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George E. Peterson

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Decentralization in Latin America

*Learning through Experience*

George E. Peterson

The World Bank
Washington, D.C.
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George E. Peterson is a senior fellow at the Urban Institute in Washington, D.C. He has published several books on decentralization and local government, in both the United States and the developing world.

The publication is part of the World Bank Latin American and Caribbean Studies series. Although these publications do not represent World Bank policy, they are intended to be thought-provoking and worthy of discussion, and they are designed to open a dialogue to explore creative solutions to pressing problems. Comments on this paper are welcome and will be published on the LAC Home Page, which is part of the World Bank's site on the World Wide Web. Please send comments via e-mail to laffairs@worldbank.org or via post to LAC External Affairs, The World Bank, 1818 H St. N.W., Washington, D.C. 20433, U.S.A.

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FOREWORD

THIS DOCUMENT HAS BEEN prepared to help educate the public—voters and taxpayers in Latin America, as well as public officials and policy-makers throughout the Hemisphere—about the critical choices facing nations undergoing what I have called the “quiet revolution” of decentralization in Latin America and the Caribbean. Nations throughout the region have extended power-sharing arrangements to local governments, backed by automatic revenue transfers that double, even quadruple local government incomes compared with a decade ago. From Mexico to Argentina, cities are now spending 20 to 40 percent of public-sector revenues, amounting to significant fractions of GDP.

In tandem with these changes, and possibly of greater importance, the region has achieved a democratic transition. Virtually every mayor and councilmember in the more than 13,000 units of state (or intermediate) and local governments is now chosen by democratic vote. All but a few places have completed this transition. These shifts of decision-making power, shared revenue, and democratic reforms have changed the face of local government and have posed challenges for central- and local-government leaders, as well as for civil society and financial and technical assistance organizations.

This report was commissioned by the Technical Department for Latin America and the Caribbean to provide perspective and insight into important issues of public choice raised by the quiet revolution. This work is in keeping with the Technical Department’s mandate to address issues that are “upstream” from the lending operations and that cut across the several disciplines and country departments at the World Bank.

George Peterson provides trenchant and penetrating insight into these issues and has a gift for clarity in expository writing. Dr. Peterson has a distinguished career in economics and finance of intergovernmental affairs and has published and lectured widely on these subjects. He was co-author of the Technical Department’s founding study on decentralization, published in 1991. That report laid down the basic analytical framework, which is also seen in the present volume.¹

In the past five years, the Technical Department has conducted numerous follow-up studies focusing on intergovernmental affairs in spending assignments, finance and management, as well as specific sectoral concerns like health and education. The most recent study analyzes the origins and dissemination of innovation in best practice among local governments.²

Interested readers can find text files or references to these and other works on the World Bank’s web site or by contacting the Public Affairs Office of the World Bank or its Infrastructure Network.

Tim Campbell
Principal Urban Sector Specialist
Latin America and the Caribbean
Technical Department
INTRODUCTION

FOR ALMOST A DECADE, a wave of decentralization has been sweeping through Latin America. Governments that have traditionally been centralized have transferred many of their service responsibilities, and much of their revenue, to local governments or to states and provinces.

No single motivation lies behind this transfer of authority. However, most decentralization initiatives embrace two fundamental propositions. Each implies a critique of past governing patterns as well as a set of priorities for reform.

First, decentralization can strengthen democratic participation in government. Decentralization has been accompanied by popular election of mayors and by other steps designed to expand the participation of ordinary citizens in local governance. Citizens form their first expectations of how government should work by observation at the local level. If they are able to take part in setting priorities for municipal budgets, to hold public officials accountable for their performance while in office, and to collaborate with municipal authorities in delivering services through neighborhood groups or other organizations, their initial experience is likely to strengthen the demand for participatory democracy at all levels.

Of course, decentralization does not guarantee that local governments will listen to the voices of ordinary citizens. Local elites may operate municipal institutions in a closed manner that makes them less accessible to the populace than central-government offices in the capital. A citizen's first taste of municipal political life may involve corruption or extreme favoritism toward adherents of the party in local office. Decentralization creates an opportunity for greater citizen control in governance, but other reforms must occur simultaneously if this opportunity is to be realized.

Second, decentralization can improve the quality and coverage of local public services. Frustration with the way national institutions supply local services like drinking water, road improvements, schooling, and primary health care underlies much of the demand for local control. The desire to be served more effectively by the public sector adds a crucial practical dimension to current decentralization initiatives. It distinguishes them from earlier efforts at enhancing municipal authority, which often were premised on ideological opposition to central government or the desire to maintain regional life of a separate character from the rest of the nation.

Decentralization's potential for improving public services stems largely from the efficiency
of incorporating local citizens' demands into expenditure decisions. Local residents are better positioned than anyone else to determine their own priorities for government services and local public works. And if they are required to raise part of the resources to pay for service improvements, they almost certainly will have opinions about how public funds should be spent. A system that permits residents to participate in local budget choice should satisfy public-service demands more effectively than a system that prescribes local service levels from central-government ministries.

Through aggressive oversight of local service providers or the use of self-help construction, municipalities may also be able to build roads and schools more cheaply than national institutions, or to find ways to restrain the operating costs and to improve the quality of local schools and health clinics. In this way, decentralization opens the possibility for greater efficiency in service production as well as greater attention to public preferences when setting priorities.

The potential efficiencies of decentralization are not self-executing, any more than is the linkage between decentralization and democracy. There must be mechanisms that accurately capture the public's service demands and make clear the connection between services received and fees or taxes paid. Even when citizens' demands are clearly expressed and local governments wish to be responsive, they may be unable to deliver services efficiently. Municipal employees may lack technical skills. Economies of scale may make it impossible for small municipalities to provide certain types of services effectively.

For all these reasons, decentralization is a venture into the uncertain. Practical decentralization does not end with a one-time transfer of revenues and responsibilities, achieved by constitutional amendment or new legislation. It requires the work of at least a generation devoted to creating new institutions, then modifying them in the light of experience.

Decentralization also introduces new risks into national governance. Central authorities lose some control over the aggregate public-sector budget, and they may be less well equipped to respond to macroeconomic shocks or less able to implement nationwide investment plans. Budget pressures at the central level will increase if revenue sources are relinquished to lower levels of government more rapidly than service responsibilities can be transferred. The very act of fine-tuning intergovernmental financing arrangements or modifying service assignments, so necessary to an implementation process that proceeds by trial and error, can inject instability into the national fiscal picture. Successful decentralization cannot treat these repercussions on central budgets as an afterthought. Central authorities are critical partners in the decentralization process. Their roles need clarification and adequate budget support as much as those of other levels of government.

**Purpose and Organization of This Publication**

This publication takes stock of Latin America's experience with the new wave of decentralization. Major changes in government structure clearly are under way. Table 1 illustrates just how strongly revenues and expenditure responsibilities

<table>
<thead>
<tr>
<th>Country and Decentralization Measure</th>
<th>Years</th>
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<tbody>
<tr>
<td>Brazil State and Municipal Share of Public Sector Expenditure</td>
<td>1990 1991</td>
</tr>
<tr>
<td>Chile Regional and Municipal Share of Public Sector Expenditure</td>
<td>1980 1992</td>
</tr>
<tr>
<td>Colombia Departmental and Municipal Share of Centrally Collected Revenue</td>
<td>1991 1997</td>
</tr>
<tr>
<td>Bolivia Municipal Share of Centrally Collected Revenue</td>
<td>1992 1995</td>
</tr>
</tbody>
</table>

p=projected under current law

Sources: Brazil: Werneck (1992); Wilets (1993); Wiesner (1994)
Chile: Yañez (1994)
Colombia: Valenzuela (1995); Salto Social (1994)
Bolivia: Molina (1994)
are shifting from central authorities to municipalities and intermediate levels of government.

It is premature to speculate about the ultimate consequences of restructuring government on this scale, but it is not too early to look at different countries' experience for lessons as to which decentralization strategies work best in the Latin American context. In weighing implementation approaches, we can now draw upon a wealth of institutional experiments carried out at the local level, as well as national differences in the approach to intergovernmental finance. This practical experience forms part of the collective record that mayors, finance ministers, and donor institutions can consult in deciding on their own next steps in consolidating the shift of governing authority.

This paper is organized around three main challenges to making decentralization succeed—both as an efficient arrangement for service delivery and financing and as a support for democracy:

- *Establishing the National Fiscal Framework*
- *Moving Government Closer to the People*
- *Improving Municipal Service Delivery*
DECENTRALIZATION CHANGES THE RULES of the game in public finance. It shifts some of the responsibility for providing public services to lower levels of government, along with some of the revenues formerly collected and retained by the central government. The fiscal framework that is established for this transfer goes far to establish the efficiency of the new arrangements, both for local governments and for central authorities.

In principle, a decentralization plan can be designed that will shift service responsibilities and revenue sources in any mix that central authorities and their negotiating partners decide. In some parts of the world, decentralization has been adopted explicitly as a mechanism for reducing central-government deficits and cutting aggregate public-sector expenditures. For example, in the United States during the 1980s, federal grants to states and localities were cut, reducing federal outlays, with the expectation (partially fulfilled) that lower levels of government, once confronted with the full costs of sustaining program spending, would choose not to replace a good part of the lost federal funds. This strategy was designed first as a federal deficit-reduction measure and second as a means of restraining total public-sector spending.

Central governments in Central and Eastern Europe have turned over highly subsidized activities like housing supply and water provision to local authorities to run at their own expense. Sometimes they have only partially compensated municipalities for the costs of assuming responsibility for school and health services. These decentralization measures have formed part of an explicit strategy for balancing central-government budgets.

In Latin America, fears that the central government will try to export its budget deficits to provinces or municipalities also have influenced the debate over decentralization. Local authorities have sought to establish guarantees that this will not happen. Colombia's 1991 constitution, for example, requires that all transfers of service responsibilities from the central government be accompanied by a resource transfer adequate to finance the services at their current or mandated level. Other national legislatures are debating similar laws. In Brazil and Colombia, the future growth of intergovernmental revenue sharing
was guaranteed in new constitutions; in Bolivia, Venezuela, Argentina, and other countries, revenue-sharing commitments for several years into the future were spelled out in national laws. These laws were intended to reduce the financial risks of decentralization for local governments.

**Latin American Fiscal Decentralization: Revenues First**

In actuality, however, fiscal decentralization throughout most of Latin America has been executed in a way that favors local government budgets. The decentralization process has started by transferring to localities or provinces a larger—often, much larger—share of centrally collected revenues. These transfers typically are specified as a percentage of central revenue collections. At first, few offsetting spending obligations have been shifted to local authorities. Only after the transfer of revenues is well under way has the devolution of service functions, or negotiations over service devolution, begun.

In Brazil, the 1988 constitutional changes cut approximately six percentage points from the central government's share of the final retention of public-sector revenues. These revenues were reassigned to state and local authorities. The new constitution did not formally transfer any expenditure responsibilities from the central level to states or municipalities, nor was a plan drawn up to ensure that actual transfers achieved fiscal neutrality. The result has been a redistribution of resources that created a windfall gain for municipalities while tightening the squeeze on the central budget.

In Colombia, the controller general estimated that the expenditure transfers proposed in the initial decentralization decree, Decree 77, would by 1992 reduce central-government expenditures by 6.1 billion pesos (1987 pesos), compared with a loss of 39.0 billion pesos in revenue to the central budget from the additional sharing of value-added taxes prescribed by law. Thus, decentralization from the outset was recognized to be a financially costly proposition for the central government. Even this calculation, however, turned out to be optimistic, because in the early years there were essentially no expenditure savings to the central budget. Colombia's 1991 constitution attempted to correct this problem and achieve greater fiscal balance by assigning a growing portion of centrally collected revenues to lower level governments, while at the same time seeking to offset the revenue transfers with new spending obligations, especially for basic health care and education. Revenue transfers continued to exceed expenditure transfers, however.

Other countries show a similar fiscal pattern. In Venezuela decentralization legislation increased the states' share of centrally collected ordinary revenues from 15 percent to 20 percent over a five-year period ending in 1995. A legal framework is in place for transferring service and expenditure responsibilities to the states, but actual transfers require voluntary, negotiated agreements, which are running well behind expenditure transfers. In Guatemala a constitutional amendment prescribing the transfer of 8 percent of central-level revenues to local governments (subsequently raised to 10 percent) was not offset by a transfer of central-government expenditure responsibilities. Rather, the action was intended to boost municipalities' incomes so that they could embark on a new program of public improvements. The transfer of additional central-government revenues to municipalities in Bolivia, effected in 1994, had the same rationale.

The political motivation for a fiscal strategy like this is easy to understand. Subnational governments start off by receiving net fiscal benefits from decentralization. This fiscal gain has made them more enthusiastic partners in devolution, or at least has muted the opposition to decentralization among local governments often found in other parts of the world. But there are clear dangers to central-government finances if revenue is transferred without concurrent responsibilities for providing services.

On the other hand, local governments often have a legitimate reluctance to accept new responsibilities. That's because the revenue-sharing formulas being introduced today are designed in part to rectify past fiscal mismatches: Traditionally, municipal legislation assigned local governments a vast array of functions but did
BOX 1
Two Versions of Intergovernmental Gridlock

Brazil’s central government now keeps only slightly more than a third of public-sector revenue collections. The rest is distributed to states and municipalities, mostly through automatic revenue sharing, or assigned to states by granting them exclusive access to important revenue sources, like the value-added tax. Revenue sharing with sub-national governments was accelerated by the 1988 constitution. The constitution did not prescribe corresponding service transfers, and local authorities have been reluctant to assume them voluntarily. The federal administration maintains that, as a result of the constitutional changes, the revenues remaining to it are insufficient to carry out the functions it still must perform.

The 1988 constitution prescribed a review of the constitutional provisions five years after adoption. At that time the administration proposed revamping the revenue-sharing arrangements. Various alternatives were floated. One proposal called for a new federal-rural pact that would explicitly transfer expenditure and service functions to state and local authorities to offset the revenues already transferred. Another called for reducing the percentage of revenues shared with states and municipalities. A third called for giving states further taxing powers, but requiring them to finance a greater share of their operations from own-source revenues. None of these proposals made headway in Congress. Resolution of the impasse has been made more difficult by the fact that changes in the constitution must be approved by a 60 percent majority vote in Congress.

Colombia initiated decentralization in the 1980s by transferring large and increasing amounts of shared taxes to departments and municipalities. Service functions devolved only later in an ad hoc manner. The 1991 constitution attempted to correct this situation by assigning responsibility for education, health, and basic infrastructure systems to subnational units, while broadening general revenue sharing and allocating funds to pay for the specific services that were transferred.

Colombia’s step-by-step process has been partly successful, but it has generated tension between levels of government. For example, revenues for education were first transferred from the central government to municipalities. Then the responsibility and revenues for personnel management, curriculum development, and other operating functions of schools were reassigned to the departments, while municipalities retained responsibility for constructing and maintaining school buildings. Some of the larger municipalities have refused to surrender control over local schools. The teachers’ union wants to restore a national-government role in curriculum and pay-setting. The intergovernmental logjam is being resolved largely through case-by-case negotiation by municipalities, departments, and the central government.

Central authorities in Colombia also have announced that they will try to cut back the growth of revenue sharing promised in the constitution for future years. They argue that the transfers are increasing the aggregate public-sector deficit. In effect, central government has been unable to cut its other spending deeply enough to make room for the promised revenue transfers.

not provide for adequate resources to perform these functions. Thus, local authorities sometimes view the new revenue transfers from the central government as compensating them more adequately for functions they already are trying to perform, not as additional income that should be offset by the transfer of new expenditure responsibilities. This is particularly true of poor localities, where the combination of government transfers and own-source revenues historically
has been insufficient to finance even rudimentary services.

**The Risks of Fiscally Unbalanced Decentralization and High Levels of Automatic Revenue Sharing**

Decentralizing revenues before expenditures carries dangers for the intergovernmental financing system.

**Risks for National Fiscal Management**

A strategy that transfers unrestricted, general-purpose revenues first, then negotiates over expenditure responsibilities, injects uncertainty and instability into the national macroeconomic picture. The transfer of revenue streams makes necessary a second-round debate over how to restore central-government budgetary balance. As indicated in Box 1, this debate can easily lead to gridlock. Once local governments possess a formal guarantee of higher levels of revenue sharing, they have few incentives to negotiate away these fiscal gains by accepting further service obligations.

The legal obligation to maintain high levels of revenue sharing can become particularly burdensome when the central government is attempting to carry out fiscal restructuring to cut revenue streams. The country's revenue-sharing pact, however, has hampered the central government's ability to implement national fiscal policy. In the 1990s, central authorities have sought to address structural imbalances through an austerity package that combines tax reforms, increased tax collections, and expenditure cuts, including large-scale public work-force reductions. These measures were intended to close the public-sector deficit.

However, because the austerity package increased central-government tax collections, revenue-sharing payments also had to increase. About 57 percent of incremental tax receipts were automatically distributed to the provinces. Some provincial governments refused to participate in spending restraint. They added to civil service rolls and used revenue-sharing transfers to avoid provincial tax increases. In effect, the provinces negated part of the fiscal retrenchment implemented at the central level. The provinces that added most substantially to public employment were those that rely most heavily on federal transfers. This presents the paradox of a federal government making steep cuts in its own work force, while transferring funds that make it possible to hire new workers in the provincial governments that have been least aggressive in exercising cost control. The federal government reacted by requesting emergency powers that would give it greater control over intergovernmental tax and spending decisions.

Eventually, in 1996 a fiscal compromise was negotiated that allowed the central government to retain more of the budgetary benefits of its belt-tightening and to reduce the share of additional tax revenues automatically transferred to the provinces.

*Sources: Tanzi (1995); Porto and Sanginetti (1993); Vega (1995).*
the public-sector deficit. Argentina’s experience (Box 2) exemplifies the difficulties of implementing structural reform when intergovernmental financing is exempted from adjustment. The International Monetary Fund has expressed concern that, in various countries throughout the region, automatic revenue sharing of the magnitude now in effect limits central authorities’ ability to make the structural adjustments that are needed for macroeconomic stabilization.3

**Risks for Intergovernmental Financing**

It is ironic that formula-driven revenue sharing should now be seen as an obstacle to good fiscal management. For many years, the multilateral banks have urged Latin American countries to adopt more transparent, predictable, and stable revenue-sharing and grant systems.4 Formerly, central governments tended to negotiate fiscal transfers on a case-by-case basis. At its worst, this system created incentives for lower-level governments to run budget deficits, since the state or local authorities in the worst financial condition could show the greatest “need” for central-government assistance. Almost everywhere, the system hampered long-term investment and service planning because local governments could not accurately predict their future revenues. The lack of transparency in the grant system exaggerated political factors in resource allocation.

Recent decentralization initiatives have gone far to substitute clearly defined revenue-sharing and grant formulas for ad hoc transfers. The constitutions or basic laws of Argentina, Brazil, Colombia, Venezuela, the countries of Central America, and other nations now contain formulas that establish transfer entitlements. These changes have increased the predictability of local revenues and removed many of the incentives to local fiscal mismanagement.

But the rigidity of formula-driven revenue sharing can add to intergovernmental strain, as happened in Argentina’s fiscal adjustment, for example (see Box 2). And the very certainty and growth of revenue sharing have precipitated a new set of risks. From a central-government perspective they have restricted the flexibility of macroeconomic managers to adjust all parts of the public-sector budget, including intergovernmental transfers, to cope with changing economic conditions or to correct structural imbalances.

Fiscal flexibility has been further reduced by the fact that provincial and local governments often have pledged their future intergovernmental transfers as security for borrowing. In Colombia, once transfer growth was formalized in the 1991 constitution, there followed an explosion of local indebtedness. Municipal debt to banks rose from 494 billion pesos in 1992 to 1,278 billion pesos in 1994; municipal bond issues grew equally rapidly.5 This new level of debt can be serviced adequately by the transfers prescribed in the constitution, but it makes it even more difficult to reduce the speed of transfer growth in the future, if this is deemed necessary. Future revenue-sharing payments represent the only security for much of the local borrowing.

Another kind of fiscal imbalance resulting from decentralized authority has troubled Brazil and Argentina. State governments have been allowed to finance their deficits by borrowing from state banks. Brazilian state and local governments now are estimated to owe $140 billion, mostly to state banks.6 Much of this debt never will be paid. These borrowing arrangements effectively decentralize monetary authority, because states and provinces can borrow from banks they control, without meeting normal commercial standards of creditworthiness or debt repayment. Recent legal changes are supposed to have curtailed these practices in both Argentina and Brazil, but the de facto decentralization of the money supply stands as an extreme example of crippling central government’s control of the economy by ceding the wrong functions to subnational levels of government.

**Risks for Local Government Efficiency**

The efficiency claims for decentralization rest on the presumption that local governments pay for goods having purely local benefits from
local resources. They then must balance the communal gains from expanding services against the costs. This linkage between costs and benefits can be decentralized still further, to the individual consumer, in the form of user charges.

Both user charges and local taxes serve as pricing mechanisms, allowing consumers to buy different kinds or amounts of service depending upon their preferences. Decentralization makes possible a different choice of priorities in each community. User charges are a suitable mechanism for paying for services having private benefits, and where the collection of fees is administratively feasible. Local taxes, imposed on local tax bases, are the appropriate way to pay for local collective goods, which benefit the entire local community but not those outside it. In each case, either the individual citizen or the community collectively must exercise consumer choice within a budget constraint. This process produces a more efficient matching of local services with citizen demand than does central government prescription of local service levels.

Nevertheless, national subsidies still have a role to play in a decentralized financing system. The challenge is to design subsidy supports in a way that reinforces local choice within a budget constraint rather than overrides it. One option is to provide poor households with vouchers that they can use to buy services of their own selection. Chile, for example, provides vouchers for all school-aged children; these can be used to buy schooling from either municipal or private-sector schools. The voucher amount is sufficient to pay for full basic schooling in either sector. Vouchers have been used similarly to help pay for the health-care expenses of lower-income families.

Alternatively, the central government can give grants to local governments to help pay for the cost of providing individual services. A health grant to a municipality can help pay for basic health care; a schooling grant can help pay for basic education. Grant amounts vary according to the number of local services users, but also may take into account the special needs of certain communities or the limited capacity of a community to raise revenues on its own. This approach uses transfers to subsidize the producers of critical local public services rather than the consumers.

General tax and revenue sharing is more difficult to fit into an efficient financing framework. Transfers of this kind support all of a local government’s spending, regardless of whether there is a national interest in the expenditures. It is appropriate to use general revenue sharing to reduce differences in local governments’ general taxing capacity, as a means of equalizing resources across communities. Or it can be justified on the grounds that the central government is a more efficient tax collector than local governments. Central authorities can collect revenues through national taxes, then return the revenues either to the communities where they were generated, or share them among all communities according to formulas that introduce an element of redistribution in favor of poorer communities.

However, once general revenue-sharing transfers become the principal source of local revenues, it becomes difficult to maintain the connection between local services and local costs that lies at the heart of efficient decentralization. Broad-based revenue sharing in Latin America has become such an important element in local budgets that it threatens to sever the linkage between service costs and local service demands.

Even functional transfers can have a similar problem, often bundling a number of different kinds of assistance into a single grant. In Colombia, for example, in addition to general tax sharing, national assistance for education and health are bundled together in the *situido fiscal*, which is distributed according to a complicated set of local needs factors. This makes it difficult to relate intergovernmental transfers to actual service costs.

And from the perspective of linking the funding of services to the services themselves, large increases in unrestricted revenue sharing have been found to *discourage* own-source revenue generation. Studies in Brazil, Colombia, Ecuador, Guatemala, and Mexico, among other countries, have reported a decline in local own-source revenues in the face of increased general purpose grants. Central-government transfers end
up being used to reduce local taxes and user charges, even for services that have purely local benefits and are most efficiently financed at the local level.7

Brazilian municipalities illustrate a situation commonly found in the region. In the 1988 constitution local governments were given more taxing powers and greater control over local tax rates, as well as more revenue-sharing entitlements. Two new local taxes were established—a tax on property sales and a retail sales tax on fuels. Local governments have the freedom to set local property-tax rates and can establish discretionary user fees over a broad range of services. They also can levy betterment taxes to finance capital improvements. In practice, however, Brazilian municipalities have made meager use of their taxing authority. Property taxes are imposed at very low rates; even then, collection is spotty. User fees hardly figure in local budgets; they account for only 3.7 percent of total revenues in capital cities. Betterment taxes, an ideal mechanism for financing medium-sized capital projects, are very rarely used. Instead, the share of transfer revenues in local budgets has increased.8

Elsewhere the same behavior can be found. Venezuelan municipalities have flexibility of rate setting over the two most important local sources of revenue, the business tax and the property tax. They also can set user-fee levels. Despite this flexibility, local governments in Venezuela collect an insignificant 3 percent of total public-sector revenues. In Mexico, municipalities have proved reluctant to ask states for the authority to levy property taxes and set property tax rates, even though local control is provided for by law. Throughout the region municipal authorities have tended to resist increasing water fees to levels adequate for cost recovery.

In short, local governments tend to prefer “free” central transfers to the politically costly course of raising own-source revenues. The political appeal of avoiding local taxes is obvious. But municipalities’ unwillingness to pay for their own expenditures leaves them with less control over their budgets—and makes them vulnerable to changes in central-government grant policy.

The aversion to local self-financing, however, may be beginning to disappear. As municipalities face the reality of strong citizen demand for services, they have proved willing to raise the revenues to pay for them—especially in larger and wealthier cities. In Mexico, a new political administration in León, considered a leader in citizen responsiveness, negotiated the transfer of property tax authority to the city from the state, then nearly quadrupled property tax receipts between 1988 and 1991.9 Mid-sized and economically prosperous cities in Colombia likewise have substantially raised local tax collections as a result of decentralization, even in the face of larger central-government transfers.10 Table 2 illustrates the rapid growth of own-source revenues in Mexico City, partly necessitated by central-government fiscal pressures that led to reductions in the growth of revenue sharing and central transfers. As these pressures become more widespread, municipalities will be obliged to raise own-source revenues if they wish to satisfy citizen service demands.

Of course, own-source revenue generation is more feasible for cities possessing strong tax bases than for small and poor communities. For the latter, access to nationally collected revenues will have to remain a large part of any realistic strategy for financing local budgets. Even in these communities, however, the linkage between services received and local taxes or fees paid can be strengthened by requiring local participation in covering service costs.

### The Assignment of Functions

Fiscal decentralization requires clarity of functional assignments among the levels of government, as much as clarity of revenue distribu-

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<tr>
<th>Table 2</th>
<th>Changes in Local Resource Mobilization, Mexico City Federal District</th>
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<tbody>
<tr>
<td>Item</td>
<td></td>
</tr>
<tr>
<td>Own-Source Income</td>
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</tr>
<tr>
<td>Revenue Sharing</td>
<td>60%</td>
</tr>
<tr>
<td>Central Transfers</td>
<td>15%</td>
</tr>
<tr>
<td>Debt Financing</td>
<td>9%</td>
</tr>
</tbody>
</table>

tion. The greatest controversies in implementing decentralization have arisen when national laws leave functional responsibilities unclear, or assign the same functions to more than one level of government. Both Mexico and Brazil, for example, have relied on so-called “common competencies”—functions that can be carried out by municipalities or by states or sometimes by the federal government. On occasion this approach has permitted innovative collaborations to spring up, as state and local authorities work out their own forms of cooperation in the field. At other times, however, it has produced vacuums in service coverage when no governmental authority wants to accept service responsibility, or collisions in policy when overlapping levels of government operate separately designed programs in the same field.

Under fiscal stress, it is tempting for any level of government to walk away from costly service provision. Without a clear assignment of service responsibilities, withdrawal is easier. In both Brazil and Mexico, state governments have sometimes unilaterally suspended service activities, asserting that municipalities will have to use their own resources to provide these services if they want them to continue.

Emerging Lessons for Better Implementation

In their haste to begin the task of decentralization, countries often have constructed fiscal frameworks they later discovered, through experience, did not fully serve their purposes. In fact, among central-government fiscal managers there has developed something of a backlash against decentralization initiatives, on the grounds that these have curtailed central authorities’ ability to carry out fiscal restructuring. These have curtailed central authorities’ ability to carry out fiscal restructuring.

• There is a trade-off between the fiscal framework that works best for macroeconomic management and the framework that works best for municipal or provincial management. Macroeconomic managers do not want to be locked into large revenue-sharing or other financial commitments that restrict their ability to shape fiscal policy for the entire public sector. Local government managers want a stable, predictable, and transparent intergovernmental financing system that is not subject to the central government’s unilateral change. These potentially conflicting goals have to be reconciled as far as possible in designing revenue-transfer systems.

• The fiscal risks from decentralization are greatest under an unbalanced financing strategy that creates large windfall gains and losses. A fiscally neutral policy that matches revenue transfers with service responsibilities goes far to “sterilize” decentralization’s macroeconomic impact. Unbalanced fiscal decentralization—where centrally financed revenue sharing greatly exceeds the costs of the services being transferred to local control—not only creates central-government budget problems but promotes inefficiency in local service delivery. Constitutional commitments to future revenue-sharing levels need to ensure that spending from central budgets can realistically be reduced at the speed necessary to make room for the increased transfers being promised.

• There must be controls over subnational indebtedness. Debt discipline can be exerted by the credit market if subnational authorities borrow from private financial institutions. Or it can be exerted by central-government regulation. (In Chile, municipal governments cannot incur debt, forcing capital spending to be financed from central-level grants, local current-account savings, or private-sector firms’ investing in “public” infrastructure.) Debt discipline is subverted when state or local authorities are able to borrow from decentralized public financial institutions under their control, without being obliged to meet market standards of creditworthiness.

• Decentralization of local fiscal control has lagged behind the sharing of revenues and should be accelerated. The greatest promise of decentralization lies in local authorities’ making their own decisions about both the revenue and expenditure sides of the budget. Central authorities until very recently have been reluctant to cede control over matters like local tax rates and local fees schedules, or to broaden the menu of taxes from which sub-
national authorities can choose. Local governments have been reluctant to ask for more fiscal independence—or to exercise the revenue-raising options now available to them—preferring the security of central transfers. Realization of the full promise of decentralization will require greater use of own-source revenues, especially in larger municipalities with adequate tax potential. Municipal self-financing through user fees and local taxes has the additional advantage of being entirely neutral with respect to central-government fiscal policy.

- **Finance should follow function.** If the architects of the most recent round of decentralization in Latin America were to start anew, they probably would give more attention from the beginning to the assignment of functions. Local governments have a comparative advantage in providing certain kinds of services—based on the qualifications of municipal personnel, the special goals for decentralization in each country, and the importance of bringing service management closer to the people. Once there is agreement on which functions should be transferred to the local (or state) level, the cost of these functions can be calculated. Then revenues (or revenue-raising capacity) can be transferred to pay for them. This process is the reverse of that followed in many Latin American countries, where revenues have been devolved first; then a search has been initiated for expenditure functions that can be transferred to absorb the revenues.

Of course, the decentralization process cannot be restarted. However, as intergovernmental sorting-out moves ahead, there will be opportunities for restoring equilibrium. The first question always to ask is: Can this function be most effectively performed at the local, state, or national level? Answering that question will allow countries to adjust financing arrangements accordingly.
PROPONENTS OF DECENTRALIZATION OFTEN SAY they want to shift government authority “closer to the people.” The expression is not without its ambiguities. Political scientist Morton Grodzins once considered six different meanings that “closer to the people” had been asked to bear in political writings. He concluded that, under all of the meanings, the proposition that local government automatically is closer to the people in the way it functions is impossible to verify.14

Decentralization only provides a framework for governance. It cannot guarantee more effective citizen participation in civic life or higher standards of public accountability. To incorporate the voice of the citizenry, decentralization has to be supplemented by other types of institutional reforms. Fortunately, throughout Latin America there are now numerous examples of how decentralized government is giving specific meaning to the phrase “closer to the people”—and in the process becoming more effective.

ELECTED LOCAL REPRESENTATION

One of the most fundamental transformations in local governance has involved the strengthening of elected leadership. The spread of democratic elections in Latin America has been largely from the top down. Elected civilian regimes were first instituted at the national level. Only later did local voting for mayors and councils take root, typically as part of the decentralization process.15 Table 3 illustrates how recently local democratic elections were established (or, often, re-established) in selected countries of the region.

By the middle of 1996, elected mayors headed local governments virtually everywhere in Latin America. The only exceptions were Mexico City (where elections are scheduled for 1997), Costa Rica (where elected city councils appoint city managers as chief executives), and a few rural regions where indigenous peoples have retained traditional forms of selecting their leaders.

Elections are a fundamental tool that the citizenry can use to choose leaders and to hold
them accountable for performance in office. However, not all electoral systems are equally effective in strengthening public accountability. Countries in the region are gradually modifying their voting methods, both to sharpen voter control over officeholders and to give mayors a better chance to establish a track record of performance that voters can judge.

Direct, popular election of mayors has now largely replaced the former practice of indirect election of mayors by city council members from among their number (see Table 3). Indirect election of mayors tended to perpetuate the strength of political insiders, who often were more accountable to their party hierarchy than to the public at large.

Another step in sharpening local accountability has been to separate voting for local officials from voting for national representatives. In Latin America, when citizens have been asked to vote for candidates at all levels on a combined ballot, local issues have tended to be overwhelmed by national or state issues and by contests between national political parties. This tendency was reinforced in some countries by the requirement that voters support the same party’s slate at the local and national level. In separate municipal elections, voters must focus on local matters, such as the performance of a mayor in office or the specific platform of reform of a mayoral candidate. Now combined local and national ballots are becoming rare. In fact, it is increasingly common to find large municipalities governed by opposition parties that do not hold office at the national or state level. In some places, local civic groups have put together candidate slates to run for office without national party affiliation. All of these changes have strengthened the ability of local election campaigns to identify and resolve, through voting, major choices about municipal priorities.

The concept of accountability through voting also can be reinforced by lengthening mayors’ terms of office. Short terms of office do not allow mayors to establish a track record to put before the voters. Bolivia is an example of a country that has extended the mayoral term of office as part of an effort to strengthen accountability. It found that the previous mayoral period—two years—was too brief a period to allow a new mayor to become familiar with government, enact a program, and campaign for reelection on the results of that program. The mayoral term was lengthened to five years at the same time the country adopted direct elections.

Likewise, accountability could be improved by eliminating prohibitions against mayoral reelection. The prohibitions against re-election originally were intended to prevent local regimes from entrenching themselves in power, but they also have prevented voters from renewing the mandates of mayors who perform well.

Table 4 compares some of the features of local electoral systems as of early 1996. The voting structure by itself cannot guarantee that local government will be responsive to the people, but most of the changes that have been made have been designed to give mayors a stronger and better defined popular mandate.

The election of council members is more problematic. Voting for councilors often is still by blocked party lists. That is, voters must vote a straight party line; they cannot divide their votes between candidates of different parties. Voting often is also by closed list. That is, each party

<table>
<thead>
<tr>
<th>Table 3</th>
<th>Election of Mayors</th>
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<tbody>
<tr>
<td>Year Local Elections Established or Resumed</td>
<td>Popular or Indirect Election (Year indicates date of last change)</td>
</tr>
<tr>
<td>Country</td>
<td>1983b</td>
</tr>
<tr>
<td>Bolivia</td>
<td>1992</td>
</tr>
<tr>
<td>Chile</td>
<td>1988</td>
</tr>
<tr>
<td>Colombia</td>
<td>1978</td>
</tr>
<tr>
<td>Ecuador</td>
<td>1990</td>
</tr>
<tr>
<td>Nicaragua</td>
<td>1991</td>
</tr>
<tr>
<td>Panama</td>
<td>1990</td>
</tr>
<tr>
<td>Paraguay</td>
<td>1990</td>
</tr>
<tr>
<td>Peru</td>
<td>1993</td>
</tr>
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*Except Buenos Aires. The first mayoral elections were held in Buenos Aires in 1996.

bLegislation has been proposed for direct election of mayors in Chile.

cCities over 100,000 population and those that are provincial capitals have direct elections. Others have indirect elections of mayors.
ranks its candidates, determining who will sit on the council at different levels of total voting support; a voter cannot single out individual candidates to vote for. This practice tends to obscure voter accountability in the municipal council. Although under such a system voters theoretically could hold parties, rather than individuals, accountable, in Latin America the result has been the creation of party machines, where lifetime politicians get ahead by being accountable only to the party apparatus, not to the electorate. The weak public mandate of councilors appears to have contributed to generally weak oversight by councils of the local executive branch. As a result, strong mayors having individual identities before the electorate commonly dominate municipal authority. The Mexicans term this local balance of power “presidencialismo.”

The practical significance of popular elections depends on communities’ willingness to use voting as a stimulus to more comprehensive change. In Colombia, the combination of popular elections and greater local budget responsibilities has brought a new kind of mayor into politics. A national survey of mayors conducted in 1994 found that 52 percent had university degrees. More than half (53 percent) had worked in the private sector immediately before taking office, and most of the rest had private-sector work histories. This private-sector experience contributed to a much stronger consumer orientation in the conduct of municipal affairs. Similarly, in Northern Mexico, where party competition has been introduced into mayoral elections, a large proportion of newly elected mayors have private-sector management experience. These mayors have been assertive in introducing the idea of a more entrepreneurial, self-reliant city.

Innovations in electoral accountability stretch beyond Election Day. The new generation of mayors has found a variety of ways to stay in contact with voters between elections. Many issue quarterly or more frequent reports on the progress made in implementing their campaign promises, or hold open sessions where citizens can comment on public services and other matters. Municipal budgets have become public documents. A number of mayors routinely conduct public opinion polling to uncover citizen service and investment priorities.

**CABILDOS ABIERTOS AND OTHER PUBLIC MEETINGS**

As important as local elections have been to developing democratic accountability in the region, periodic mass voting is a blunt instrument for expressing the popular will on con-

<table>
<thead>
<tr>
<th>Table 4</th>
<th>Selected Features of Local Electoral Systems</th>
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<tbody>
<tr>
<td></td>
<td>Mayoral Term of Office (Years)</td>
</tr>
<tr>
<td>Argentina</td>
<td>4</td>
</tr>
<tr>
<td>Bolivia</td>
<td>5</td>
</tr>
<tr>
<td>Brazil</td>
<td>5</td>
</tr>
<tr>
<td>Chile</td>
<td>4</td>
</tr>
<tr>
<td>Colombia</td>
<td>3</td>
</tr>
<tr>
<td>Ecuador</td>
<td>4</td>
</tr>
<tr>
<td>Guatemala</td>
<td>3</td>
</tr>
<tr>
<td>Honduras</td>
<td>4</td>
</tr>
<tr>
<td>Mexico</td>
<td>3</td>
</tr>
<tr>
<td>Panama</td>
<td>6</td>
</tr>
<tr>
<td>Peru</td>
<td>3</td>
</tr>
<tr>
<td>Venezuela</td>
<td>3</td>
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*Guatemala City has a four year term of office.

concrete issues. For this reason, public authorities have introduced a number of practices that allow for more extensive consultation with the public.

Several countries—especially those in Central America—have revived the practice of open town meetings or cabildos abiertos. For example, El Salvador’s 1986 revision of the municipal code and Honduras’ 1990 municipal law both require that all towns hold regular cabildos abiertos to discuss community priorities.

One of the few empirical studies of how mayors and citizens view these institutions was recently conducted in El Salvador. Citizens viewed the town meetings as valuable opportunities to express their requests for public works projects. They considered the town meetings to be open to all and attendance to be representative of the community. However, they complained that the cabildos abiertos were used only to identify project requests. Citizens were not allowed to participate in actual project selection. Nor was there public discussion of broader development plans.

Mayors revealed a more negative attitude toward the cabildos abiertos. They did not see the meetings as beneficial and actively resisted citizen involvement in the priority-setting process. Mayors said that they did not feel the cabildos abiertos were useful settings for discussing project costs and did not believe it was possible to deny project requests in a public setting. Mayors as a whole did not convene the number of meetings (five per year) that they were required to hold according to the municipal law.

The survey’s findings are consistent with impressions of other types of large meetings held to gather citizen “demand” for neighborhood public works projects. Meetings of this type often have been held in conjunction with the operations of Social Investment Funds. They almost inevitably produce a one-way flow of information. Citizens are able to voice their views on project needs, but they do not have adequate access to cost or budget information to truly participate in priority setting. It is rarely clear how public officials translate the voice of the community expressed in this manner into a list of projects to be financed.

Municipal Partnership with Community Organizations

Latin America has a rich fabric of community and grassroots organizations. These range from neighborhood and block associations to mothers’ committees, workers’ organizations, and school associations. A tradition of self-help flourishes among these associations, but cooperation with municipal government has not always been easy. Many of the community groups were formed during periods of military rule. They have had a history either of opposition to government or of solving community problems outside the formal framework of government.

The democratization of municipal government has produced numerous attempts to increase civic participation by coordinating the activities of community groups with those of the municipality. These efforts are illustrated in Boxes 3–5. From this experience it is clear that successful collaboration between municipal government and community organizations requires ceding real power over resources. Citizen “advisory committees” are not highly valued by the population. Effective popular participation with local government has been organized mostly around public works projects that bring immediate benefits to participants, and around a process that allows participation in budget allocation (Boxes 3 and 4).

Simple and clearly understood rules are required to establish how community groups’ priorities will be translated into government’s resource decisions. The entire process needs to move forward swiftly. Civic participation of this kind is self-reinforcing, because citizens quickly see the products of their effort. Otherwise, citizen engagement can itself become a bureaucratic process.

One of the most comprehensive efforts at organizing civic participation is in León, Mexico, under the Sistema de Organización Ciudadana. The city set up 19 different citizen councils, ranging from the Council on Culture to the Council on Neighborhoods and Settlements. The city formally recognized 200 different settlement committees, each of which elected 12 officers.
Participatory Budgeting in Brazil

The left-wing Partido do Trabalhadores (PT) came to power in a number of Brazilian municipalities in the mid-1980s. It sponsored a political platform that expanded the powers of neighborhood associations, proposing to use them as the base for "popular councils" with budgetary authority. This goal for increased public participation in government came into conflict with the formal powers of traditional municipal institutions, giving rise to considerable tension. Between 1988 and 1992, 12 of the 36 PT mayors split with their own party, partly over the issue of how much authority should reside in the municipal executive relative to the new participatory bodies. Efforts to carve out a formal role for community organizations in approving municipal budgets initially failed, even in the largest PT-controlled cities such as Sao Paulo and Porto Alegre.

Over time, however, the popular councils in some cities acquired a large practical role in budget preparation. In the city of Itabuna (pop. 280,000) neighborhoods were grouped into seven regions. The mayor and his staff hold one or more public meetings per year in each region, at which they present the city's budget, including both recurrent and capital expenses, portrayed on large poster boards. The meeting focuses on how to invest the amount budgeted for capital expenses. The organizers explain what is realistically achievable with the resources available and indicate that the preferences of each neighborhood will be weighted with those of other neighborhoods to reach a ranking of priorities. Based on these sessions, the technical staff devises an investment program. The mayor and staff then hold a citywide meeting to present the capital budget results, this time to a council of representatives elected from each neighborhood region. The council's job is to monitor the city's efforts to implement the budget decisions.

Participatory budgeting in Itabuna resulted in a large shift of investment resources toward water and sanitation, the top priorities expressed by citizens. Similar methods of community consultation over capital priorities have been adopted in Porto Alegre.

Sources: Assis (1993); Campbell (1995); Nickson (1995).

A more direct process of citizen participation and one that moves swiftly—60 days from start to finish—is illustrated in Box 4. The capital budgeting and planning process in La Florida, Chile, assigns citizen groups direct responsibility for choosing neighborhood-scale public works projects as well as larger, sectional projects.

A different kind of partnership between municipal governments and community organizations is represented by Bolivia's Popular Participation Law (Box 5). Here, the principal linkage is one of municipal accountability to the community. The law, which took effect in 1994, has translated the general concept of accountability, which almost always receives lip service in decentralization initiatives, into a well defined, formal structure. As with the capital budgeting process in La Florida, a large part of the law's
La Florida, Chile: A Partnership with Community Groups in Capital Planning and Budgeting

While has some 335,000 legally recognized community organizations. They are groups with strong local roots, whose presence in the community long preceded the restoration of municipal democracy. La Florida, in the Greater Santiago metropolitan region, has developed a formal mechanism for incorporating these groups into the municipality's capital budgeting process. There are more than 1,000 community organizations in La Florida alone.

At the start of the budget cycle, the municipality convenes a large assembly of all the legally registered community organizations. The capital budget is organized around 16 geographic neighborhoods and four sectors. The municipal government establishes an overall investment ceiling. Besides this global budget constraint, community groups are given a catalog of per-unit costs for capital works—e.g., the cost per square meter of road paving, or the cost per traffic signal. They are then asked to consult with citizens, negotiate with other organizations, and propose a capital project list for their neighborhood or sector.

The community groups have 60 days to consult with the citizenry on project priorities. Then there is a final assembly, which representatives of all the community groups attend, to come to a consensus on the projects that will go into La Florida's capital budget, subject to the global budget constraint. If a consensus cannot be reached, the mayor makes the final decision—a prospect that promotes compromise. Some of the projects on the final list are built by the municipality, some by community organizations, and some by the private sector under contract with the municipality.

In this process, community groups exercise real decision-making power. However, they are required to recognize and accept the global budget ceiling. The system is designed from the outset to force community organizations to make realistic investment demands, by fitting their project lists within the budget constraint, by acknowledging the true unit costs of different types of projects, and by facing up to the trade-offs between competing neighborhoods.

Effectiveness is due to the clarity with which it assigns roles to different parties and to the fact that these roles are formally recognized, in this case in national legislation.

Referendums

Some municipal investments cannot be delegated to the community level. Major investments in trunk infrastructure, like main water distribution lines or principal roads, for example, are likely to affect the entire municipality. Citizens may have to express their demand for these investments through other means than consultation with community organizations.

A few mayors have held referendums to obtain citizen guidance on such investment decisions. A referendum allows individuals to vote on single-issue questions of public concern. In Switzerland and some parts of the United States, referendums are used to decide everything from property tax rates for local school financing to bond issuance to pay for economic development projects or policy matters such as the continuation of local rent control.

Within Latin America, only Chile recognizes referendums as legally binding methods of reaching decisions about public expenditures. At least 50 percent of eligible voters must participate in a referendum for it to have legal validity. Elsewhere, for the most part, mayors have used referendums as advisory tools to gather public opinion and to focus public attention on major policy choices. The mayor of Tijuana, Mexico,
constructed a referendum around a proposed program of road construction, road replacement, and drainage. The ballot question proposed a specific way to pay for the investment package. Individual tax shares were established, in part according to the amount of direct benefit each individual received from the projects. The combined investment and cost-sharing plan was submitted to the electorate. Though the vote was not legally binding, the city used public approval (64 percent voted “yes”) as a demonstration of popular support in its effort to obtain authorization of bond issuance from the state.

The mayor of Las Condes, Chile, used a similar citywide referendum to gain public approval of a user-fee system to pay for investment in new highways and interchanges. Because the party in power locally was part of the national opposition, the mayor used the referendum to show national authorities there was public support for the investment strategy.

In countries that have a long tradition of using referendums as instruments for public choice, propositions can be placed on the ballot by any group that obtains a sufficient number of signatures. Often, these groups are opposed to current municipal policy. In Latin America, however, mayors are the only ones so far to have initiated referendums—to heighten public awareness of issues and obtain a clear mandate for action that the mayors favor. Nonetheless, the submission to the electorate of clear investment proposals, accompanied by clear price tags, is part of a new style of governance that is more transparent and accountable.

**Do Citizens Trust Municipal Governments To Set Priorities?**

In the end, the best indication of whether decentralization has moved government “closer to the people” is the trust citizens place in municipal authorities.

**BOX 5**

**Bolivia: Community Oversight of Municipalities**

Olivia's Popular Participation Law creates new community organizations—organizaciones territoriales de base—that are expressly assigned the role of proposing, controlling, and supervising local investment projects and the provision of public services according to the needs of the community in the areas of education, health, basic sanitation, local roads, and urban and rural development. All of these functions have become local government responsibilities.

The law endows municipalities with new tax-sharing revenues for meeting the investment priorities designated by community organizations, and stipulates that 90 percent of these resources must be used directly for community investments. The community organizations also serve as oversight committees—comités de vigilancia—to oversee municipal budget expenditures, supervise construction progress on works, and to monitor the quality of service delivery by municipal service entities.

If investment resources are not spent as programmed by the community, or works are not completed or financed within budget, the law empowers the community organizations to lodge complaints with a special office in the executive branch and, through it, with the Senate. If the complaints are found valid and not remedied, a municipality may lose its tax-sharing revenues.

As of mid-1995, roughly 5 percent of the complaints filed by vigilance committees had been found valid. In two cases, towns' revenue-sharing entitlements were cut.

Table 5
Whom Do You Trust More?
(Opinion survey of total of 1,900 respondents in Colombia)

<table>
<thead>
<tr>
<th>Municipality</th>
<th>Manizales</th>
<th>Valledupar</th>
<th>Ipiales</th>
<th>Zipaquira</th>
</tr>
</thead>
<tbody>
<tr>
<td>National Government</td>
<td>8%</td>
<td>6%</td>
<td>27%</td>
<td>43%</td>
</tr>
<tr>
<td></td>
<td>92%</td>
<td>94%</td>
<td>73%</td>
<td>57%</td>
</tr>
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</table>


Not surprisingly, there is no uniform answer to the question of whether citizens trust municipal governments to make spending choices on their behalf. There are, however, fragmentary signs that are encouraging. Citizen surveys in four Colombian cities, conducted after decentralization, found that an overwhelming majority of respondents trusted local government to a greater degree than national government (see Table 5).

By contrast, the 1,034 respondents to a similar survey in El Salvador in 1994 did not feel especially “close” to their municipal governments. In terms of citizen trust, municipal governments ranked ahead of the national government but below religious institutions and community organizations (though far ahead of labor unions and political parties). Three-fourths of the respondents reported that they saw little or no opportunity to participate in local government. Fully 85 percent knew of few if any attempts by the municipal council to obtain community input.

These differences in citizen confidence in municipal government correspond with differences between El Salvador and Colombia in the extent to which municipal institutions have been opened to citizen participation, and they suggest that local citizens are discerning customers when it comes to evaluating different “models” of decentralization.

Emerging Lessons for Better Implementation

Citizen participation sometimes can appear to be a soft goal, not as specific or measurable as better service coverage or better budget management. However, it pays off in greater trust in local government and appears to be closely correlated, in citizens’ views, with local service quality.

- Voting is the most basic act of citizen participation. The separation of local from national elections, the increase in the length of mayoral terms, and the adoption of direct election of mayors are all reforms that have made mayors more accountable to the electorate. Similar reforms to increase the accountability to municipal councils are needed. Without them, councils are likely to remain relatively weak institutions, poorly equipped to exercise oversight over strong mayors.

- Direct citizen participation requires that citizens have clear information regarding the municipal budget and service costs, and that they participate in actual budget choices. In the absence of a cost constraint, citizen preferences about service supply or investment priorities are scarcely worth gathering. Sharing budget and cost data implies a willingness on the part of public authorities to surrender exclusive control of key information. It therefore has symbolic importance for citizen participation in decision-making, as well as practical utility for improving the quality of choices. In the most effective models of citizen participation, citizen groups actually make choices about how limited budget resources will be allocated.

- There are benefits to formal structures that clearly spell out the roles citizens and community organizations should play in collaborating with municipal government. Transparency and predictability are nowhere more important than in defining the processes that will be followed in community participation. A clear, stable set of rules allows participants to learn from experience, and to apply that experience in the future. Without well-defined rules, there always is the possibility that government institutions will “consult” with the
public only so long as they obtain the answers they want.

- **Citizens expect concrete results from participation, especially a greater say in neighborhood capital projects.** They have limited tolerance for longer-term planning or “policy” discussions. Initial participation strategies have been most successful when they focus on selecting, building, and financing local public works. The experience gained in this kind of collective decision-making may provide the groundwork for broader community involvement in service delivery at a subsequent stage.

- **Mayors looking for innovative ideas on how to generate citizen participation do not have to look outside Latin America for relevant experience.** A wide variety of techniques for capturing public service demands have already been tried in the region, and the region is compiling a vast empirical record on how to incorporate citizen participation and citizen choice into decentralization. It will be valuable to monitor closely how citizens feel these different approaches have succeeded and whether it is possible to transplant promising innovations from one part of the region to another.
A TRANSFER OF SERVICE RESPONSIBILITIES to local authorities will make citizens better off only if local governments are capable—or swiftly become capable—of delivering services effectively. Fear that municipalities will not be able to perform the functions assigned to them has become the principal roadblock to moving ahead with decentralization plans.

Municipalities do not have to achieve unreasonably high performance standards to justify decentralization. Frustration with national service providers has made citizens willing to try new arrangements. Early indications of municipal performance are encouraging. A survey of four cities in Colombia, for example, found that most citizens believed public services had improved as a result of decentralization, though there clearly were differences in the degree of enthusiasm (Table 6). Objective measures of service quality (like the degree of household coverage, frequency of service interruption, etc.) confirmed that on balance decentralization had improved water supply, sewerage, road maintenance, and education in these municipalities and in others that were studied.

Central authorities can improve the chances of successful decentralization by phasing in the transfer of service responsibilities. The contrast between Colombia’s first efforts at decentralization and its subsequent strategy is instructive. Colombia initially attempted to transfer entire blocks of functions to large numbers of municipalities. For example, between late 1987 and January 1, 1989, almost 1,000 water and sewerage systems were turned over to local governments. Department-level institutions were supposed to assist in the transition by providing technical assistance, but they were not equipped to do so.

In subsequent decentralization planning, Colombia has moved more slowly. Municipalities and departments must demonstrate that they are ready to administer new functions before a transfer takes place. In the health sector, a five-year timetable was adopted for devolution, with responsibilities transferred first to the largest municipalities with the best-developed local
Only after these transfers were digested did devolution move on to smaller localities. This gradual approach has reduced the risk of spectacular failures that would turn the population against decentralization in general. It also provides an opportunity to adjust later rounds of devolution in light of initial experience.

One consequence of this step-by-step decentralization, however, is that functional responsibilities do not get devolved to the local level as fast as revenues must be transferred under the schedule established in the constitution. A cautious attitude toward municipal service capacity can exacerbate the central government's fiscal imbalance, by leading it to retain service responsibilities even in the face of mandated revenue transfers.

**Strengthening Municipal Service Capacity**

Two broad strategies have dominated efforts to upgrade municipal capacity for service delivery. One strategy seeks to strengthen the skills of municipal workers, to improve municipal management methods, and to reduce the turnover of trained employees. This strategy tries to address the capacity gap directly. It is typically implemented through technical assistance and training programs for local governments.

The second strategy seeks to build into the municipal service delivery system more opportunities for citizen feedback and control, as well as financial incentives for good service performance. This approach tries to create a framework of service accountability—arguing that once municipalities feel financial and voter pressure for improving service quality, they will find ways on their own to upgrade their staffs or take other steps necessary for service improvement.

The two strategies sometimes are presented as alternatives, but they in fact closely complement each other. Skill-training often is wasted unless reinforced by a system that makes municipalities want to use the newly acquired skills in service delivery. On the other hand, municipalities that lack the technical ability to deliver services can squander resources and exhaust citizen good will, no matter how attentively they listen to citizen service demands.

**Professionalization of Municipal Staffs**

Traditionally, municipal work forces in Latin America have been “bottom-weighted” with large numbers of unskilled workers.

One of the most encouraging results of decentralization has been a transformation in many countries of the character of the municipal work force. The size of technical and professional staffs has grown rapidly. The number of unskilled workers has shrunk. Unskilled workers have been cut partly because municipalities have found it more efficient to contract out work like construction or street cleaning than to maintain a permanent work force for this purpose. The changing skill mix also reflects municipalities' acceptance of cost-effective service delivery as their primary mission. This contrasts with the past, when local governments often saw themselves as employers of last resort and appealed for political support as much through job provision as through service delivery. This tradition continues in some parts of the region, but is gradually being displaced by a model that emphasizes

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**Table 6**

<table>
<thead>
<tr>
<th></th>
<th>Manizales</th>
<th>Valledupar</th>
<th>Ipiales</th>
<th>Zipaquira</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improved</td>
<td>73%</td>
<td>78%</td>
<td>53%</td>
<td>31%</td>
</tr>
<tr>
<td>Stayed the same</td>
<td>25%</td>
<td>20%</td>
<td>36%</td>
<td>49%</td>
</tr>
<tr>
<td>Worsened</td>
<td>2%</td>
<td>2%</td>
<td>11%</td>
<td>20%</td>
</tr>
</tbody>
</table>

*Source: Fiszbein (1995).*
competence in service delivery at reasonable cost. Local governments are becoming more responsive to citizens as “consumers” who want cost-effective services.

Table 7 demonstrates the profound changes made in the composition of the municipal work force in Chile and Colombia during the period of service decentralization. Municipal governments are reshaping themselves to operate with leaner, more flexible, and more skilled labor forces. The number of municipal workers per 1,000 residents in these countries contrasts sharply with the ratios found in Brazil or Argentina, where local service delivery rationalization has been less well defined.

<table>
<thead>
<tr>
<th>Table 7</th>
<th>Changes in Structure of Municipal Work Forces*</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Ratio of Total Workers to Professional and Technical Staff</td>
</tr>
<tr>
<td>Chile</td>
<td>12.7</td>
</tr>
<tr>
<td>Colombia</td>
<td>39.2</td>
</tr>
<tr>
<td>Argentina</td>
<td>N.A.</td>
</tr>
</tbody>
</table>

*Excludes school and health workers transferred from central authorities as part of decentralization.


Upgrading Output Expectations of Local Public Employees

Technical skills are not the only requirement of a cost-effective municipal work force. Of at least equal importance is a management style that imbues workers at all skill levels with a sense of mission and the desire to produce results. This commitment can be encouraged by stressing outputs in service delivery and by devices as simple as regular recognition of employees or service units that produce the best results. Box 6 illustrates a way of bringing health workers “closer to the people” and encouraging them to take more responsibility for the results of their work. In this case, it was a state government agency that assumed the initiative—sometimes in the face of municipal government opposition—again illustrating that it is the style of service delivery, more than the formal status of the service delivery organization, that distinguishes effective decentralization.

Stability in the Public Work Force

Organizations striving to upgrade municipal service performance regularly struggle with a trade-off between giving public workers greater job stability and making them more responsive to elected leadership. Historically, it has been common for newly elected municipal administrations to dismiss large numbers of workers from the municipal payroll, especially when a change of party is involved. A new administration has its own set of party loyalists to reward when it comes to power.

High turnover rates often have been identified as a critical point of weakness in municipal governance. Municipal training may seem pointless in this environment. One follow-up study of 300 municipal workers who had received specialized training in tax and financial administration found that only 67, slightly more than 20 percent, still worked for the municipality three and four years later.24 Some of those who left were dismissed when a new mayor was elected. Others chose to use their newly acquired skills in higher paying jobs in the private sector.

Turnover can be tackled in a variety of ways. One option, broadly debated throughout the region, is to create a civil service system that covers subnational workers. A civil service system establishes career tracks of professional advancement and prohibits dismissal from office for political reasons except for top management positions. Both Brazil and Colombia have extended civil service coverage to municipal employees.

During periods of political reform, however, an entrenched public labor force protected by law from removal can be at least as great a threat to
Worker Implementation of the Ceará (Brazil) Preventive Health Program

Ceará is one of the poorest states of Brazil, situated in the arid Northeast. In the late 1980s and early 1990s Ceará implemented a program of child immunization, prenatal care, and infant care that succeeded in reducing infant death rates from 102 per 1,000—one of the highest rates in Latin America—to 65 per 1,000. The program won the 1993 UNICEF Maurice Paté prize for child support programs in worldwide competition.

These results were achieved by 7,400 unskilled workers serving as local health agents, paid at minimum wages. Health agents visited 70 percent of the homes in the state, transforming infant care practices. The state managers of the program recruited health agents in each town. Though there were no formal schooling requirements, they emphasized that the job was highly competitive and that agents would be selected for the job based on their leadership potential and their commitment to the program’s success. The entire hiring process was merit-based, and position of health agent became prestigious in rural towns, despite the low pay relative to other public-sector jobs.

Workers did not receive job tenure, as is customary for public employees in Brazil. Instead, they were hired as “temporary” workers, whose continued employment would depend upon performance. Workers were given the flexibility to work outside of rigid rules, being free to identify and tackle other public health issues in their communities like environmental hazards, or to identify on their own the methods that would be most effective in helping poor mothers improve child care. All workers lived in the communities where they worked.

The expectation of high-quality work and worker commitment set the program apart from traditional public employment. So did the continuing reinforcement provided by program managers in the form of frequent awards for individuals and program teams that achieved reductions in infant mortality.


Effective service delivery as a work force plagued by high turnover. Brazil has periodically tried to improve the cost-effectiveness of government, and to reduce the fiscal deficit, by reducing the size of state and local work forces and introducing performance standards for employees. However, these initiatives have been hampered by the constitutional prohibition against sacking civil servants at any level. The constitutional protections have made it virtually impossible to cut labor costs, even as payrolls escalate to the point of squeezing out investment and other expenditures.

The complexity of Brazil’s civil service rules, as well as the political sensitivity of modifying them, are revealed by the tentative agreement reached in the fall of 1995 by the congressional committee charged with considering civil service reform (Box 7). But the issue has defied resolution, and no final agreement on civil service reform proposals had been reached by the time of this writing. Although civil service rigidities may be most extreme in Brazil, municipalities elsewhere in the region have found that national rules governing selection and management of school personnel, for example, can severely restrict local ability to reform service delivery. A decentralization plan that devolves budgetary and formal service responsibility to the local level but retains control of personnel decisions at the center is almost certain to produce frustration. No level of government then has the flexibility to respond to customer demands.

Accountability and Service Delivery

The technical capacity of municipalities to provide services has to be supplemented by a
BOX 7

Proposed Civil Service Compromise (Brazil)

Brazil’s 1988 constitution bans firing government employees at all levels once they have been employed for two years. The measures were adopted out of fear that politicians would abuse the right to appoint and dismiss workers whenever there was a change of administration.

However, the inability to dismiss workers, coupled with generous pension benefits tied to years of service (100 percent salary replacement, with full adjustment for inflation, after 35 years of service for men and after 30 years of service for women) has driven up government labor costs. Some states now spend more than 90 percent of revenues on wages and pensions. The State of Rio Grande do Sul spends 41 percent of its revenues on pensions alone.

The outlines of a congressional committee compromise on civil service reform, reached in the fall of 1995, reveal the kind of restrictions state and local governments face. Under the proposal, states and municipalities for the first time would be allowed to cut their work forces, but only if the government wage bill exceeded 60 percent of revenues, and only for as long as personnel spending remained above this threshold. Other provisions would require that young civil servants and apprentices be laid off first, while older workers retained their positions. The authorization for personnel layoffs by states and municipalities would extend only through 1998, the period of the current presidency.

Cost control under the current administrative regime is virtually impossible. Antonio Britto, governor of Rio Grande do Sul, summed up the crisis in Brazilian federalism this way: “Any politician today who has been a mayor or governor knows that Brazil’s states and municipalities are ungovernable without cuts to the absurdities and privileges in public administration.”

Despite general acknowledgment that high benefit levels and lax work rules for public workers have prevented cost-effective service delivery and perpetuated fiscal strain at all levels of government, a political consensus on reform has proved virtually impossible to put together. The issue remained unresolved as of mid-1996.


Output Measurement, Comparison, and Accountability

The routine gathering and publication of information on service quality has proved to be one of the strongest devices for upgrading municipal performance. The Audit Commission of Great Britain exemplifies how regularly published information can be used to promote efficiency. The Audit Commission publishes unit cost comparisons, as well as service quality indicators, for the entire range of local public services—from refuse collection and vehicle maintenance to school test results and government overhead rates. The data provide a context for judging the quality and costs of services in any one jurisdiction.

Within Latin America, Chile pioneered this kind of public service disclosure. It regularly publishes the results of standardized school tests, for both public and private schools. It also publishes comparative unit costs for such items as municipal trash collection, for public as well as private providers.
Both Chile and Great Britain use measures of local service performance as an aid to potential competition. Most Chilean municipalities contract with the private sector for routine services like trash collection or street maintenance. Comparative cost data provide information to potential competitors as to where there may be opportunities for market expansion because current provider costs are high. The data also assist consumers in making market choices. Under the Chilean voucher system, for example, households may choose to send their children to public or private schools using a government voucher. The regularly published information on school costs, school test results, and teacher characteristics are intended to help families make an informed choice about schooling alternatives. Competition among schools is expected to improve educational quality and to restrain costs.

Colombia has recently adopted a system that builds information on service quality into vertical accountability. Under the new national development plan, each public institution must publicly define its mission, adopt output (or “results”) goals that reflect its mission, and regularly measure progress toward the goals. Every institution is supposed to evaluate annually and publicly its output performance. Institutions are subject, as well, to external “results” evaluation by a government auditor.

**Incorporating Market Principles into Municipal Service Delivery**

In the private sector, the best assurance of consumer satisfaction and cost efficiency comes from a competitive market. Customers who are dissatisfied with the quality or expense of the services supplied by a given provider can turn to a competitor. Market pressures force providers to be responsive to customer priorities in order to stay in business.

Many of the same market principles carry over to municipal service delivery—either in the form of literal competitive markets or the construction of service delivery systems that incorporate similar incentives. In fact, a market orientation in service provision is probably the most profound source of change in countries that have substantially upgraded local service delivery. This orientation starts with the pricing of public services at levels that reflect actual costs, and extends through encouragement of competition in the public sector. The structure of intergovernmental aid should also be designed to enforce incentives for cost restraint and enhancement of service quality.

Box 8 illustrates how selected countries have moved toward incorporating market principles into municipal service delivery. Each of the initiatives seeks to strengthen the linkage between what consumers pay for public services and what they receive, while widening the range of service choice for citizens.

**Efficient Intergovernmental Grant Structures**

Many of the most important municipal service functions are financed in large part through intergovernmental transfers. The design of grant structures, therefore, takes on special importance. These may promote or hinder efficiency in service delivery. Grants that reimburse local authorities for actual service costs, whatever their level, for example, tend to drive up service costs, since local authorities bear none of the burden of their own expenditure decisions.

A consensus is emerging in the region regarding the broad structure of grant-in-aid systems:

- **Specific functions of national importance that are transferred from the central level to local authorities should be accompanied by revenue transfers that must be spent on the function.** The allocation formulas should be simple and transparent, and based on standardized rather than actual costs. For example, school funding can be distributed on the basis of a uniform per-student payment, adjusted for special needs.

- **Capital projects and other activities that have significance beyond local borders are most appropriately financed by matching grants, in which the central or state government absorbs part of the projects’**
Incorporating Market Principles into Municipal Service Delivery

In a private market, customers must pay the full cost of service provision. Otherwise, suppliers will go out of business. In contrast, public suppliers of local services traditionally have recovered only a small percentage of costs. Their losses have been covered by subsidies from the general resources of municipal budgets. For example, it has been estimated that water charges recover only 20–30 percent of water supply costs in Mexico and a comparable percentage in Brazil.

Establishment of service fees that recover the full costs of service provision represents one important step toward a market model of service delivery. For example, Colombia has embarked on a seven-year program that raises water fees annually to the point that, by the year 2002, there must be 100 percent cost recovery by all water providers, including the costs of capital investment. Besides eliminating the need for public subsidy of water companies, the measure is expected to restrain the demand for new investment in the water sector. Experience in other countries has shown that demand for water consumption falls significantly when prices are raised, partly because consumers find it in their interest to repair leaks or turn off taps that otherwise are allowed to run freely. Lower consumer demand, in turn, reduces the need for new investment in water supply facilities. Of course, market pricing of water service makes sense only when municipalities have the capacity to measure household consumption and consumers have the ability to change their consumption levels in response to price adjustments. It also requires targeted subsidization plan to protect low income families' ability to obtain water.

Pricing principles also can be built into household investment decisions. Pricing of this kind often is found in municipal loan programs. For example, in barrios of Honduras, small communities in the state of Paraná, Brazil, and other locations, communities are given the choice of having inside water supply or outdoor water connections, at a clearly identified differential cost per household that covers the cost of each kind of investment. Community members then vote on the kind of service they want to pay for. All members are obligated to accept the community's decision, by contributing equally to the cost of the preferred solution.

In some service functions, the principles of a private market can be adopted directly. Municipalities, for example, can conduct competitive bidding among private suppliers for the right to provide trash collection or street cleaning services. Although only one franchise may be awarded, competition for the franchise rights and the prospect of rebidding after the current performance period place market pressure on the supplier. Some municipalities have sharpened local competition by dividing larger cities into separate zones and awarding separate contracts for trash collection in each. This strategy maintains overt competition and establishes clear benchmark comparisons of service costs. At the same time each supplier is able to benefit from the economies of servicing all buildings within its franchise zone. It also ensures that there will be more than one company able to bid when bids open up.

Chile has gone furthest toward incorporating market competition into the provision of basic human services. It provides households with school vouchers that will pay the cost of their children's schooling at either municipal or private schools. New organizations are free to enter the school market by setting up competing schools. Each school is responsible for its costs, and household members can bargain directly with suppliers. Transfers of all kinds should follow clear, stable rules. There should be no case-by-case pleading for funds from the state as a basis for municipal financing.
deficits, overruns in project costs, or other consequences of poor management. When local finances have deteriorated to the extent that a higher level rescue package is needed, intervention should be contingent on local government’s adoption of drastic budget-balancing measures and management reforms. Argentina, for example, has adopted a system of financial bailout for provinces, or by provinces for municipalities, that extends emergency loans that can be converted into grants if the recipients make agreed-upon progress toward cutting costs, privatizing service delivery, and closing local operating deficits.28

Emerging Lessons for Better Implementation

Central-government ministries often resist decentralization because they are skeptical about the ability of local governments to deliver services. Even when responsibilities have been formally devolved, central authorities may try to retain de facto control out of concern for the lack of professionalism of local authorities. There is no denying that many local governments are poorly equipped to take on new functions or even to perform adequately the functions already assigned to them. But there are other factors encouraging decentralization.

Box 9

School and Health Care Grants in Chile; Matching Grants in Mexico

Chile has the longest experience in the region in redesigning grants specifically to make service decentralization more efficient.

When Chile devolved schooling and health care responsibilities to the local level, it initially reimbursed localities for 100 percent of service costs adjusted for inflation. However, costs for both functions soon escalated. The grant structure was redesigned to help restrain costs.

Under the current grant system, municipal schools are able to fund somewhat less than 90 percent of their costs through the per-pupil payments they receive from central authorities. Per-pupil payments are fixed so that there are no incentives (and no rewards) for high costs. Grant payments are pegged to pupil days in school. This has proved an effective spur to higher attendance rates.

In primary health care, government grants now cover about 75 percent of actual costs. The initial practice of financing essentially all local costs precipitated a rapid expansion of local health services. The government subsequently lowered its share of cost coverage and placed a ceiling on reimbursement levels. Local cost-sharing provides municipalities with a fiscal incentive to keep health care costs under control.

Mexico has perhaps the region’s most extensive experience in matching grants. Since it was launched in 1989, its National Solidarity Program (PRONASOL or Solidaridad) has distributed more than US$8 billion in federal funds for infrastructure projects, much of it blended on a matching basis with state and local funds. The matching rates required of state and local governments vary, depending upon both local wealth and the character of investment. Cost-recoverable projects require higher state and local matching rates.

The matching grant system has succeeded in bringing different levels of government into collaborative capital planning and has helped the national government implement its investment priorities. Some observers, however, have argued that variable matching grants of this kind steer resources too strongly in the direction desired by central authorities and open the way for political discrimination.

Block grants may be more appropriate vehicles for financing capital expenditures for functions that now are entirely the responsibility of subnational authorities. For functions that have substantial externalities, a stable and transparent system of matching grants is appropriate.
• Citizen demand for decentralization is high, driven by frustration with the quality of service delivery from the center. From the small pieces of evidence that we possess, citizens seem to feel that decentralization has improved service quality. They support pressing ahead with further devolution. From the perspective of residents outside the capital, there is so much need for improvement in service provision that fear of municipal incompetence is not sufficient reason to maintain the status quo.

• At least in intermediate-sized cities, the present skills of the municipal work force are not a good indicator of the skills potentially available to the community. One of the most pronounced effects of decentralization has been to draw a new generation of mayors into local politics. These mayors typically come from the private sector and are better educated. They are more “modern” in their approach to government and service supply, and they know how to hire managers of similar background. In effect, genuine decentralization, which enlarges the scope for local initiative and problem solving, permits local government to tap a new supply of leaders.

• Cost-effective service delivery requires an overhaul of the municipal work force—a pruning of unskilled workers and recruiting of skilled labor. The transformation of the municipal work force in countries like Chile and Colombia has been a remarkable accomplishment. Other countries will have to make equal efforts to upgrade the skill levels of municipal workers if citizens are to receive the public services they want at reasonable cost.

• Changes in management style can also improve worker productivity. As service functions are devolved to the local level, management can be reorganized to be more effective. Institutions that establish objectives based on results, but give workers greater freedom to decide how to achieve the results and recognize those who succeed, build most effectively on the potential of decentralized management.

• Improving work-force responsiveness and service efficiency will require greater managerial control over the municipal labor force. At this point, indifferent workers or workers who do not appear at all for work are more of a threat to service quality than politically inspired turnover. Civil service coverage may be able to help establish municipal career paths and provide incentives for employees to upgrade their skills, but rules that prohibit employee dismissals based on performance or impede labor flexibility in responding to changing local needs are obstacles to service improvement. Systems that devolve budgetary responsibilities to the local level but retain personnel control at the center—or prohibit worker dismissals by law—are inconsistent with decentralization.

• The intergovernmental grant structure is critical to local service efficiency. In the past, central-level grants have often been poorly designed. They have rewarded high cost structures and maintained central-level control over spending even for functions that have been formally decentralized. A new generation of grants is now being introduced that provides greater incentives for cost control and service efficiency.
CONCLUDING THOUGHTS

LATIN AMERICA HAS EXPERIENCED numerous waves of decentralization since the countries of the region first gained their independence. Each has finally ended with a recentralizing of authority at the national level. Many authors have noted that this cycle of decentralization and recentralization has had less to do with disagreement over the most effective structure of government than with quarrels between different political elites who, when possessing national power, favor centralization and, when out of power, prefer decentralization.

Whether the current decentralization initiatives will prove more durable remains to be determined. These initiatives do, however, possess distinguishing characteristics that set them apart from past efforts at transferring power from the national to the local level. First, they place much greater emphasis on practical service delivery. Public dissatisfaction with the level and quality of public services has been the driving force behind the recent changes. Citizen satisfaction with services also provides a yardstick by which the accomplishments of decentralization and other government reforms can be measured.

Second, decentralization of service delivery is occurring at a time when the state is taking its responsibilities for macro-economic management and fiscal restructuring far more seriously. This suggests a division of labor that may be sustainable, where the central government concentrates on solidifying the economic and fiscal framework of the country, and subnational governments assume more responsibility for service delivery or for oversight of service delivery by the private sector. The intergovernmental financing rules are crucial to this division of labor. They must simultaneously provide local governments with stability and predictability of financing, while providing the central government the flexibility and resources needed for macroeconomic management.

Third, the current wave of decentralization has produced a remarkable variety of local experiments in citizen participation in governance. This experience is building a grass-roots constituency for local civic engagement, as well as a thick web of democratic institutions. Citi-
zens' expectations that they have a right to participate in municipal government may prove to be the best bulwark of decentralization.

Robert Putnam, in his remarkable study of a quarter century of decentralization in Italy, noted that there is an extremely high correlation between the effectiveness of institutions in service delivery, citizen trust in these institutions, and citizen participation. Where local institutions are effective at service delivery (as measured by such simple indices as the ability to deliver services on time or respond to citizen inquiries), people had far greater faith in the decentralization process. Effective institutions, in turn, were more open to citizen involvement.

In the end, decentralization probably should not be viewed as a goal in itself. It is an instrument for achieving more effective service-delivery systems, for opening the institutions of governance to wider civic participation, and for increasing public trust in government. There are other instruments, as well, for achieving these goals. Decentralization, in fact, is one of many reforms taking place in the way the public sector is managed in the region. Specific decentralization proposals should be judged according to how well they serve these deeper purposes of effective service performance and democratic participation in governance. The spirit animating decentralization should not fall victim to rigid demands that more funding and powers be transferred to lower levels of government.


Development, and the Federación de Municipios del Istmo.


NOTES

3 Tanzi, 1995; Ahmed et al., 1995.
4 For example, see World Bank, 1990; Winkler, 1994.
5 Superintendencia Bancaria (Colombia), 1995.
6 Economist, 1996. The State of São Paulo now owes lenders $58 billion. The annual increase in state debt in 1995 exceeded the state’s total annual tax revenues, even though São Paulo had no new borrowing. Real interest rates in excess of 20 percent, coupled with the state’s failure to make interest or principal payments, accounted for the growth in indebtedness.
7 For example, see Villela, 1993; Shah, 1991; Schroeder, 1990; Sánchez and Gutiérrez, 1994.
8 World Bank, 1992a.
15 Fox, 1994.
17 Ziccardi, 1995b.
18 Federación Colombiana de Municipios, 1994.
20 The historical role of cabildos abiertos as democratic institutions also seems to have been exaggerated. In the early colonial years, cabildos abiertos were convened sporadically by mayors, largely in response to emergencies or royal celebrations. They were not open to all inhabitants but to invited notables. Cabildos abiertos were briefly reactivated during the independence movement, but rapidly disappeared afterward. See Nickson, 1995.
22 Ibid.
23 Quehl and Call, 1994.
24 Peterson, 1990.
29 Campbell, 1994b.
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