of large scale diversion of resources of public funds, poorly performing schools and hospitals, and development projects ill-suited to local needs. Compounding these are weaknesses in tax administration and widespread tax evasion that limit resource mobilization

by the government.

What can be done about the current crisis of lack of government accountability? Political scientists typically emphasize the role of political institutions, sociologists focus on the role of ethical norms, while economists study economic incentives and how they are shaped by the institutional setup. The division between politics and economics has been mirrored by the distinction frequently drawn between **political** and **bureaucratic** corruption, concepts which go back at least to Susan Rose-Ackerman's (1978) pioneering book.² In a democratic context, political corruption refers to the problem of agency between citizen and elected official, and the way it is affected by institutions that define the electoral process, such as division of powers between different branches and levels of government, the role of the legal system, media and civil society in influencing public policy and its implementation. In short it deals with the policy formulation process, and high level corruption of politicians. In contrast bureaucratic corruption is concerned with problems of policy implementation, and how it can be stymied by poor information and coordination systems, corruption among government bureaucrats and employees. This is the kind of petty corruption that is more visible to citizens in their everyday lives, manifested by bribes that citizens must pay government officials to receive the services to which they are entitled. As Rose-Ackerman pointed out, bureaucratic corruption arises from the delegation of authority by politicians to bureaucrats over the implementation of its programs. It is influenced by systems of pay, task assignment and monitoring of bureaucrats, as well as the internal organization of the bureaucracy. Unlike political institutions that define the extent and scope of high-level political corruption, bureaucratic corruption has been the main focus of economists accustomed to analyzing problems of information and incentives.

A watertight distinction between political and bureaucratic corruption is of course impossible. High level political corruption encourages low level bureaucratic corruption, by avoiding firm steps that might eradicate the latter. Robert Wade's description of the market for public office within the Andhra Pradesh irrigation bureaucracy vividly describes the way that bribes cascade upwards through the bureaucracy, all the way up to politicians that

²Susan Rose-Ackerman, *Corruption: A Study in Political Economy*, New York: Academic Press, 1978.

need to rely on such illicit sources of income to contest elections successfully.³ In reverse vein, the BBC Program *Yes Minister* indicates the enormous influence exercised by top bureaucrats over policy formulation.

Yet it can be argued that the distinction between political and bureaucratic corruption is a fruitful one, for various reasons. It allows focus on a different set of institutions, the analysis of which corresponds to the comparative specialization of disparate disciplines of politics and economics. It is possibly true, moreover, that the two are characterized by different historical patterns. High-level political corruption seems an almost universal feature of all societies, judging from the frequency of corruption scandals that surface in the media and topple governments nowadays. Reliable data comparable across different countries on political corruption is of course not available. Efforts to gauge the extent of political corruption would also have to contend with the problem of identifying the extent of legalized forms of corrupt influence, for instance of the form where special interest groups can purchase influence via lobbies and campaign contributions. But it is undeniable that the problem is pervasive, affecting countries at all levels of development.

On the other hand, casual empiricism would suggest that low level bureaucratic corruption tends to eventually decline and perhaps vanish in the course of economic development. This is confirmed by the corruption index compiled for different countries by Paolo Mauro based on bribes paid by business people show a strong pattern for corruption to be lower in wealthier countries, a pattern also matched by other indices of bureaucratic inefficiency, red tape and integrity of the judicial system.⁴ Indeed, in countries such as Japan the contrast between high levels of political corruption and the near absence of bureaucratic corruption in their dealings with common citizens is striking. Nineteenth century accounts of political machines in local government in the United States indicate widespread corruption at all levels, on a range and scale comparable to those observed in developing countries today. Yet much of the low level corruption seems to have disappeared or significantly reduced today, owing in large measure to a set of ‘progressive’ reforms in city administration at the

³Robert Wade, “The Market for Public Office: Why the Indian State is Not Better at Development,” *World Development*, 13(4), 1985, 467-97.

⁴Paolo Mauro, “Corruption and Growth,” *Quarterly Journal of Economics*, CX(3), August 1995, 681-712.

turn of the previous century.⁵ These reforms effectively transferred authority away from corrupt politicians to professional bureaucrats with long term appointments, less immune to the pressures of machine politics and short term re-election goals. Political corruption was replaced by a professional and largely honest bureaucracy.

However, the relevance of the American historical experience for developing countries a century later is unclear, since the nature of the problem is somewhat different. A large part of the problem in developing countries is a high level of bureaucratic corruption. Shifting responsibility from corrupt politicians to corrupt bureaucrats may not improve matters much, and would possibly make them worse. This makes the problem of combating corruption substantially more difficult. Common observers are consequently led to adopt a fatalistic attitude, arguing that reforms in political institutions or ethical norms are essential. Economists' discussion of changes in bureaucratic hiring, salary or task assignment policies are dismissed as exercises in a theoretical vacuum, with no hope for practical implementation.

Yet there *is* hope, I would contend. At the very least, there are many new reform options available. My optimism is based on a large number of bold and innovative reform experiments that have begun to be undertaken around the developing world in the last decade in the interest of promoting government accountability. In many cases the effects on certain dimensions seem to be nothing short of dramatic. In others the effects are difficult to evaluate, with a number of potential pitfalls and problems that need to be assessed and offset against the advantages. In yet other cases, practical implementation has strayed from original intent and have not been effective at all. Irrespective of how they are eventually evaluated, this period of active experimentation with different sorts of reform put to rest the fatalistic notion that nothing other than complete paralysis can be expected in the struggle to enhance government accountability. Most of these administrative reforms have occurred within given political systems and within a relatively short span of time. So they cannot

⁵For citations to historical accounts of corruption in local city governments, and related analyses see James Rauch "Bureaucracy, Infrastructure and Economic Growth: Evidence From U.S. Cities During the Progressive Era," *American Economic Review*, 85(4), 1996, 968-979, and Rebecca Menes, "The Effect of Patronage Politics on City Government in American Cities 1900-10," NBER Working Paper 6975,1999.

be said to be driven by changes in fundamental political institutions, political leaders or changes in ethical mores.

The purpose of these lectures will be to document and review some of these reforms, and newly emerging research that seeks to evaluate them. I hope this perspective on international reform experiences will be useful in a variety of ways. It should provide would-be policy reformers in other countries with a window on experiments pursued elsewhere. For social scientists, it provides an opportunity to constructively proceed to the challenging task of evaluating concrete policy experiments, and suggesting new ones. As will become evident, the reforms being undertaken involve changes both in political institutions and bureaucracies in some degree. Their analysis therefore necessitates a political economy approach, which should bring disciplines of politics and economics closer together. And most of all, discussion of these reforms should dispel the complete cynicism that is commonly heard in many discussions of corruption, by demonstrating that policy experiments intended to enhance government accountability are in motion throughout the developing world, despite the absence of far-reaching changes in underlying ethical values or political institutions. Instead of expressing mere anguish and despair, I hope public discussions will proceed to the constructive task of appraising alternative reform approaches for their suitability to any given country or region in a pragmatic vein.

2 Overview

The simplest formulation of the problem of bureaucratic corruption views bureaucracies as an agency intermediate between politicians and citizens, delegated authority by the former to deal with the latter on its behalf. See Figure 1 for this classic depiction as a three layer vertical hierarchy, corresponding to a unitary non-federated government. Bureaucrats are appointed and monitored by politicians, and report to them exclusively. They are allocated authority over collecting taxes, regulating behavior, and delivering government services to citizens. Bureaucrats are not directly accountable to citizens: whatever accountability exists is indirect. Citizens unhappy with government policies or the performance of bureaucrats hold elected politicians responsible, and can eject them from office either via electoral or non-

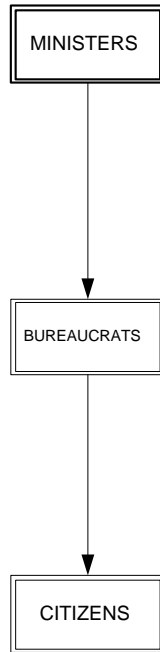


Figure 1: CENTRALIZED BUREAUCRACY

electoral processes. The threat of being ejected is the only force that motivates politicians to monitor and control the behavior of bureaucrats.

Bureaucratic corruption arises when bureaucrats behave in a self-interested fashion, rather than in the social interest. This corresponds then to the consequences of a decline in ethical norms of bureaucrats. Their control over citizens awards them with near-monopoly powers with regard to issuance of public services and government permits, and to relevant information concerning eligibility of different citizens or regions to receive these benefits. When their ethical values erode, they can charge bribes for delivering these services, and divert resources from public funds or resources into black markets or their personal consumption. Accordingly, government resources do not reach for whom they are intended. Growth is stunted on account of the high cost of conducting private business and delivering infrastructure service. Since the poor are less able to pay bribes than the rich, benefits of public expenditures do not reach those in greatest need; redistributive programs end up with limited impact on poverty alleviation. Taxpayers are less willing to comply with

their tax obligations, knowing that their contributions are likely to end up in the pockets of corrupt officials rather than serving any real social purpose.

The scope for such opportunistic behavior stems from the lack of ability or interest of politicians in controlling bureaucratic corruption. Ministers cannot of course run governments by themselves and dispense with the bureaucracy. Resources have to be allocated between different sorts of projects in different regions, materials required for these projects have to be procured, and benefits from these projects must be distributed across and within communities. These require the collection and processing of relevant local information, beyond the capacity of any central minister. Such decisions must therefore be devolved, and they have traditionally been delegated to a centralized bureaucracy consisting of government departments reporting to ministers. A fundamental problem of control then automatically arises: even if ministers were motivated to improve performance, the very lack of relevant local information that necessitates delegation of powers to bureaucrats, also prevents them from effectively controlling the latter. If the minister does not know if region A had a greater need for a road than region B, how can he check if the bureaucrat who selected region A as the location of the road behaved honestly or not? The problem is of course further compounded if the minister cannot verify whether the road was built anywhere at all.

Matters are even worse if the problem of bureaucratic corruption is complemented by political corruption: the minister may know perfectly well that the road was built at the inappropriate location or not built at all, and yet do nothing to rectify the situation or punish the errant bureaucrat. The decision concerning the road may actually have been made by the minister, and dictated to the bureaucrat. If such political corruption is at the root of the problem, then nothing short of political reform will make any difference.

In this context three alternative classes of reforms can be considered to enhance accountability of government. The first involves **bureaucratic reforms** which strengthen mechanisms of control exercised by politicians over bureaucrats. These include changes in pay, monitoring, task assignments, planning and information systems, reorganization of functions and divisions within bureaucracies. Ministers could seek to motivate bureaucrats by monitoring their performance more closely, instituting carrots and sticks to encourage

appropriate behavior, and reducing the extent of discretionary authority devolved to them. Reforms in planning and budgeting systems could be intended to improve coordination across different government agencies, and improve the flow of information available for planning. By themselves these reforms have little or no impact on political corruption. They may or may not have an impact on bureaucratic corruption, depending on the ability and motivation of politicians to utilize the expanded controls in an effective way. In a context of widespread political corruption, they are unlikely to be ineffective.

The second approach involves **political decentralization**, i.e., devolution of power to local governments. Discretionary authority over program selection and implementation could be shifted away from central bureaucrats and transferred to elected officials in local governments. See Figure 2 for an illustration. Despite being widely referred to as *decentralization*, these reforms may or may not be accompanied by a reduction of authority of central ministers. In more limited versions, ministers latter may still retain discretionary authority over the allocation of resources across regions and localities. Only the authority over intraregional allocations is transferred from bureaucrats to local governments. Specifically, locally elected government officials instead of central bureaucrats decide how local projects will be constructed or maintained, and how the benefits will be allocated within the local community. In other more extensive versions, the decentralization can be accompanied by substantial financial devolution as well. Local governments can receive a substantial fraction of central revenues based on formula grants, and can levy and collect own revenues through local taxes and user fees. The overall scale of spending on any given local project in a community is then decided by the community itself, rather than dictated by tied grants from the center. In these more extensive versions, the discretionary authority of central ministers is also reduced. In either limited or extensive versions, decentralization of powers to local governments reduce the scope for bureaucratic corruption by shifting discretionary authority over intra-community allocation away from bureaucrats to local communities. The extensive versions additionally limit the scope for high level political discretion, while expanding these at the local government level. These changes could also be accompanied by improvements in the informational base of decisions concerning local use of resources, since local communities are better informed than either central politicians or bureaucrats

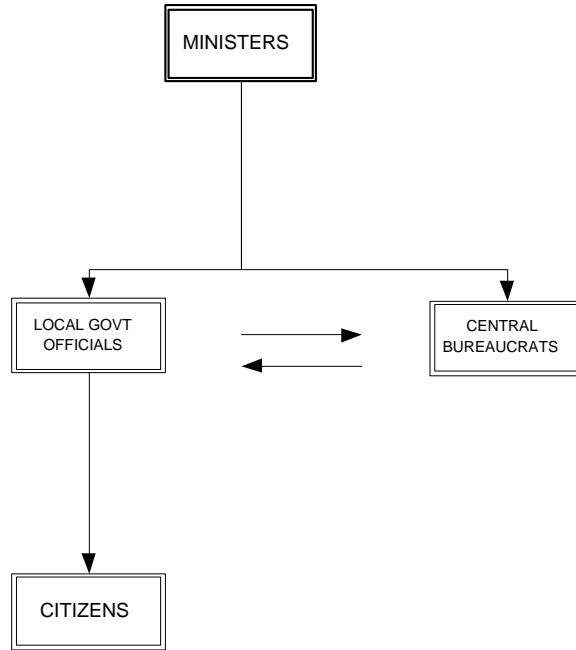


Figure 2: POLITICAL DECENTRALIZATION

concerning local costs and needs.

The third category of reforms are aimed at limiting the monopoly power of bureaucrats by expanding the range of alternatives and information available to citizens. The public sector may be opened to competition from private providers. Instead of providing services directly, the government may offer vouchers, cash or in-kind aid to households that subsequently select between public and private providers. The center may disseminate information about citizen entitlements and provide avenues for citizens to file complaints about poor service conditions. These correspond to what Albert Hirschman has referred to as *exit* and *voice* as disciplining devices on poorly performing public institutions.⁶ Particularly in schools, the voice option can include citizen and NGO participation in school management. By and large these reforms reduce the vertical hierarchical character of traditional top-down state systems depicted in Figure 1, by empowering citizens in a variety of ways, as depicted in Figure 3. They represent an alternative form of decentralization, which does not change

⁶Albert Hirschman, *Exit, Voice and Loyalty*, Cambridge, MA: Harvard University Press, 1970.

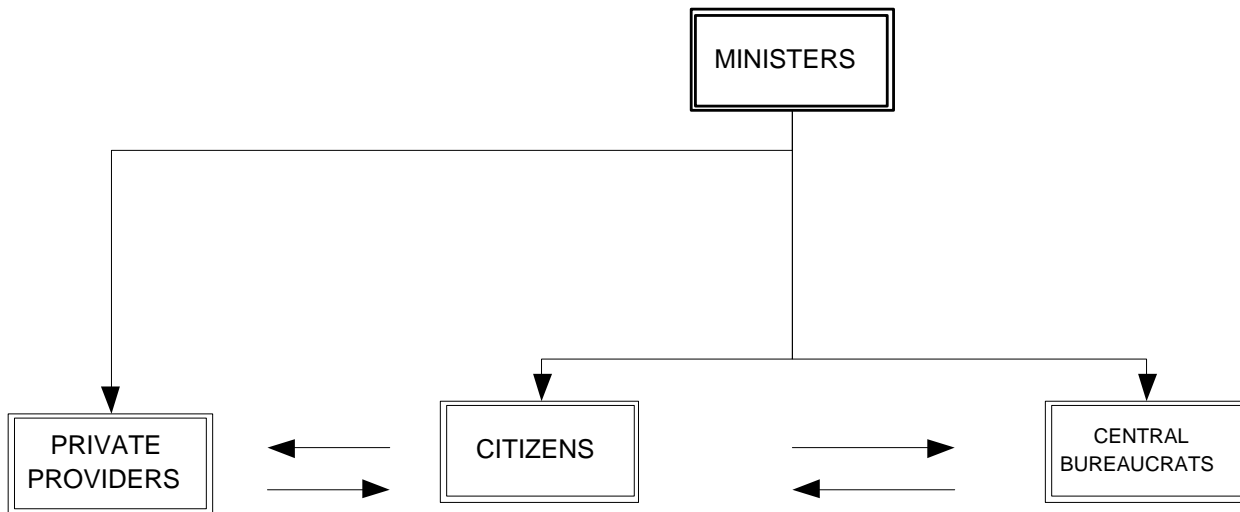


Figure 3: CIVIC DECENTRALIZATION

the traditional character of government, but instead provides citizens with greater exit and voice options. So I will refer to this third category as **civic decentralization** or **citizen empowerment**.

I will subsequently describe reform experiments of all three types: **bureaucracy reform**, **political** and **civic decentralization** that have been tried in various countries, and the evidence available so far concerning their effectiveness.

3 Bureaucratic Reforms

The topic most frequently discussed is the role of civil service wages in fostering bureaucratic corruption, and the scope for salary reform. Romesh Dutt anticipated much of this in his description of problems of judicial and police administration under the British. On the latter, he quoted Frederick Halliday, the first Lieutenant Governor of Bengal:

“The truth is that the subordinate officers of the Police are generally very much underpaid, and being exposed to great temptations, are extremely corrupt...”⁷

and then went on to contrast the scale of responsibilities of Thanadars, clerks and Jamadars with their meagre salaries. Concerning magistrates, he quoted Sir Henry Strachey on the fitness of Indians to serve without the superintendence of Europeans:

“If the Natives are not qualified for these or any other offices, I conceive the fault to be ours, not theirs. If we encourage them, if we pay them well, if we raise them in their own estimation, they will soon be found fit for any official employment in India....*But we place the European beyond the reach of temptation. To the Native, a man whose ancestors perhaps bore high command, we assign some ministerial office, with a poor stipend of twenty or thirty rupees a month. Then we pronounce that the Indians are corrupt, and no race of men but the Company’s European servants are fit to govern them.....*Let the Native Judges be well paid, and they will do their duty well; of this I feel the strongest conviction. The expense would be little or nothing, as the fees might defray the whole, though it would be better to give the Native Judge liberal salaries.”⁸

The view that bureaucratic corruption is rooted in poor pay is the basis of the modern theory of ‘efficiency wages’. The first modern proponents of this theory were Gary Becker and George Stigler, in their discussion of how to discourage corruption among law enforcers when detection of such corruption is uncertain:

“The fundamental answer is to *raise* the salaries of enforcers above what they could get elsewhere, by an amount inversely related to the probability of detection, and directly related to the size of bribes and the cost of malfeasance. A difference in salaries imposes a cost of dismissal equal to the present value

⁷R.C. Dutt, *Economic History of India*, Volume 2: In The Victoria Age, New York: Burt Franklin, 1903, p. 195.

⁸Italics as in original, quoted in R.C. Dutt, *Economic History of India*, Volume 1: Early British Rule, New York: Burt Franklin, 1901, pp. 320 and 316 respectively.

of the difference between the future earnings stream in enforcement and other occupations.”⁹

The logic of this rule is illustrated most simply as follows. Suppose the official will be detected taking a bribe of size b with probability d . In that event the official will be subsequently dismissed from employment with probability f ; with the remaining probability the official is not dismissed but is made to pay back the bribe. Let v denote the income of the official in whichever occupation will select upon dismissal, and w the salary in service. If the official has become completely self-serving, he will decide whether to take the bribe based entirely on a cold logic of personal economic costs and benefits. The expected income gain is $(1 - d)b$, the bribe times the probability of escaping detection. The expected cost is $fd(w - v)$, the probability of being dismissed subsequent to taking the bribe times the pecuniary loss from dismissal. Accordingly the official will be deterred from corruption if the cost $fd(w - v)$ exceeds the gain $(1 - d)b$. For this it must be the case that the official receives a salary in excess of his opportunities elsewhere:

$$w - v \geq \frac{(1 - d)}{df} b \quad (1)$$

While this condition conforms to simple common sense, it has some interesting implications. For instance it qualifies the common belief that raising salaries of government employees invariably solves the problem of bureaucratic corruption. This is true only if there is sufficient likelihood that corruption will be detected, and punished by dismissal. If either d or f is sufficiently close to zero, then condition (1) will always be violated, no matter how high the salary w happens to be. It is not simply a high salary that will deter corruption, but one backed up by a credible threat of monitoring and punishment. The civil service code in many countries makes it very difficult to dismiss public officials under any circumstances. Raising salaries in such contexts will have no effect on corruption of bureaucrats.

Other complications may also arise. The preceding argument assumed that the bribe level b is given. In most situations, however, the official can set the bribe, either unilaterally

⁹G. Becker and G. Stigler, “Law Enforcement, Malfeasance and Compensation of Enforcers,” *Journal of Law and Economics*, III(1), 1974, p. 6.

or following negotiation with bribe givers. A raise in the salary w may then cause the bribe to change. Usually corruption penalties are more severe for bribe takers than bribe givers: then a higher salary raises the expected cost of corruption for the official more than for the bribe giver. This is likely to cause the bribe level to increase. Indeed, corruption may perversely increase following an salary hike which is incremental rather than drastic. For instance if condition (1) is violated before the hike, and continues to be violated after the hike, then the official will continue to be corrupt, and charge a higher bribe. Only if the hike is sufficiently large as to cause (1) to be satisfied will the corruption be eliminated. Following a process of salary increases the effect on corruption may be to make the situation worse before ultimately making it better. And incremental reforms may be worse than no reform at all.¹⁰

Accordingly, the policy of paying efficiency wages to eliminate corruption may require a sufficiently drastic salary hike which may prove too expensive for the government of a poor country. The magnitude of the required hike depends on the institutional context (as represented by the parameters d and f in condition (1)). If monitoring is weak, there is relatively little scope for external pressure from the media and civil society, civil service norms prohibit dismissal, legal institutions do not permit speedy punishment, or the size of bribes is inordinately large, the required efficiency wage might then be too large to be fiscally feasible. Tim Besley and John McLaren have accordingly argued that it may well be optimal for governments in countries with a poor institutional context to tolerate rather than eliminate corruption.¹¹ Moreover, the appropriate efficiency wage will differ between different departments of the government — e.g., the police might need a higher efficiency wage than school teachers — contrary to civil service norms concerning pay equity.

What are the alternatives to paying efficiency wages? One suggestion is to use carrots rather than the stick, i.e., measure the performance of bureaucrats in some fashion, and pay bonuses for good performance. Such proposals are practical when reasonable measures

¹⁰This argument is further elaborated in D. Mookherjee and I. Png, “Corruptible Law Enforcers: How Should They Be Compensated?” *Economic Journal*, 105, 1995, 145-59.

¹¹T. Besley and J. McLaren, “Taxes and Bribery: The Role of Wage Incentives,” *Economic Journal*, 103, 1993, 119-41.

of performance are available, as in the context of tax collection, where they have been implemented in a number of different countries (to be reviewed below). The effects and desirability of these bonus schemes have been extensively discussed in the theoretical literature, which has pointed out that they are also subject to some of the same problems as efficiency wages. To eliminate corruption a sufficiently large bonus may be required, while those of smaller size may simply serve to preserve corruption and raise the bribe rate. Sufficiently large bonuses may be too expensive for the government, and violate norms of pay equity among officials.

We shall shortly describe recent experience with pay reforms in some countries. Before that it is appropriate to mention one additional general point. Even if raises in salaries or bonuses for government officials may fail to eliminate corruption, and have the opposite effect of raising bribes, they may nevertheless succeed on other dimensions. In the tax collection context, paying higher bribes will make tax evasion a more expensive prospect for corrupt taxpayers, and thus enhance compliance among taxpayers. This is accentuated as the prospect of securing higher bribes can spur tax officials to work harder to unearth tax evasion. Consequently the reform may witness a rise in tax collections and tax fines collected by officials. Visible indicators may thus indicate the reforms are successful, while they may happen to increase corruption at the same time. In a sense the reforms would indeed be working, if one views the primary purpose of the tax collection agency as collecting revenues collected and deterring tax evasion. But this may be too narrow a perspective, one which ignores the means employed by tax officials to raise more revenues.

3.1 Reforms in Pay Systems

Following the onset of deep seated fiscal crises during the 1980s, a number of countries in Latin America and Africa embarked on substantive reforms in tax administration. Most of these involved changes in salary and bonus systems for tax collectors. I will discuss the experiences of Brazil, Mexico, Ghana and Peru in turn.

In December 1988 the Brazilian government created a bonus program for tax collectors. A bonus fund called FUNDAP was set up, receiving approximately 68% of all fines

collected from taxpayers for noncompliance with tax laws. These bonuses were allocated between individual and group rewards in a 30:70 split. Group rewards were paid to the local tax agency involved, on the basis of performance relative to other tax agencies in the country. Individual rewards were based on a formula based on evaluations of performance by supervisors, relative to other officials in the same agency. The bonuses payable were capped by the salary of a government minister. The size of these bonuses since have been significant: in 1992 for instance rewards to officials were reported to vary between Cr\$4 million and 8 million per month, whereas the basic salary of a senior tax auditor was Cr\$1.9 million a month. So the size of the rewards have been very large on average, between two and four times the salary levels.

The effects of this reform on fines collected have been evaluated in a recent paper by Charles Kahn, Emilson De Silva and James Ziliak.¹² The share of federal taxes in GDP rose appreciably from 14.8% in 1988 to 17% in 1992. There was a sharp trend break in the rate of fines collected per tax inspection: they rose almost six times between 1989 and 1992. Nevertheless attribution of the causes of this rise is a nontrivial exercise for many reasons. There were many other changes occurring at the same time in the tax laws: marginal tax rates on all categories of taxes dropped significantly, while the tax base was broadened. Tax forms were simplified, withholding procedures adopted and simplified, and special audit programs for large taxpayers instituted. There was a reallocation of audits across different categories of audits, across different categories of taxes, and different regions. Nevertheless, Kahn, Silva and Ziliak use OLS and fixed effect regressions to separate out the role of these allocation effects, and estimate a 75% increase in the growth rate of fines per inspection as a result of the bonus scheme. It is likely that this underestimates the true impact, since the other changes in the tax system occurring at the same time should have enhanced taxpayer compliance. The results cannot be attributed to macroeconomic changes either, since real GDP in Brazil experienced little variation over this period.

Mexico adopted similar bonus reforms for its tax collectors during the period 1989-92.¹³

¹²C. Kahn, E.C.D. Silva and J.P. Ziliak, "Performance-Based Wages in Tax Collection: The Brazilian Tax Collection Reform and its Effects," *Economic Journal*, 111, January 2001, 188-205.

¹³For further details of the Mexico and Peru cases, see A. Das-Gupta and D. Mookherjee, *Incentive and*

Each tax agency was awarded a bonus fund, approximating about 60% of fines collected, which is distributed between individual and group rewards. In the early 1990s they were estimated at about 130% of salary levels. Bonuses received were capped at 250% of salaries. Both the number of audits and files per audit increased sharply overnight. The fraction of taxpayers audited rose from 3.2% in 1988 to 5.5% in 1990 and 8.9% in 1993. Almost 90% of all audits generated additional revenue in 1990, compared with 38% in 1988. The benefit-cost ratio of these audits rose from 4 in 1988, to 27 in 1990, and 46 in 1993. An econometric evaluation of the role of the bonus reform in generating these outcomes has not yet been carried out to the best of my knowledge. These changes were accompanied by a drastic overhaul of the entire Mexican tax administration, so it is difficult to separate out the role of the bonus reforms from other administrative reforms that may have increased the effectiveness of audits.¹⁴

Ghana responded to a deep-seated fiscal crisis in the mid-1980s with a significant reform of its tax administration in 1985.¹⁵ These reforms were motivated to reduce mounting tax evasion and corruption amongst tax officials. By 1983 the ratio of taxes had dropped to 4.5%, compared with 13% in 1973. High rates of inflation combined with fixed nominal wages for civil servants caused their real salaries to drop to one sixth of their former values. The tax administration had become increasingly disorganized, with haphazard storage of taxpayer files, concentration of assessment and collection functions by the same officer, and virtual cessation of properly conducted audits. The economic crisis was partly responsible for the takeover by the Rawlings regime in 1981 on an anti-corruption platform. Following a brief crackdown on corruption, the government followed a more structured approach from 1984 onwards, lowering and rationalizing tax rates, relying more on presumptive taxes and measures to curb the size of the underground economy. In 1985 they reorganized the tax administration in order to rationalize operations, providing greater autonomy over budgets,

Institutional Reform in Tax Enforcement: A Review of Developing Country Experience, New Delhi: Oxford University Press, 1998, Ch.9.

¹⁴However, in interviews Mexican tax officials indicated the reward system to be the single most effective cause of improved audit performance.

¹⁵This account is based on S. Chand and K. Moene, "Controlling Fiscal Corruption," *World Development*, 1999.

salary and monitoring of tax officials. Efforts were made to weed out corrupt tax officers, collection and assessment functions were separated, and facilities set up to receive taxpayer complaints against corrupt officers. A bonus scheme was introduced, which set aside a significant fraction of excess of revenues collected over a target level, which could be used for improvement of departmental facilities. This scheme was retained until 1992, when it was withdrawn owing to lack of backup legislation, and the sense that the fiscal emergency had passed. Together with a policy of civil service retrenchment, the government granted major wage increases to civil servants. Tax revenues recovered to 12% of GDP by 1988, and ultimately reached 17% by 1988. It is difficult, however to separate out the roles of reforms in tax laws from those in tax administration that were taking place at the same time.

Peru instituted drastic tax administration reforms beginning in 1991, based on the efficiency wage strategy rather than payment of bonuses. This followed a fiscal crisis in the late 1980s (whence tax revenues fell from 15.6% of GDP in 1980, to 13.2% in 1985, 8.5% in 1988 and 5.8% in 1989). In 1990 the government reconstituted its tax agency (SUNAT) as a decentralized, formally autonomous public institution, with its own net worth, and with its revenues set at 2% of all taxes administered. The key element of the restructuring strategy was the emphasis on human resources and salaries owing to awareness of growing levels of corruption and incompetence within the organization. The previous two decades had witnessed a significant growth in employment, combined with shrinking salary levels in real terms (by about one half between 1982 and 1987). The new administration used its autonomy to raise salary levels and at the same time reduce the size of the workforce. The average monthly remuneration within the tax agency increased tenfold, from \$65 in September 1991 to \$635 in July 1992. The increase was especially pronounced for managerial and professional cadres (which increased from \$204 to \$1471, and from \$62 to \$871, per month, respectively).

At the same time, the total workforce was cut by one third, and in the capital city Lima by two thirds. Officials were retained on the basis of their performance in a number of tests, and reports of their integrity from the Public Registrar and the Controller of Public Accounts. Since 1991, staff strength has been increasing. However, hiring has become very selective: only 2.7% of those applying in 1991 were selected. New recruits were kept on

probation for nine months, following an initial training period. Promotions were decided by upper level managers. As a result of these policies, the relative size of professionals in tax administration increased from one third to almost one half. Officials known to be most corrupt had been induced to leave the organization. Revenues rose to 9% of GDP in 1991, compared with 5.4% in 1990. However, as in the case of Mexico or Ghana, there is no systematic study of the effects of the wage-employment reforms, in isolation from all the other changes taking place in tax policy, tax administration and the economy as a whole.

More detailed information concerning the efficacy of efficiency wage policies is available from a study by Rafael Di Tella and Ernesto Schargrotsky of a crackdown of corruption in public hospitals in Buenos Aires, Argentina during 1996-97.¹⁶ This crackdown was carried out by a new city government following an electoral campaign focused on the issue of corruption in the previous administration. In September 1996 the new Health Secretary began to monitor prices paid by all public hospitals in procuring basic supplies such as normal saline, ethyl alcohol and hydrogen peroxide, going back to June or August 1996. The initiative lasted till December 1997; after which it was abandoned. What the Health Secretary intended to do with the collected information was not made clear. But there was general anticipation of a crackdown on those procurement officers procuring at above-normal prices.

In their analysis Di Tella and Schargrotsky identify three phases of the initiative: June 1996-August 1996 which preceded the initiative but for which price information was collected; September 1996-May 1997 when the expectations of a crackdown were at their highest; and June 1997-December 1997 when expectations of a crackdown melted following failure of the government to take any concrete action and newspaper reports of its weakening resolve. Di Tella and Schargrotsky show that procurement prices during the middle phase fell 17%, a number consistent with bribe estimates obtained from interviews of Argentine businesspeople. In the third phase they were still 10% below the pre-crackdown level. Having collected data on wages and perceptions of likelihood of dismissal following detection of corruption in different hospitals, they find strong evidence in favor of the Becker-Stigler

¹⁶Rafael di Tella and Ernesto Schargrotsky, "The Role of Wages and Auditing during a Crackdown on Corruption in the City of Buenos Aires," mimeo, Harvard Business School, 2000.

theory. In particular, as condition (1) indicates, there is a strong interactive effect of salary levels and monitoring intensity. Higher salaries cause corruption to decline, and the extent of this decline is greatest when the probability of monitoring is intermediate. They estimate a doubling of wages would cause procurement prices to drop by more than 20%. The highlight of their analysis is careful use of micro-panel data to identify the role of the wage and monitoring intensities, after controlling for possible omitted variables, unobserved heterogeneity across hospitals, or the possibility of reverse causation from corruption levels to wages or monitoring intensity.

3.2 Problems of Relying on Wage and Monitoring Reforms within Bureaucracies

The Argentina study serves to highlight the role of monitoring policies as a complement to raising salaries as a means of curbing bureaucratic corruption. The mere threat of taking action against hospitals procuring at above market prices served to reduce corruption significantly. Had the crackdown been actually effected and sustained, the effects would presumably have been even more drastic. But the fact that it remained a mere threat for less than one year, despite forming part of the mandate of the new government, suggests the difficulty of relying on efficiency wages as a means of combating corruption. As explained above, such policies are effective only if combined with significant efforts to monitor and punish corruption. ‘Crackdowns’ are rarely sustainable by governments, presumably owing to the political and internal opposition they encounter. Even in the context of Communist China, Francis Lui provides an account of the experience with the periodic crackdowns since 1949, that typically lasted one to two years each, and have become less effective in the last two or three decades.¹⁷ One of the reasons given for this is that coalitions of officials including higher level officials acted to protect an official being investigated, by misguiding investigators, and leaking information. Accounts of public administration in India are rife with accounts of the insufficiency of inspectors and auditors, and the inability of higher

¹⁷Francis Lui, “A Dynamic Model of Corruption Deterrence,” *Journal of Public Economics*, 31(2), November 1986, 215-36.

officials to act upon adverse audit reports when they happen to be filed.¹⁸

The difficulty of investigating and establishing the incidence of corruption is compounded by civil service norms and legal difficulties in securing dismissal. The worst consequence for a tarnished official is frequently transfer to a less lucrative assignment, or a temporary suspension for a few months. Transfer policies often tend to be used instead by political superiors to reward or punish compliance with their own personal agendas, rather than merit based performance.¹⁹ These difficulties limit the practical effectiveness of efficiency wage policies.

Bonus schemes present an alternative way of trying to motivate officials. They can however be implemented only in those contexts where objective metrics of superior performance are available. In most areas where the role of the bureaucrat's role is to deliver services to citizens dispersed over a large area, and where information systems are weak, it is very difficult for hierarchical superiors to measure performance. Robert Wade's comparative account of the performance of irrigation bureaucracies in Andhra Pradesh and Korea makes this point quite clear.²⁰ One of the key weaknesses he pinpoints in Andhra Pradesh is that the topography and scale of the areas covered, combined with the weak communication and information systems, made it very difficult for the performance of local irrigation guards to be monitored by their superiors. The system was also designed to minimize the involvement of local residents in the management of the system, so there was no attempt to solicit their

¹⁸See, for instance, Chapter 3 of my book with Arindam Das-Gupta (cited above) which lists and cites numerous government committees that have repeatedly mentioned this in the case of the Indian tax administration. Section 7.4 of the *Public Report on Basic Education in India (PROBE)*, New Delhi: Oxford University Press provides evidence concerning infrequency of inspections, and lack of follow up action in schools in the BIMARU states of Northern India. The Government of West Bengal sponsored report on *The Status of Primary Education in West Bengal*, headed by Raghavendra Chattopadhyay, 1999 also mentions the problems arising from the large number of schools under the ambit of a single school (circle) inspector — 60 or 70, resulting in weaknesses in supervision and monitoring of teachers.

¹⁹For a detailed examination of the process of transfers on Indian bureaucrats, see Dan Banik, "The Transfer Raj: Indian Civil Servants on the Move," mimeo, Centre for Development and Environment, University of Oslo.

²⁰Robert Wade, "How Infrastructure Agencies Motivate Staff: Canal Irrigation in India and the Republic of Korea," in *Infrastructure Strategies in East Asia*, Ashoka Mody (ed.), World Bank, 1997.

perception of water delivery decisions made by the guards. If supervisors sent to check on the guards are themselves corruptible, one cannot expect reliable information concerning performance of lower level employees to percolate upwards to higher levels.

In other contexts similar problems arise. In schools or hospitals, a key problem is that teachers and doctors do not show up for work, and that material supplies such as construction materials, textbooks and medical supplies are diverted to the black market. Tracking such diversions are difficult enough by local residents, and doubly so by hierarchical superiors located hundreds of miles away in the state capital. Even deeper problems arise with respect to defining measures of good performance, conditional on which bonuses can be paid. How does one measure the output of a teacher, or a policeman? As Bengt Holmstrom and Paul Milgrom have argued, designing such performance metrics is tricky even in the context of developed countries, owing to their multidimensional nature, where some dimensions more difficult than others to measure.²¹ Measuring and rewarding the more measurable dimensions may be dysfunctional, since they may cause the official to divert effort towards those dimensions that are measured, at the expense of those that are not. For instance, if teachers are evaluated on the basis of their students' grades, they might then be motivated to redirect their teaching to emphasize examination technique at the expense of real learning; in extreme cases even to leak exam questions to their students.

The multidimensional character of performance afflicts nearly all areas, even that of tax collection. One implication of bonuses may be for tax inspectors to step up extortion and harassment of honest taxpayers, owing to their incentive to cite the latter for fabricated tax offenses.²² Or they may enter into collusive deals with the taxpayers to cite tax offenses that can later be appealed by the taxpayer and expect to be revoked.

²¹B. Holmstrom and P. Milgrom, "Multitask Principal-Agent Analyses: Incentive Contracts, Asset Ownership and Job Design," *Journal of Law, Economics and Organization*, 7, 1990, 24-52. See also J. Tirole, "The Internal Organization of Government," *Oxford Economic Papers*, 1993.

²²For further elaboration of this and related problems associated with incentive design in tax administration, see D. Mookherjee, "Incentive Reforms in Developing Country Bureaucracies: Lessons from Tax Administration," *Annual World Bank Conference on Development Economics 1997*, B. Pleskovic and J. Stiglitz (Ed.), World Bank 1998.

The possibility of artificially inflating short term collection figures at the expense of long term outcomes is a perennial problem in the design of performance incentives for managers in all organizations. It is a problem in private companies just as much as public bureaucracies, when managers are frequently rotated or promoted across different positions, or may leave the organization to join another one. Private companies use stock awards and stock options to align incentives of top level managers with those of shareholders. By their very nature, of course, these cannot be replicated for government department officials. For middle and lower level employees of private organizations, performance incentives are based on profit or cost centers, in which managers are strongly motivated to control departmental costs. In contrast, government departments are not bottom-line driven and consequently rarely organized into profit or cost centers; if anything managers have an incentive to expand the departmental budget as far as possible. In such contexts, the institution of bonus schemes may create incentives for overinflated performance evaluations by managers for their subordinates, in exchange for reciprocal favors, or in order to placate militant employees.

These problems would afflict even those government ministers that might genuinely seek to improve the performance of the bureaucracies they head. If bureaucratic corruption is strongly intertwined with political corruption, the ministers will have a stake in resisting any reform effort, and can design their implementation so that they do not work. As Mary Shirley and Colin Xu have documented for over a dozen countries, attempting to improve the performance of public sector enterprises by creating performance measures and related incentive schemes rarely succeed, owing to lack of political will in designing and implementing these contracts appropriately:

“..the governments negotiating our sample contracts chose to pledge actions that they were not motivated or able to implement. Second, with the exception of India, Korea and Mexico, the supervisory agencies were not given the capacity to negotiate, monitor and evaluate well. Their information advantage was reinforced by other government actions, such as giving them low pay and status, frequently moving them within the government, and failing to force the SOEs to comply with their information requirements. This allowed managers to ma-

nipulate the targets, which proved to be a serious failing of all the contracts in our sample.”²³

The problem is even harder for bureaucracies that lack objective performance measures. The lack of political will at the highest levels is probably the most serious roadblock to serious reforms within public bureaucracies.

If so, what explains the institution of incentive reforms in tax administrations of Brazil, Mexico, Peru or Ghana? In all these cases the reforms were carried out by newly elected governments following deep-seated fiscal crises. A similar sense of ‘crisis’ is less likely in the context of delivery of social services, where the effects of cutbacks in service deliveries are unlikely to be visible or threaten the survival of the government. The lack of political will in such sectors is compounded by the greater difficulty of measuring performance and monitoring corruption. So the same approach is much less likely to work outside the area of tax collection. Besides, little is known about the sustainability or effectiveness of these reforms in the longer term. Neither is anything known about the side effects they may have given rise to, such as corruption, extortion, and harassment of innocent citizens.

I have argued elsewhere that incentive reforms within tax administration require complementary organizational reforms to make them effective, and avoid such undesired side effects.²⁴ These include investments in information systems, enhanced third-party supervisory structures to avoid collusion, restructured tasks to limit the discretion of tax inspectors, reform of budgeting systems, and of legal mechanisms of appeals, penalties and prosecution. Yet of half a dozen countries studied in my book on tax enforcement with Arindam Das-Gupta, only one country, Mexico, can be said to have carried out such a comprehensive reform. The unique character of the state in Mexico, and the lack of an institutionalized civil service, was instrumental in this respect. If this happens to be the experience in the

²³Mary Shirley and Colin Xu, “Information, Incentives and Commitment: An Empirical Analysis of Contracts Between Government and State Enterprises,” *Journal of Law, Economics and Organization*, 14(2), 1998, p. 376. See also Shirley and Xu, “Empirical Effects of Performance Contracts: Evidence from China,” Working Paper, Development Research Group, World Bank, 1998.

²⁴See my article in the 1997 Annual World Bank Conference in Development Economics, already cited above.

area of tax collection, where incentive reforms are the most feasible, and where governments have the greatest incentive to reform, there is little hope indeed that such approaches can be relied on in the context of social services or infrastructure delivery.

4 Political Decentralization

The problems of enhancing accountability via internal reforms of bureaucracies urge the need to try other approaches. Robert Wade's evaluation of comparative strength of the Korean irrigation system *vis-a-vis* the Indian one is instructive. The main distinguishing feature of the Korean system is that management of the canals is handed over to local communities, after the government irrigation department had constructed the canals. The allocation of water within the community and maintenance operations were the responsibility of patrolmen appointed by the community of users themselves. Combined with easier topography, a smaller scale of supervision and enhanced communication systems, the Korean system was more accountable to users than the one in Andhra Pradesh. Delivery patterns and maintenance were monitored by users; a patrolman diverting water in exchange for bribes would be easier to detect and dismiss in the Korean system. Such penalties would be accentuated by social sanctions within the community, since the patrolman was a local resident. Such local information could not percolate upwards to the supervisors of guards appointed by a central bureaucracy in Andhra Pradesh, located hundreds of miles away. Moreover, the supervisors in the Andhra system had no positive incentive to monitor and punish corrupt behavior by guards when such reports from local users did emerge. If anything, the cascading bribe system meant they had every incentive to camouflage and protect local corruption by their subordinates. By contrast, disaffected users in Korea would have a strong incentive to fire and punish a corrupt patrolman, since they would themselves be bearing the cost of such corruption. Such an accountability mechanism was augmented in Korea by designing contests among local irrigation managers of neighboring communities.

Besides enhancing accountability of service providers, devolution of power to manage the delivery system of public services has other advantages as well.²⁵ Local users are typically

²⁵These advantages have also been stressed in the context of proposed reforms in water management

better informed about the need for maintenance of local facilities, and the nature of repairs required. They have a maximum incentive in ensuring that these repairs are carried out speedily, and can organize it themselves if suitable finances are available. In Korea, these were funded by local user charges. Collection of charges was not a serious problem (relative to tax collection) as the rest of the community benefitted directly from their collection, and users were motivated to contribute to a service that tangibly benefits themselves. User interests also motivate them to monitor use of the charges collected by local officials for the purpose they were intended. In Andhra Pradesh by contrast, the local irrigation officials had little incentive in the upkeep of facilities. Even in the rare instance when problems were reported to higher level officials, long periods would elapse before these officials could come to inspect the facilities, and even longer for them to authorize and execute the repairs. Besides these practical advantages of superior accountability and local information, popular participation in management has the wider political advantage of offering citizens a greater sense of empowerment, lowering their sense of alienation and frustration with the system of government.

The overcentralized structure of government in India is of course rooted historically in the nature of British colonial administration. Romesh Dutt rued the inability of the British colonial government to devolve power to local communities:

“It is somewhat remarkable that no British administrator of this period seriously endeavoured to improve the police and general administration of the country by accepting the cooperation of the people themselves and their Village Communities”. (Dutt (1903, p. 196))

And echoing the view to be later enunciated at length by Radhakumud Mookerji²⁶ he went on to say:

“India had been the earliest home of Village Communities, and for centuries and thousands of years these self-governing Communities had maintained order

systems in India by A. Vaidyanathan, *Water Resource Management: Institutions and Irrigation Development in India*, New Delhi: Oxford University Press, 1999, especially Chapter 3.

²⁶ *Local Government in Ancient India*, 1920, reprinted 1989, New Delhi: Low Price Publications.

and peace, and settled disputes in villages, even when there was anarchy in the realm.....And in Northern India, Sir Charles Metcalfe had stated in 1830 that “the Village Communities are little republics having nearly everything they want within themselves. They seem to last where nothing else lasts. Dynasty after dynasty tumbles down, revolution succeeds to revolution, Hindu, Pathan, Moghal, Mahratta, Sikh, English, are masters in turn, but the Village Communities remain the same...The union of the Village Communities, each one forming a separated little State in itself, has, I conceive contributed more than any other cause to the preservation of the people of India through all revolutions and changes which they have suffered, and it is in a high degree conducive to their happiness, and to the enjoyment of a great portion of freedom and independence.” ... It is a lamentable fact that these ancient and self-governing institutions have declined, and virtually disappeared, under the too centralised administration of British rule...No system of successful self-government has been introduced after the old forms were effaced; no representatives of the village population help the administration of the present day; and an alien Government lacks that popular basis, that touch with the people, which Hindu and Mahomedan Governments wisely maintained through centuries. ” (Dutt (1903, pp. 196-197))

Yet, this enthusiasm about the vitalization of local village communities has not been universally shared. The design of the Indian Constitution in the late 1940s consciously avoided creating a system of local government. Babasaheb Ambedkar, among the chief architects of the Constitution, justified this in a speech to the Constituent Assembly in November 1948:

“The love of the intellectual Indian for the village community is of course infinite, if not pathetic. It is largely due to the fulsome praise bestowed upon it by Metcalfe who described them as little republics having nearly everything that they want within themselves, and almost independent of any foreign relations...That they have survived through all vicissitudes may be a fact. But mere survival has no value. The question is on what plane they have survived. Surely

on a low, on a selfish level. I hold that these village republics have been the ruination of India. I am therefore surprised that those who condemn provincialism and communalism should come forward as champions of the village. What is the village but a sink of localism, a den of ignorance, narrow-mindedness and communalism?"²⁷

Nevertheless more recently there has been considerable progress towards devolution of power to elected local governments, in India as well as many other developing countries. In India the Balwantrai Mehta report in 1957 suggested a three tier structure of local government, which was left to individual state governments to implement at their will. Only a few state governments actually did, such as Karnataka and Maharashtra for brief periods in the 1960s and 1970s, and West Bengal since 1978. The 73rd and 74th amendments to the Indian Constitution adopted in the early 1990s extended this mandatorily to the entire country, while leaving details of implementation to individual states. Elsewhere in the world a similar wave of decentralization of service delivery to local governments has gathered momentum in the 1990s in many countries, including Albania, Bolivia, Bosnia, Brazil, Ethiopia, Malawi, Madagascar, Philippines, South Africa, Uzbekistan, Uganda, and Zambia.²⁸ I will describe some of these experiences in more detail shortly below.

Ambedkar's concern about the negative consequences of decentralization have been highlighted by many academics and commentators on this movement. Many traditional communities are characterized by a lop-sided allocation of social, economic and political power. It is possible therefore that devolution of power to local communities will be captured by local elites, who will divert them to benefit themselves at the expense of minorities and the poor. Local governments may be less accountable than bureaucrats appointed by the central government, in which case there may be no net increase in the accountability of the delivery program. It is the very concern with the potential for such local capture that

²⁷As quoted in Mathew and Nayak, "Panchayats at Work," *Economic and Political Weekly*, July 6 1996, p. 1765.

²⁸For a broader account of these initiatives, see J. Conning and M. Kevane, "Community Based Targeting Mechanisms for Social Safety Nets," mimeo, Williams College, 1999 and World Bank, *Entering the 21st Century*, Chapter 7, Decentralization: Rethinking Government, 2000, Oxford University Press.

had led designers of the US Constitution also to argue for retention of powers with the federal government. More than two centuries back, in the Federalist Papers (no. 10), James Madison justified federal powers on the basis of greater proneness of local governments to capture by elites and special interests:

”The smaller the society, the fewer probably will be the distinct parties and interests composing it; the fewer the distinct parties and interests, the more frequently will a majority be found of the same party; and the smaller the number of individuals composing a majority, and the smaller the compass within which they are placed, the more easily will they concert and execute their plans of oppression. Extend the sphere and you take in a greater variety of parties and interests; you make it less probable that a majority of the whole will have a common motive to invade the rights of other citizens; or if such a common motive exists, it will be more difficult for all who feel it to discover their own strength and to act in unison with each other”.

Similar views concerning the need for federal powers have been expressed more recently in the United States in the wake of the Civil Rights movement of the 1960s.²⁹

Decentralization is thus characterized by a number of potential advantages, of better local information that may be brought to bear on selection and targeting of government service programs, and the reduction of authority of central bureaucrats that do not face pressures of accountability. Offsetting this is the potential for capture of local governments by local elites, which can worsen targeting of benefits within communities.

Other disadvantages of decentralization have been emphasized by the traditional literature on fiscal federalism.³⁰ The most important of these are spillover effects of decisions across communities, which would be ignored by each individual community in a decentralized system, but could be internalized by a central government. This is pertinent to

²⁹See, for instance, Grant McConnell, *Private Power and American Democracy*, Vintage Books, 1966, p.348.

³⁰For a summary of this literature, see R. Inman and D. Rubinfeld, “Rethinking Federalism,” *Journal of Economic Perspectives*, 11(4), 1997, 43-64.

investment in highway transport and communication, eradication of communicable diseases, control of pollution and waste disposal. It is less relevant to decisions with a purely local impact, such as elementary education, water and sanitation, local roads, or selection of local beneficiaries of redistributive programs. In the context of the former category of investments subject to significant spillovers, some coordination and control would need to be exercised by central authorities, via tax-subsidy formulae and appropriate regulations.

Another potential disadvantage of decentralization stems from lack of ability to exploit economies of scale. While this factor is clearly relevant in the context of construction of overhead facilities, it is less important in local management. Recall that the Korean irrigation system was based on separation of construction and maintenance, with the former remaining within the ambit of responsibility of central authorities, while the latter was devolved to local communities. Similarly in the context of schools and health facilities, day to day management, procurement of raw material supplies, and oversight of teachers and doctors can be devolved in large degree to local communities, while responsibility for school building construction or curriculum development can remain with central authorities. Moreover, the presence of economies of scale necessitate centralization of production, but not of distribution. In the context of electricity, for instance, decentralization does not mean that every local community should generate its own power. The economies of scale principally arise in generation, rather than transmission or distribution. Power generation can be centralized in either public or private sectors, while procurement can be decentralized to local governments.

Given the existence of these numerous costs and benefits, decentralization cannot be expected to be a universal panacea for curing the ills of an over-centralized delivery system. In the case of significant intercommunity spillovers or economies of scale, mixed centralized-decentralized systems need to be considered. It is principally the aspect of day-to-day management, and expression of local investment priorities that can be devolved to local communities, where accountability problems are the most acute. In this respect the main potential advantage of decentralization is richer local information and accountability pressures. The main disadvantage is the potential for capture of local governments by local elites. The trade-off between these contrasting effects need to be assessed to evaluate the

extent to which decentralization enhances accountability.

In ongoing work with Pranab Bardhan, I have analytically explored some of the implications of this trade-off.³¹ Decentralization can generally be expected to enhance cost-effectiveness, since the scope for local users to gain from cost-padding or diversions is less than for a less accountable ‘outsider’ such as an employee of the central government. Hence the overall volume of services can be expected to increase, even if expenditure allotments from the center remain unchanged. Service volumes are likely to increase even further for services desired by local citizens in an extensive decentralization accompanied by fiscal devolution, as they would tend to agree to adjust local taxes and fees to fund larger contributions for services that are urgently needed. These may be accompanied by cutbacks in other areas that are less valued, resulting in a closer match of spending allocations to commonly shared local preferences.

Contrasted to these advantages are a number of potential disadvantages. A decentralization may be accompanied by a worsening of intra-community targeting in the presence of substantial local capture. Development programs can be diverted to benefit local elites, so poor households might end up worse off compared to centralization. With sufficient local capture, a decentralization may diminish (utilitarian measures of) welfare even while it happens to increase aggregate service volumes, enhance cost-effectiveness and eliminate overt bribes. Therefore service volumes, cost, or bribery-based corruption measures are insufficient criteria to evaluate decentralization experiments; they need to be supplemented with measures of the allocation of benefits within local communities.

The extent of local capture also impacts on desired patterns of fiscal devolution. If local governments become fiscally self-sufficient with sufficient internal revenue raising capacity, there is the risk that they resort to regressive financing patterns whereby non-elites are taxed to bear the burden of providing services to local elites. Restrictions on the ability of local governments to levy local taxes may then be desirable, even at the cost of reducing

³¹P. Bardhan and D. Mookherjee, “Relative Capture of Government at Local and National Levels,” *American Economic Review*, 90(2), 135-139; “Corruption and Decentralization of Infrastructure Delivery in Developing Countries,” and “Decentralizing Anti-Poverty Program Delivery in Developing Countries,” both 2000 working papers, Institute for Economic Development, Boston University.

flexibility of service provision to local need. In this connection user charges represent a useful compromise between the need for matching provision to local needs, and avoiding an unduly heavy fiscal burden on the local poor. Since no category of users can be compelled to use the service, this imposes a limit on the extent that small users can be expropriated to pay for service allocations to local elites. So when the service can be funded by user charges, there is no risk that small users be made worse off by decentralization, no matter how much local governments are vulnerable to capture. In the context of infrastructure services such as irrigation or electricity, the danger of local capture is therefore not that important so long as such services are funded by user fees.

User charges cannot however be used to finance anti-poverty programs, since by their very nature these programs are targeted at groups that do not have the ability to pay for the service. Examples include distribution of food, housing, schooling and health care to those below the poverty line. In such contexts, the extent of capture of local governments *vis-a-vis* the central government is a critical determinant of the welfare impact of decentralization. If local governments are equally or less vulnerable to capture than the central government, then decentralization is likely to improve both efficiency and equity. But the opposite may be the case when capture at the local level is much greater than at the central level.

There is however very little empirical evidence concerning the extent of relative capture of governments at different levels. Nor is there any theoretical reason to predispose ourselves to any particular pattern. Capture is an outcome of the political process by which governments are elected at central and local levels, the nature of the policy making process, and the ways these operate to advantage certain groups at the expense of others. The nature of social and economic inequality, and patterns of political participation by different social groups are clearly important determinants. Some of these factors provide support to the Madisonian presumption in favor of greater capture at the local level, such as greater cohesiveness of interest groups, and lower media coverage at the local level. Others may make for less local than central capture — greater power of campaign funds in national elections, scope for coalition politics in national legislatures, keener electoral competition at the local level, and better information concerning candidates in local elections based on informal sources. The contrasting roles of these diverse factors suggest that the extent of

relative capture at the local level is likely to be context- and system-specific. As explained above, assessing this is a key step in evaluating the success of decentralization initiatives. With few exceptions existing empirical studies on decentralization have only focused on effects on the volume of services delivered within communities. Largely owing to lack of suitable micro-level data, they have abstracted from the effect of decentralization on service allocations *within* communities.

4.1 Specific Country Experiences

Participatory Budgeting in Brazil³²

The *Partido dos Trabalhadores* (Workers Party, henceforth PT) was founded in Brazil in the 1980s out of the labour movement which had been instrumental in the earlier struggle against military dictatorship. It won a number of local elections in several important cities, such as Sao Paulo, Porto Alegre, Santos, Belo Horizonte, Campinas, Vitoria etc, and introduced in all of them reforms in municipal governments that encouraged direct political participation by local citizens. Of these, the reforms have been most successful in Porto Alegre, and have been sought to be emulated elsewhere in Brazil and other countries. The success of this reform greatly bolstered the political reputation of the PT, causing their vote share to rise from 32 % in 1988 to 48% in 1992 and 56% in 1996. Approval ratings of the government in 1996 indicated an 85% approval in 1996.

The main aspect of the reforms in Porto Alegre concerned the process of ‘participative budgeting’. The city was divided into 16 regions. A number of different ‘thematic’ areas: transportation, education, health, economic development and taxation, city organization and urban development were identified. The budgeting process starts with a number of different rounds of popular assemblies within each region which are attended by local residents and neighborhood associations. These assembly meetings discuss investment priorities across thematic areas and across sub-regions, review accounts, evaluate past investments, and elect representatives to a city-wide council called COP (Participative Budgeting Coun-

³²This account is based on Boaventura De Sousa Santos, “Participatory Budgeting in Porto Alegre: Towards a Redistributive Democracy,” *Politics and Society*, 26(4), 1998.

cil).

The priorities expressed by each regional assembly is passed on to the COP council. Their elected representatives to the COP, along with representatives of the Mayor and other departments, review progress with collection of revenues. The COP then allocates available resources across regions based on the priorities submitted by each region from the earlier assemblies, and a transparent formula based system. The formula assigns weights to different regions based on their population, existing access to infrastructure and services, and fraction of residents in extreme need. Regions in greater need by these criteria are given a higher weight, so poorer regions get preference over wealthier ones.

Participation rates in the assemblies have been high on average — the office of the mayor estimated in 1996 that if the hundreds of intermediate meetings were taken into account, total participation amounted to one hundred thousand, or 8% of the city's population. It is not known, however, the extent to which this is subject to double counting of the same individuals attending multiple assembly meetings. Moreover, the participation was skewed against lower income and less educated groups: approximately 40% were estimated to have household income between 1 to 3 times the minimum wage and had elementary education, and 60% had an income upto 5 times the minimum wage. Participation of women was not high, ranging between 15 and 20%. Not surprisingly, participation rates were skewed in favor of the self-employed, retired and at-home workers.

The results of this budgeting process in Porto Alegre have been impressive in terms of some indicators of service delivery levels. The proportion of city population with access to basic sanitation (water and sewage) nearly doubled, from 49% in 1989 to 98% for water and 85% for sewage in 1996. In seven years almost universal access was therefore secured, as against half the population previously. The number of students enrolled in elementary or secondary schools also doubled during this period. One half of the street pavement deficit was eliminated during this period. Many slums were urbanized. All of this was rendered possible by a 48% increase in local revenue collection.

A careful appraisal of the role of these budgeting reforms requires the difficult task of isolating their impact from other changes that may have been occurring at the same time,

such as changes in overall fiscal spending levels, or in income distribution. The principal impact of the reforms seems to have been to alter the pattern of resource allocation across regions, increase the volume of services to many poor regions, and limit the extent to which resources were diverted relative to historical standards or those prevailing elsewhere in the country.³³ But not much information is available concerning the intra-regional allocation of these resources across different classes of residents, making it difficult to assess the extent of local capture. Service allocations within each region were for most part based on political negotiation or direct decisions of elected delegates, rather than a transparent formula-based system of the kind used in allocating budget resources across regions. Data concerning service deliveries in different micro-regions, or to households in different socio-economic classes do not appear to have been used in any assessment so far. It must be said, however, that it is quite likely that the targeting success of these programs increased overall, since wealthy people are likely to have had access to basic water, sanitation, paved roads and education prior to 1989, implying that the expansion in access must have primarily benefited the poor. As long as the taxes that financed the service extensions were not regressive, the program is therefore very likely to have been pro-poor.

Bolivia³⁴

Bolivia entered the 1990's with a Presidential-style democracy determined to reverse the experience of forty years of alternating military-civil rule with a centralized state-led system. A major decentralization initiative was announced in 1994 consisting of four major reforms: (1) 198 new municipalities were created, almost twice the number previously existing, and the latter were expanded to include suburbs and neighboring rural areas; (2) the share of national tax revenues devolved from the central government to the municipalities was raised from 10 to 20 %; (3) administrative authority, investment responsibility and title to all local

³³For instance, the Parliamentary Commission for Investigation set up in Brazil following the 'budget mafia' scandal estimated that 64% of social expenditures in the 1993 Union Budget were 'irregularly' allocated to ghost entities.

³⁴This section is based on Jean-Paul Faguet, "Does Decentralization Increase Government Responsiveness to Local Needs? Decentralization and Public Investment in Bolivia," Working Paper no 999, Centre for Economic Performance, London School of Economics, March 2001.

health, education, road and irrigation infrastructure was devolved to the municipalities; and (4) oversight committees consisting of representatives of local grassroots organizations were established to oversee municipal spending and propose new projects.

As in the case of Porto Alegre, effects on the allocation of resources across regions, and across sectors, have been dramatic. Before the decentralization the nine state or departmental capitals received 93% of all funds devolved from the center, leaving 7% for the other 302 municipalities. After decentralization these shares stood at 38% and 62% respectively. This resulted in a massive shift of resources in favor of the smaller and poorer municipalities. In the three years prior to the decentralization one half of all municipalities received no public investment at all, and these were for most part the poorest municipalities in the country.

Changes in the allocation of spending from production to the social sector were equally dramatic, . Between 1991-3, 73% of all public investment in Bolivia was accounted for by transport, hydrocarbons, energy and 'multisectoral' (a hodge-podge of many different sectors difficult to categorize). After the decentralization education, urban development, water and sanitation constituted 79% of all municipal investment. In an econometric analysis, Faguet (2001) finds that these were mostly accounted for by investment patterns in the poorest municipalities that previously received negligible resources. Public investment in education, water and sanitation rose significantly in three quarters of all municipalities, urban development and water management in one third, and agriculture and health in one fifths of all municipalities. Moreover, the investments responded to measures of local need. For instance the expansion in education spending was greater on average in municipalities with a lower literacy rate, with fewer private schools. Investment in water and sanitation rose more in municipalities where fewer people had sewerage previously. Agriculture investments rose more in regions with greater malnutrition. Only in the context of water management and urban development did the opposite pattern emerge: regions with more facilities expanded more subsequent to decentralization.

Faguet's analysis does not examine allocations within municipalities. Nor does it measure outcomes, for instance effects on school enrollment rates, school performance, or access rates to water and sanitation services. Only data concerning spending levels was incorpo-

rated in his analysis. So relative cost-effectiveness or the extent of local capture cannot be assessed. Household level data on access to basic services would be required for this purpose. Alternative interpretations of the pattern of changed investment allocation may also stress the role of inter-regional spillovers and loss of scale economies that may have accounted for the declining significance of investments in transport, communication and industry sectors. So a more complete assessment of the impact of the decentralization is required.

Philippines³⁵

Decentralization in the Philippines was mandated by the new democratic constitution of 1987. A Local Government Code was enacted in 1991 and implemented in 1992-93. This code mandated regular elections to local governments, devolved finances and responsibility for delivery of most basic services. For instance, municipalities were assigned responsibility for primary health care, disease control, purchase of medical supplies and equipment, municipal health clinics and school buildings. Below the 1500-odd municipalities, there are over 40,000 *barangays*, the primary implementing units of this process. Above the municipalities are 77 provinces and 69 cities. 40% of central government revenues collected three years back are transferred to sub-national governments through the Internal Revenue Allotment (IRA). Provinces and cities received 23% of this, municipalities received 34% and *barangays* 20%. It is allocated across regions according to a formula: 50% by population, 25% by land area and the rest equally. Besides this there are two autonomous regions for Muslims, which replicate most central government functions at the regional level.

No study is available on the impact on service delivery outcomes, for instance by contrasting these before and after the decentralization, as in the case of Porto Alegre and Bolivia. In a citizen survey in June 1999, 58% of respondents said health outcomes had improved with decentralization, 34% saying it had remained the same, and 8% saying it had worsened. There was a commonly expressed view that corruption in medicine procure-

³⁵The discussion of this and the Ugandan experience subsequently relies on O. Azfar, S. Kahkonen and P. Meagher, "Conditions for Effective Decentralized Governance: A Synthesis of Research Findings," Working Paper, IRIS Center, University of Maryland, December 2000.

ment had dropped significantly following decentralization. On the other hand, the most notable improvements in public health (immunizations, malaria, TB, child health etc.) in the Philippines had been achieved in the 1980s; these deteriorated in the 1990s. Medical experts have voiced concerns about loss of scale economies and expertise, decline in technical training and quality, and a drop in local demand for immunizations and infectious disease control. However, many of these functions remained primarily under the aegis of the central government so no clear picture emerges concerning the impact of the decentralization *per se*.

Omar Azfar *et al.* (2000) instead adopt an indirect approach: they examine a variety of factors that might be important in determining the effect of decentralization. They survey households and government officials at municipal and provincial levels with respect to stated public investment priorities in the local area. Stated priorities of officials at the municipal level turned out to weakly match those of residents, while officials at the provincial level did not. This provides some evidence in favor of the view that decentralization improved the quality of information used in decisions concerning public investment. Across sectors, the match between municipal officials and citizens was significantly positive with regard to roads, bridges and canals, zero for education, and significantly negative with respect to health.

Azfar and his associates study household and municipal government officials' reports on corruption. They find these responses to be significantly positively correlated with one another, thus lending credibility to the reliability of the corruption estimates. One third of households thought corruption was very common. A greater percentage of households and officials reported corruption in the central government compared to local government. Levels of corruption at the municipal level in turn explained local health outcomes, such as immunizations and incidence of measles, after controlling for a host of local socio-economic, education, media and medical supply variables. This suggests that decentralization may reduce corruption and thereby improve health outcomes, consistent with the majority household perception (reported above) that health outcomes had improved following decentralization.

Evidence concerning relative capture is more elusive. Azfar *et al.* (2000) voice caution

concerning the prospect of capture of local governments, but are not able to find any firm evidence concerning its extent and impact on intra-community allocations. Election turnouts in both local and national elections were high and of similar magnitude: 80 and 86% respectively. Character issues remained the most important in both elections (35 and 25% respectively). Citizens relied on media (TV mainly, used by two-thirds of the population) for the bulk of their news concerning national elections, and to a somewhat lesser extent (33% radio and 22% TV) for news concerning local elections. Likewise, they relied more on the media for news concerning national corruption compared with local corruption, where informal sources of information such as family and social networks were more important. Without knowing the relative quality of the two sources of information, however, it is not clear what this implies about the extent of relative capture.

Uganda

The 1995 Constitution of Uganda provided a general framework for decentralization, which was spelt out in greater detail in the 1997 Local Government Act, which defined five levels of government. Of these the most important are 45 districts and 800 sub-counties. Districts were assigned jurisdiction over primary and secondary education, primary health, water provision, roads, planning and licensing. Some of the primary education and health functions were devolved to lower levels. The sub-county level acts as the primary local tax collector, based on head and property taxes, licenses and fees. They remit between a third to a half of collected revenues up to the Districts, and smaller shares to lower levels. District governments are required in turn to allocate one third of their revenues to lower levels according to a formula based on child mortality, number of school age children, population and area. These are supplemented by central government grants.

The implementation of these initiatives have been flawed in the health sector. Many important decisions reportedly continue to be under central control, such as salaries and staffing, drug procurement and allocation, and hospital funding. Levels of corruption in the health sector appear to be traditionally high, though there are reports of recent improvements. A survey of 12 health units in two districts found evidence of large levels of leakage – ranging between 40 and 94% — of public supply of drugs, diverted by health

workers to illegal private sales.³⁶ User fee guidelines were not followed, with health workers charging higher fees to patients and pocketing the difference. Salary levels were low, causing poor quality workers to be employed, encouraging high levels of corruption and turnover. Some attempts have been initiated recently to curb these problems, with public posting of user fees, receipt of citizen complaints against overcharging by local health committees, and inspecting supply inventories in clinics. But there is little direct evidence concerning the effect of decentralization on health outcomes. Likewise, no evidence is available concerning the effect of the fiscal decentralization on education outcomes. In the next section, however, we shall report on the role of informal forms of decentralization of schools through greater involvement of parent teacher associations.

Similar to their Philippines study, Azfar *et. al.* (2000) assess some of the factors that are likely to influence the impact of decentralization, and obtain qualitatively similar conclusions. Investment priority responses of government officials at lower levels matched citizen preferences better than at the higher (district) level. Reported levels of corruption in Uganda are almost twice as high compared to the Philippines. But unlike the Philippines, there is little consistency across household and official reports of corruption. They also find a greater reliance on community leaders for news concerning local corruption and local elections, which they interpret as evidence of greater potential for local capture in Uganda. Overall, however, there is little empirical evidence concerning the effects of the decentralization on outcomes at the level of households in different socio-economic categories, just as in the case of the Philippines.

Food-For-Education Program in Bangladesh³⁷

The only available detailed study of targeting performance of a decentralized program using household level information pertains to a decentralized food-for-education (FFE) program in Bangladesh, carried out by Emanuella Galasso and Martin Ravallion. The program

³⁶See D. Asimwe *et al.*, "Informal Health Markets and Formal Health Financing Policy in Uganda," in S. Bennett, B. McPake and A. Mills (Ed.), *Private Health Providers in Developing Countries: Serving the Public Interest?*, Zed Books, London, 1997.

³⁷This discussion draws on E. Galasso and M. Ravallion, "Decentralized Targeting of an Anti-Poverty Program," Working Paper, Development Research Group, World Bank, 2001.

sought to encourage school enrollment of poor rural families, by providing food rations to selected households conditional on a class attendance rate of at least 85%. Over two million children participated in this program in 1995, amounting to 13% of all children enrolled. The central government first selected 1200 Union Parishads (UPs), out of 4500 rural UPs in the country. The UPs are the next level below the Thanas, of which there are 490. All thanas were represented. Participating UPs were selected in consultation with the Thana Education Committee, and a minister in charge of coordinating development activities in that part of the country. At the second stage of the program, FFE households were identified within selected UPs. Widows, day-labourers, low income professionals (weavers, fishermen, potters etc.), landless or near landless farmers, and households with school-aged children not covered by other targeted programs were officially eligible to participate. The actual selection was made by the local School Management Committee composed of parents, teachers, education specialists and school donors. Each participating household was entitled to receive 15Kg grain per month for a single child enrolled in school, and 20Kg for more than one child enrolled.

Galasso and Ravallion use data from a 1995-96 Household Expenditure Survey to assess the targeting achieved by this program. Their sample includes over 3,000 households from approximately 200 *mauzas* or villages, one fourth of which participated in the program. Their principal result is that the program was mildly pro-poor: a larger fraction of the poor (12%) received benefits from the program than the nonpoor (8%). This is accounted almost entirely by targeting *within* participating communities, rather than across communities. In this sense the study indicates the potential for decentralized programs to be more effective than centralized programs in alleviating rural poverty.

Yet they do find some evidence of local capture. Within the set of participating villages, targeting success deteriorated in communities with higher land inequality and a larger fraction of households headed by widows. In the absence of local capture, the program should have achieved superior targeting in such villages. The targeting success of the program varied considerably across participating villages: more unequal villages targeted more poorly, tending to perpetuate their inequality. A larger fraction of non-poor compared to poor households received benefits from the program in one quarter of the participating

villages.

Despite this, the level of targeting within communities was superior to that achieved across communities by central allocations. The motivation of including a large range of communities irrespective of eligibility is a common characteristic of many central development schemes, motivated by the need to muster political support for these programs, in what is commonly referred to as the ‘paradox of targeting’. Formula bound (rather than discretionary) transfers may have improved the equity of the allocation across regions, as also suggested by the experience of some other countries to be reviewed in the next Section.

5 Civic Decentralization

We now turn to the third alternative for enhancing the quality of government delivery of social services, based on empowering citizens directly. They can be provided more information, a greater range of service options, or the opportunity to get involved in managing public institutions. Or they can be provided money or vouchers to procure the required services from the market, with these transfers allocated on the basis of census information rather than discretionary authority of bureaucrats. These options also represent a form of decentralization, since they reduce the authority and monopoly power of government bureaucrats acting as intermediaries in the service delivery process. But they differ from the most common version of decentralization that relies on a restructuring of political institutions in the form of devolution to local governments. In these variants, ultimate service recipients are empowered with the right to information, the right to participate in the management of public institutions, and a range of service options within and outside the public system. Involvement of NGOs and grassroots organizations in these activities — helping citizens question and challenge bureaucrats, or set up and manage schools or clinics — also belongs to this category. So do partnerships between the public and private sectors that seek to harness the role of the latter in relieving supply constraints in the public sector, and exert competitive pressures on it. A large number of countries have begun experimenting with different variants of this approach in the last ten or fifteen years. I will now review a number of such experiments, most of which pertain to elementary education.

5.1 Access to Information

A World Bank study by Ritva Reinikka and Jakob Svensson for Uganda set out to monitor the leakage in the flow of educational funds from the central government to schools for the period 1991-95.³⁸ The Ugandan central government ministries transfers funds to district governments for paying teacher salaries, and a capitation grant per enrolled student for non-wage expenditures such as textbooks, instructional materials, and other costs of operating schools. Accounts at the district level were sufficiently murky to prohibit any effort at tracking inflows and outflows of these funds at that level. In contrast, the financial accounts of schools were comprehensive. The study compared the outflow of funds from the central government with the monies actually received by the schools. While the bulk of the central funds for teacher salaries did reach the schools, it turned out that only 13% of the capitation grants for non-wage expenditures were passed on by the District governments to the schools. The remaining 87% could not be traced. Either it was diverted to other categories of expenditures, or pocketed by District officials. Even more surprising is that a majority of schools received no money at all for non-wage expenditures.

The difference between the leakage rate for teacher salaries and capitation grants is explained by Reinikka and Svensson in terms of the corresponding information gaps for recipients. The Ugandan government had implemented a new budgeting system in 1992 which changed the flow of funds into expenditure categories. As part of the World Bank's structural adjustment program, non-wage recurrent expenditures were given priority program status which protected schools from within-year budget cuts. This policy was not well known to citizens, particularly outside Kampala, the capital city. Little information was available to the general public on the spending items protected within the new budgeting system. The district governments could take advantage of the limited information of schools and the general public, knowing that reducing grant disbursements to schools would not invite political attention. In contrast, failure to pay teachers salaries attracted much more attention, since teachers knew what their salaries were. This view is supported by Reinikka

³⁸R. Reinikka and J. Svensson, "Explaining Leakage of Public Funds," Working Paper, Development Research Group, World Ban, October 2001.

and Svensson's econometric analysis, which showed the leakage rates to be lower in schools that were bigger, had more qualified teachers, and higher income of the parent-teacher association. Protesting low payments of the grant would presumably be cheaper for such schools where parents and teachers are wealthier and better connected.

Following the release in 1995 of the preliminary findings of this study, the Ugandan government began to publish monthly transfers of public funds to districts in newspapers and broadcast them on the radio. It also required primary schools to post notices on all inflows of funds. An initial assessment of this disclosure policy made by the Ugandan government reported that the fraction of funds reaching the schools increased from 20% in 1995 — of the same order of magnitude as the Reinikka-Svensson study — to 90% in 1999. The causes or nature of this improvement are yet to be known. It does suggest, however, the scope for simple information disclosure policies to dramatically reduce leakage rates within the governmental delivery system. The success of this approach has now prompted neighboring African countries — Ghana, Mozambique and Tanzania — to institute similar service provider surveys to assess leakage rates recently.

5.2 Citizen Involvement in School Management³⁹

A second form of empowerment is to let citizens participate directly in the management of public service institutions. The most common form is the role of parent-teacher-associations (PTAs) in managing schools. PTAs have begun to play significant roles in Uganda, El Salvador and Nicaragua, following civil wars and consequent breakdown in central government role in the 1980s. In the community-managed program EDUCO (*Educacion con Participacion de la Comunidad*) in El Salvador, started in 1991, schools were managed autonomously by community education associations (ACEs). Members were elected by parents of the students, and given basic training in school management. The ACEs were given authority to hire and fire teachers, monitor teacher performance, equip and maintain the schools. The EDUCO program was originally intended to expand educational access in rural areas

³⁹The discussion of this and the subsequent section relies heavily on the Symposium on Education Reforms in the *World Bank Research Observer*, September 1999, 13(3), pp. 409-508.

quickly, a goal which is now believed to have been achieved. Accordingly the education ministry is contemplating its extension to all traditional schools.

Emmanuel Jimenez and Yasuyuki Sawada have evaluated the impact of the EDUCO program on school attendance rates, and student performance in mathematics and language.⁴⁰ After controlling for school and student characteristics, they find a positive significant effect on language tests, and a positive insignificant effect on math tests at the third grade level. And they find a significant negative effect on student absenteeism. These results suggest that parental involvement in school management enhanced school quality while permitting a wider and quicker spread of educational access.

Nicaragua embarked on a similar reform also in 1991, establishing councils in all public schools to ensure participation of student parents. Key management tasks were transferred from central authorities to these councils starting with a pilot program in 1993, and extended to over 100 secondary schools and 200 primary schools that acquired autonomy. The councils have the authority to hire and fire the school director, and are involved in maintaining physical and academic quality. The Education ministry retains authority over curriculum, school fees, and establishes norms for staff promotions and teacher certification. All other issues are devolved to the school councils, almost in the same manner as private schools. Elizabeth King and Berk Ozler have evaluated the effect of this reform on the basis of school-household surveys and student achievement tests, after controlling for student, family, school and teacher characteristics.⁴¹ They find that *de jure* autonomy has not translated into *de facto* autonomy in a significant number of schools in this program. Many decisions concerning pedagogical and personnel matters continue to be taken by the Ministry rather than the school council. Their main finding is that there is a significant positive effect on student performance only in schools with *de facto* autonomy; in the others there is no perceptible impact.

⁴⁰E. Jimenez and Y. Sawada, "Do Community-Managed Schools Work? An Evaluation of El Salvador's EDUCO Program," *World Bank Research Observer*, September 1999, 13(3), 415-442.

⁴¹E. King and B. Ozler, "What's Decentralization Got To Do With Learning? The Case of Nicaragua's School Autonomy Reform," Working Paper, Development Research Group, World Bank, June 2 1988.

5.3 Direct Transfers to Citizens

Mexico developed a community-based targeting system called *Programa Nacional de Solidaridad (Pronasol)* in 1988 under President Salinas, which provided resources to local Solidarity Committees for educational scholarships, local infrastructure projects-cum-employment schemes and food subsidies for the needy. This program is reported to have been politically motivated to consolidate the power of the ruling party PRI in poor areas. Targeting levels were believed to have been low, and local committees were often dominated by PRI activists rather than grass-roots citizen representatives. The President retained tight control over disbursement of funds, and is said to have allocated funds preferentially to areas where the PRI was more vulnerable.⁴² Evidence of similar political considerations in the allocation of funds across regions in central government discretionary programs have been identified in the case of Albania, Peru and Nigeria.⁴³

Pronasol was replaced by the Zedillo administration by *Progresas*, a more formula bound and better targeted program of cash grants to poor families in poor regions for children's educational expenses. The program uses a two stage process, first selecting the poorest localities based on a set of criteria. After selecting a randomly chosen fraction of the poorest localities, it undertakes a census within the chosen localities to identify the poorest households. The census collects figures on household size and demographics, characteristics of the household head (age, sex, occupation, and schooling), and its dwelling. Households classified as 'poor' according to a discriminant function based on these criteria then determines eligibility. Selected households receive an education subsidy, starting from third grade and continuing till the ninth grade, conditional on attending school at least 85% of the time. Subsidies increase with age, and are higher for girls in secondary school. A fixed transfer is also made conditional on going to health clinics for preventive check ups. As of 1999, this

⁴²For detailed references to the literature evaluating *Pronasol*, see Conning and Kevane (1999, Box 4).

⁴³A. Case, "Election Goals and Income Redistribution: Recent Evidence from Albania," *European Economic Review*, 45, March 2001, 405-423; N. Schady, "Seeking Votes: The Political Economy of Expenditures by the Peruvian Social Fund (FONCODES) 1991-95," Working Paper, Development Research Group, World Bank, 2000; and M. Ayogu, "The Political Economy of Infrastructure Investments in Nigeria," mimeo, Center for International Development, Harvard University, April 2000.

program was being implemented in nearly 50,000 rural localities in over 2000 municipalities all over the country. Approximately 2.6 million families, or 40% of all rural families, were covered. The total annual budget on the program amounted to \$777 million, or about one fifth of the entire Federal poverty alleviation budget.

A distinctive feature of *Progresa* has been the involvement of economists in its design and subsequent evaluation. In particular, localities were selected to participate in the program on a randomized basis, thus helping avoid biases in evaluation resulting from endogenous participation of communities. Consequently a large number of reserachers have begun to evaluate its effects using household data. Most studies find positive and significant effects on school enrollment and child nutrition.⁴⁴ For instance, Jere Behrman, Piyali Sengupta and Petra Todd (2000) find that grade progression rates for 12 year children from sixth to seventh grade increased by 11%, and from fifth to sixth grade increased by 9%, owing to a decrease in drop-outs and higher school re-entry rates. David Coady (2001) finds that most of *Progresa's* targeting effectiveness is achieved in the first stage where poor localities are selected, rather than in the second stage where households are selected within localities.⁴⁵ This is opposite to the pattern identified by Galasso and Ravallion for the Bangladesh FFE program (which differed insofar as selection of local beneficiaries was delegated to local communities, rather than relying on census information). Combined with the Porto Alegre and Bolivian decentralization experiences, the Coady study of *Progresa* suggests that formula bound transfer programs achieve significant gains in interregional targeting, compared with those where the central government retains discretion (as in the Albania, Nigeria and Peru cases alluded to above).

⁴⁴See the following Working Papers of the International Food Policy Research Institute, Washington DC: J. Behrman, P. Sengupta and P. Todd (2000), "Progressing through PROGRESA: An Impact Assessment of Mexico's School Subsidy Program."; E. Skoufias and S. Parker (2000), "The Impact of PROGRESA on Work, Leisure and Time Allocation." See also T. Paul Shultz (2000), 'School Subsidies for the Poor: Evaluation of a Mexican Strategy for Reducing Poverty,' mimeo, Department of Economics, Yale University.

⁴⁵D. Coady, "An Evaluation of the Distributional Power of Progresas's Cash Transfers in Mexico," Working Paper, International Food Policy Research Institute, Washington DC, May 2001.

5.4 Subsidies to Private Sector Alternatives

Finally, reform efforts can focus on enlarging the range of service options available to citizens. We describe two recent educational reforms in Pakistan and Colombia respectively that enhance access to private sector alternatives for poor families.

The Balochistan Education Foundation launched an Urban Fellowship Program in Quetta, Pakistan in 1995, which provided subsidies to starters of private schools. The subsidies were paid directly to the schools. Schools were assured of government support for three years, though they would subsequently be eligible to apply for educational grants. The initial subsidy was 100 rupees per month per girl enrolled, with an upper limit for 100 girls enrolled. This covered tuition in the lower priced private schools of the region. In addition each school received 200 rupees in startup costs per girl enrolled. The schools were also allowed to admit boys provided they made up less than half of the total enrollment, but there was no subsidy offered for enrolled boys.

To implement the program, the Balochistan Education Foundation contracted with an NGO, the Society for Community Support of Primary Education in Balochistan (SCSPEB), which had several years of prior experience in this respect. The SCSPEB conducted an initial census of each potential site to see if there was enough demand for the program, then informed relevant parents, formed a parent committee, helped this committee develop a proposal detailing the neighborhood's need for a school, and eventually invited proposals from experienced school operators. The parent committees were allowed to select a school operator from the bids received, or choose to run it themselves.

The pilot program for this involved 10 locations, corresponding to the 10 slum areas of Quetta. In each of these slum areas, three potential sites were identified, and one of them was randomly chosen for the experiment. All selected sites agreed to participate, so this ensured that the effect of the program could be evaluated without worrying about biases resulting from endogenous participation effects. Jooseup Kim, Harold Alderman and Peter Orazem (1999) have evaluated this experiment in terms of school enrollment.⁴⁶ Using

⁴⁶J. Kim, H. Alderman and P. Orazem, "Can Private Subsidies Increase Schooling for the Poor? The Quetta Urban Fellowship Program," *World Bank Research Observer*, September 1999, 443-466.

household level data they identify the effect on a household's decision to enroll its children in a school, as a function of household, school and neighborhood characteristics. This allows a relatively clean identification of the effects of location of the project in a slum area on school enrollment rates. They find that the enrollment rate in fellowship neighborhoods rose 33% for girls and 22% for boys after controlling for other characteristics. These enrollment increases were independent of neighborhood or other socio-economic characteristics — i.e., they operated uniformly in all kinds of neighborhoods and all kinds of households.

The study goes on to compare the cost-effectiveness of this reform relative to alternatives, such as building more public schools or direct education subsidies. The private schools paid far lower teacher salaries than the public schools, so the cost of the subsidy was approximately one third the cost that would have been incurred in generating similar enrollment increases by operating more government schools in the region. Start-up costs of a government primary school would have been 6,000 rupees per student, contrasted to 1,500 rupees paid in contracting fees to the NGO in the fellowship program. Kim, Alderman and Orazem also find the costs of this program to be two and a half times lower than direct income transfers to the households that would have elicited the same impact on the enrollment rates. Hence the pilot study suggests that subsidizing private schools in poor neighborhoods can be a particularly cost-effective strategy of raising school enrollment rates of poor children.

Another form of intervention more common in South and North America has been provision of education vouchers to households. These are closely related to the direct cash transfer approach. Chile has a long experience with voucher schemes, going back to the early 1980s, while other countries have begun experimenting with these more recently. Poor households are identified, and offered vouchers which they can use in any school of their choice. These vouchers can be redeemed by the school from the government. So they represent a form of education subsidy. A hallmark of these schemes is that the vouchers can typically be used in any school chosen by the students' parents, private or public. In neighborhoods where there are private school alternatives to public schools, it is commonly argued that voucher schemes exert competitive pressure on public schools to perform. Poor quality schools would lose students to better performing ones. Opponents of voucher schemes have typically argued

that such freedom of choice reinforce segregation of schools into different socio-economic or merit categories, because private schools can pick and choose among different student applicants. High quality schools get the high quality students, and vice versa, thus reducing equality of educational opportunity. Moreover, voucher schemes deprive public schools of much needed resources. Empirical evaluations of voucher schemes in Chile and the United States are yet to emerge with any definite conclusions: the results of different studies are frequently conflicting.

Colombia introduced a voucher scheme in the 1990s, whose principal motivation was somewhat different. The notion was that public schools were overcrowded, particularly in urban areas, while private schools had excess capacity. Vouchers permitting poor households to enroll in private schools were seen as a way of reallocating students across the two sectors, at relatively low cost. At the same time the government assured public schools that their current levels of funding would not decrease. The Ministry of Education initially targeted the country's 10 largest cities for participation in 1991. The program subsequently grew. By 1995, 27 of the 30 states (departments) in the country were in the program; 90,000 vouchers were awarded to students in 1800 private schools. Voucher students made up about 8 % of all students in private secondary schools. They were offered a year at a time to students that had completed fifth grade, and were continuing to higher grades. The vouchers were renewed annually conditional on being promoted to the next grade.

Most of the vouchers were issued in large urban areas where private schools were concentrated. Ten states absorbed more than 70% of all vouchers issued. Participation of a municipality was contingent on its willingness to cofinance 20% of the costs of the program. Only one quarter of all municipalities participated in the program. And even within these municipalities, only one half of private secondary schools agreed to participate. Hence the spread of the program was highly uneven, and its interregional allocation is likely to have been regressive. This is in contrast to the highly progressive pattern of interregional allocation of *Progresá* benefits in Mexico.

The targeting criterion within municipalities was a neighborhood stratification scheme, which were ranked poorest to richest on a scale from 1-6. Only students residing in neigh-

borhoods ranked 1-2 were eligible to receive the vouchers. Evaluations of intra-regional targeting of this program have been favorable: schools that responded to the program typically served students from poorer households, and voucher recipients typically came from the poorest socio-economic strata.⁴⁷

However, monitoring the program proved to be cumbersome and costly. To guard against ‘ghost’ voucher awardees, the signature of each voucher student was required four times a year prior to release of the vouchers by regional offices of program administrators. Delays in obtaining these signatures and corresponding certification by local officials delayed payments to the schools, creating difficulties for school finances. These problems, besides weakening support for the program within the Ministry of Education, caused the scheme to be terminated in 1997.

6 Concluding Comments

The principal objective of these lectures has been to provide a perspective on the experience of a number of developing countries with institutional reforms in the delivery of social services. I will conclude by summarizing the nature and intent of these reforms, and then discuss the lessons to be learnt from them for both academic researchers and policy makers.

The bulk of the reforms have been motivated by the need to address problems of resource diversion, targeting failures and inappropriate project selection that have characterized traditional development programs administered by centralized bureaucracies. These problems stemmed partly from poor information available to policy makers concerning priorities and needs of citizens in diverse regions, which stymied selection of appropriate local projects, and identification of local beneficiaries. They were severely accentuated by absence of accountability pressures on government employees appointed by a distant central government, that was either unable or insufficiently motivated to monitor their performance. Various instances of corruption, in the form of diverted resources to black markets, cost-padding in

⁴⁷For further details, see E. King, P. Orazem and D. Wohleguth, “Central Mandates and Local Initiatives: The Colombia Education Voucher Program,” *World Bank Research Observer*, September 1999, 467-492, and references cited there.

procurement, and bribes for service delivery, have been documented by diverse empirical studies. These studies confirm the large number of anecdotes and newspaper reports of widespread corruption that have crippled government programs worldwide.

Three categories of reforms to enhance accountability were distinguished. The first category consists of reforms within centralized bureaucracy to design and implement superior incentive schemes for bureaucrats, consisting of salary reforms and efforts to monitor bureaucratic performance more closely. Bureaucratic reforms typically encounter a large number of design and implementation problems. Relevant performance variables for government bureaucrats are multidimensional and frequently hard to measure. Incentive reforms run contrary to core civil service norms of guaranteed employment, and pay divorced from merit. Complementary policies of heightened monitoring are hard to implement credibly, owing to political problems and tendency for hierarchical superiors to stall and prevent high level ‘crackdowns’. These problems are compounded by weak political will of politicians to reform bureaucracies from within.

Accordingly, after a half century of frustrating experience with a delivery system operated by non-accountable centralized bureaucracies, a large number of countries have begun experimenting with various forms of decentralized delivery systems. Common to all of these is a reallocation of authority over management of the delivery system away from centrally appointed bureaucrats, towards citizen clients and their local representatives. It is important to appreciate that this does not necessarily reduce the authority of central politicians, who may still receive tax revenues and decide how to allocate them to different regions or across different investment sectors. It is really a different form of delegation, involving a change in the pattern of intermediation in the service delivery process. These reforms may or may not be accompanied by a reduction in the discretionary authority of the center with regard to the disbursement of funds. In some cases they have been accompanied by greater discretionary control of central politicians, at the expense of district governments and officials, as in the case of *Pronasol* in Mexico, or *Foncodes* in Peru. In others they have been characterized by significant devolution of financial authority by the central government to local communities, as in the case of Bolivia and Philippines. Accordingly the term ‘decentralization’ may be somewhat confusing: empowerment of local communities and citizens

is more apt.

I distinguished between two forms of such local empowerment. The first is devolution of authority to elected local governments. Here a constitutional amendment typically mandates creation of local governments, the holding of periodic elections, and the range of authority and responsibilities of elected bodies. The second relies on empowerment of citizens directly, or of their non-governmental representatives. It involves direct participation of citizens and of civil society, rather than utilizing the political process; it expands access of citizens and citizen groups to information, legal resources, management of service institutions, and private sector alternatives.

A large variety of such institutional reforms in different countries have begun to be implemented in many low and middle income countries since the late 1980s and early 1990s. It is perhaps too early to assess their effectiveness, but the indications are that they are capable of significant impact if designed and implemented suitably. Evaluating the distributional effect of these experiments requires a combination of detailed household and community surveys, across regions or points of time that have experienced varying degrees of reform. Apart from the potential non-availability of such data, the most serious evaluation problem concerns the potential endogeneity of the implementation of such reforms. Whether or not a particular country or region implemented a reform at a particular point of time may be a function of a large number of underlying political and economic circumstances. Since data on many of these circumstances may not be available to social scientists, there is a danger of falsely inferring correlations between the reforms and their distributional outcomes, when they happen to be driven by the underlying political and economic circumstances rather than by the reforms *per se*. In other words, the implementation of the reforms may be the symptom of deeper social changes, rather than the cause of observed changes in service outcomes. These endogeneity problems are minimized when the experiments are designed in a randomized fashion, as in the case of Mexico's *Progresa* system of cash transfers or the Quetta private school subsidy program in Pakistan. However, such randomization in reform implementation is often politically difficult and raises ethical dilemmas.

Many studies of the effect of decentralization to local governments are vulnerable to

this endogeneity problem. It is less severe in the case of Bolivia or Porto Alegre, since the decentralization occurred uniformly in all regions at a particular point of time. However, the studies available compare outcomes before and after the decentralization, and need to consider appropriate counterfactuals of what might have happened in the absence of the reform. These studies also rely on aggregate data concerning aggregate service levels or investments in different sectors at the community level. They need to be complemented with household surveys that measure the distributional impact of the reforms within communities, to assess the extent to which decentralization may have been hijacked by local elites. In addition, they need to separate the role of decentralization from other changes in the economy that may have been taking place at the same time. Despite these qualifications, the effects on level and composition of services at the community level do appear to be striking. Access to water, sanitation and primary education increased dramatically in Porto Alegre and Bolivia. In Bolivia the cross-regional pattern of these respond to measures of local need in exactly the way one would expect from a successful decentralization.

The studies for Uganda, Philippines and Bangladesh in contrast examined the performance of the decentralized system at a single point of time across different regions. This makes it difficult to assess the effects of the decentralization, compared to the prior status quo. Instead, it permits an assessment of the targeting success of a decentralized system across different communities as a function of their socio-economic characteristics. This was exactly the scope of the Galasso-Ravallion evaluation of the FFE program in Bangladesh. Their results were encouraging insofar as they indicated some degree of targeting success within local communities, despite the presence of elements of local capture. A comparable evaluation exercise was not possible for Uganda and Philippines owing to lack of data at the household level. The latter studies do however provide interesting evidence concerning the extent, determinants and implications of corruption in the service delivery process, besides suggesting potential problems with local capture in Uganda.

The third category of civic decentralization reforms relies on enhancing access of citizen groups to information, management of schools, education subsidies and private sector alternatives. Here the design of these experiments and availability of household level data have permitted a more detailed assessment of their effectiveness. The evidence is by and large

encouraging. The information disclosure policy in Uganda appears to have dramatically increased access of schools to disbursed central funds. Parent teacher associations in schools have gained importance both with respect to management and financing in El Salvador and Nicaragua, with positive effect on student achievement. The direct cash transfer program *Progresa* for child education and nutrition in Mexico appears to have achieved a high level of targeting via use of geographic and socio-economic criteria in the selection of regions, in contrast to the politically driven allocations of the *Pronasol* program it replaced. Effects on school enrollment and nutrition have also been favourable. Examples of other reforms in this category include subsidies to private school operators to set up schools in slum areas of Quetta, Pakistan, and educational vouchers in Colombia and Chile. While the evidence concerning the effectiveness of voucher schemes have been mixed, the Quetta initiative appeared to have been successful in raising enrollment rates of girls significantly. The design and evaluation of this policy experiment permitted a comparative evaluation with other alternatives such as building government schools or providing cash transfers to increase enrollment. Public subsidies to private schools to expand educational access to poor children turned out to be remarkably cost-effective. Hence governments should actively consider such mixed public-private partnership approaches at a time when fiscal pressures limit the ability of the public school system to meet educational needs.

What are important questions that need to be addressed in future research? The next step should clearly be (a) more detailed explorations of the effects of decentralization using household level data, and (b) the choice among different reform alternatives. Most studies have confined attention to the evaluation of a single reform that has been implemented, relative to the counterfactual of no reform at all. The next step should be assessment of the given reform relative to the counterfactual of alternative reforms. Only the Kim, Alderman and Orazem study of the Quetta private school subsidy program attempted such a comparative evaluation. Such comparative assessments require a more detailed understanding of local institutions and the way they shape behavior, an exercise which is more demanding than assessing the outcome impact of a given experiment.

Many additional design issues need to be addressed within any one of these reform strategies. In the case of local-government-based decentralization, what should be the exact range

of decisions devolved to local governments? Should they have authority over management of local schools and hospitals, besides infrastructure? What kind of say should they have over investment allocation across these sectors? What kind of financing authority should they have? How should central finances be allocated across different municipalities? How should local governments be elected? What kind of accounting and disclosure rules should they be subject to? Within the context of citizen empowerment, should the government rely on direct cash transfers, education vouchers or subsidies to private school operators? What roles should parents and NGOs have with regard to establishment and management of schools? What kinds of information and legal authority should such citizen groups be granted with regard to their rights to information and financial support from the government?

A key design issue is the role of discretion versus formulae in inter-regional grants. The evidence available so far suggests that formula based transfers that rely on geographic measures of need can achieve high levels of targeting. The experience in Porto Alegre, Bolivia and Mexico with formula-based transfers in improving equity and stability of resource transfers across regions is encouraging in this respect, particularly in contrast with the discretionary systems that previously prevailed in those countries. The evidence concerning the role of census information in targeting within communities is less favourable (e.g., in Mexico). Devolution of intra-community transfers to community representatives appeared to work well with Bangladesh's Food For Education program. These results suggest the scope for devolving intra-community allocation to local bodies, while interregional allocations are formula driven. Yet these results are merely suggestive, and more needs to be known concerning the dangers of local capture. Where this is a serious consideration, formula-bound transfers based on census information within communities may be more reliable.

One other important question concerning future research needs to be mentioned: what determines the likelihood that a given central government will want to adopt any serious reforms at all, and if it does, which variant is it likely to select? How keenly will it seek to implement it? What ensures that a given reform remains logistically, financially and politically sustainable? Our discussion focused on the countries where some reforms have taken place. Also significant are the large number of countries where no such reforms have been undertaken at all. We also noted implementation and sustainability problems in some

countries that did embark on some initiatives. This positive political economy question is important to appreciate the deeper political and economic compulsions that motivate the choice and implementation of reforms. This question has not been devoted any attention at all in the existing literature. We need to understand better the role of constitutional safeguards *vis-a-vis* discretion in the implementation of decentralization. To what extent can we really expect a central government to faithfully implement a decentralization designed to reduce its own power in a discretionary reform process?

Let me turn finally to a question I have avoided so far: what are the possible policy implications for India? A detailed discussion of this question must be reserved for another occasion. Yet I think it is appropriate to at least raise some issues in a preliminary manner, and ask what India has to learn from the recent reform experiences of other countries.

India has implemented a country-wide experiment with decentralization to local governments, since passage of the 73rd and 74th Constitutional Amendments in the early 1990s. The scale and scope of this reform is impressive by any international standard. Yet the implementation of this initiative has been devolved to various state governments, with the result that the pattern of implementation is highly uneven across states. Considering that many Indian states are larger than many of the countries whose experience I have described here, it is fair to think of the experience of each Indian state as comparable to that of entire countries elsewhere. Apart from sheer size, the fact that agriculture and social services are state subjects in the Indian Constitution implies that each state should be viewed as a separate case. The primary notion of decentralization then pertains to devolution of powers and finances from state governments to local governments (*panchayats*).

The diversity of these patterns of decentralization across different states is truly dramatic. For instance, Kerala appears to have combined the decentralization with a significant devolution of formula based transfers to *panchayats*, approximately 40% of all state revenues. Levels of citizen participation in local decision-making concerning use of these resources in Kerala also appear to be significantly above those in other states.⁴⁸ In contrast a very

⁴⁸For further details concerning the *panchayat* reforms in different states, see *Status of Panchayati Raj in the States and Union Territories of India*, George Mathew (Editor), Concept Publishing Company for Institute of Social Sciences, 2000.

limited extent of autonomy has been awarded to *panchayats* in West Bengal, as in most other states. Education and health remain entirely outside the province of *panchayati* authority. There is almost no devolution of unconditional grants to *gram panchayats*. Grants are primarily tied to specific employment, housing or irrigation programs, with detailed regulations concerning how they are to be allocated across sectors and expenditure categories. Below the district level, most grants are not driven by any transparent geographic targeting formula based on local needs. The only authority devolved to panchayats concerns selection of local beneficiaries of government programs, management and implementation of local infrastructure projects covering roads, irrigation and housing. By international standards, this is a very limited form of decentralization indeed.

In particular, there have been no reforms to expand local control over education and health facilities. The primacy of problems of teacher accountability have been repeatedly emphasized by numerous studies of primary schools in India. For instance, Jean Dreze and Haris Gazdar concluded on the basis of their surveys of schools in Uttar Pradesh that⁴⁹

“Teacher absenteeism was endemic in the sample schools. By all accounts, this is the most basic problem of the schooling system in the sample villages. One indication of the magnitude of this problem is the simple fact that two thirds of the teachers in the sample schools were absent, for one reason or another, at the time of our unannounced visit....These direct observations were amply confirmed by informal conversations with parents and local residents. Shirking and absenteeism on the part of school teachers was widely perceived as the fundamental problem of government schools in all the sample villages.”

In similar vein, the PROBE study of educational achievement in northern India indicates the seriousness of accountability issues in the performance of primary and secondary schools, and of the positive role played by local communities in improving the spread and quality of educational access in Himachal Pradesh relative to Uttar Pradesh. Questions concerning the appropriate way to encourage local control need to be addressed. The involvement of

⁴⁹J. Dreze and H. Gazdar, “Uttar Pradesh: The Burden of Inertia,” in *Indian Development: Selected Regional Perspectives*, J. Dreze and A. Sen (editors), New Delhi: Oxford University Press, 1996.

panchayats, parent teacher associations, and Village Education Councils needs to go far beyond the merely decorative functions of organizing Independence Day celebrations. Local communities must acquire *de facto* autonomy over hiring and firing of teachers, and monitoring teacher performance. They should have a significant say over school management, have access to school financial accounts, and be encouraged to contribute to school finances. The cooperation of NGOs can be sought in the setting up of new schools, and in training of teachers and parents in school administration. In urban and suburban areas, different forms of partnerships with the private sector can be considered to expand educational access for poor children. Pilot experiments can be designed for different reforms to gauge their relative effectiveness, such as subsidies to private school operators, cash transfers, vouchers, and expansions in the government school system, with subsequent plans to expand the successful experiments into large scale programs.

The West Bengal experience with decentralization is distinctive for having been sustained for over two decades now, in contrast to the rest of the country where the process has just begun. It is also unique in having been combined with a large scale land reform consisting of implementation of land ceiling laws, land redistribution to the landless, and registration and regulation of sharecroppers. It has been argued that the land reforms were complementary to the decentralization experiment, in limiting the scope for local capture, and in harnessing the information resident in local communities concerning suitable beneficiaries of the land reforms. Such accompanying land reforms are unlikely to occur elsewhere in India, primarily owing to lack of political will. Local capture is likely to be higher in states with greater land inequality, illiteracy and poverty; accordingly decentralization is less likely to yield significant accountability improvements in such states compared to West Bengal. A number of case studies for Uttar Pradesh and Madhya Pradesh have expressed pessimism based on the expectation of high local capture.⁵⁰

Designers of decentralization in India also need to devote greater attention to the electoral process by which *panchayats* are elected. So far each state has gone its own way in deciding how to institute these elections. There are many accounts of attempts by political

⁵⁰See for instance Mathew and Nayak (1996) for Madhya Pradesh, and G.K. Lieten "Panchayats in Western Uttar Pradesh," *Economic and Political Weekly*, September 28 1996, 2700-2705.

parties governing at the state level to manipulate the electoral process in favor of their own party at the local level.⁵¹ Redesigning the balance of power between *panchayat* leaders and state bureaucrats is also critical to successful implementation. If state bureaucrats continue to retain the same authority with respect to financing and execution of local projects, the decentralization will remain entirely *de jure* rather than *de facto*. This problem has been highlighted by Raghav Gaiha for Uttar Pradesh, and more generally by a number of others.⁵² Mahi Pal writes for instance:

‘But, with some exceptions in Kerala, Madhya Pradesh, Tripura and West Bengal, nothing worthwhile has been devolved to the panchayats. The bureaucracy at all tiers of panchayats is holding the balance.’

The success of the decentralization initiative in India will depend on these various aspects of its design and implementation: the range of authority and finances devolved to local governments, role for *panchayats* or other local citizen bodies in management of schools and health facilities, use of uniform, externally enforced standards for elections to *panchayats*, and redesign of relations between state bureaucrats and local authorities so as to convert *de jure* autonomy to *de facto* autonomy. The particular way that the decentralization movement has been implemented in India has awarded a very significant measure of discretion to state governments in these respects, and the resulting patterns do differ very widely. Reforms in other countries have been based on more detailed constitutional design which have awarded significantly more autonomy to local bodies. Accordingly it is likely that the experience with decentralization will be more uneven across different parts of India, and less dramatic. Increased inter-regional inequality may result from this unevenness, as some states prone to a greater crisis of government accountability will tend to implement reforms in a more half-hearted fashion, and tend to fall further behind. Education and health sec-

⁵¹P.S. Verma, ‘Zilla Parishad and Panchayat Samiti Elections in Punjab,’ *Economic and Political Weekly*, June 3 1995, 1321-1328, and G.K. Lieten ‘Panchayats in Western Uttar Pradesh,’ *Economic and Political Weekly*, September 28 1996, 2700-2705.

⁵²R. Gaiha, ‘Participation or Empowerment of Rural Poor: The Case of Panchayats in India,’ mimeo, Faculty of Management Studies, University of Delhi, April 1996. Mahi Pal, ‘Documenting Panchayat Raj,’ *Economic and Political Weekly*, September 8 2001, 3448-3450.

tors require efforts to improve their spread and quality by bringing them under effective control of local communities, and allow citizens a wider range of choices. Overall, India needs to experiment more actively and boldly to enhance government accountability. To initiate such experiments, an active public discussion of the next step of reforms is needed, in the same constructive spirit that Romesh Dutt pioneered a hundred years ago.