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## Promoting Good Governance with Social Funds and Decentralization

# Findings

Bad governance undermines development. Corruption, lack of transparency and accountability, poorly designed decentralization, inadequate service delivery, and social exclusion can all direct resources away from the poor, needy, and powerless to the rich, replete, and dominant. Development initiatives by governments and their partners seek to redress these imbalances by supporting activities designed to improve governance. Two important types of World Bank support for local governance are social funds and broadly based support for governments committed to decentralizing responsibility and power to local governments and other local institutions. But there are concerns that these two approaches, which address different elements of governance, sometimes work at cross-purposes. A study was therefore commissioned to examine the interaction between social funds and decentralization in Bolivia and Honduras (advanced decentralization), Peru and Zimbabwe (some decentralization), and Cambodia, Malawi, and Zambia (little or no decentralization). Funding for the study was provided by the Bank's thematic groups on decentralization, municipal finance, and social funds; by the government of Switzerland; and by the

United Nations Capital Development Fund. This note is based on the findings of the study.

### Aims and models

Social funds aim to empower communities by enabling them to participate in the selection, implementation, and operation and maintenance of development projects. Such funds provide direct financing for community projects designed to quickly improve basic services and reduce poverty. Since 1987 the Bank has approved about 100 social fund projects worth \$3.4 billion in more than 60 countries. Though a variety of institutional models have been used, social funds have usually been established as specialized units separate from traditional government line ministries. To promote timely support, social funds typically use procedures that are not subject to standard government procurement and other regulations.

In contrast, decentralization focuses on formal government institutions, both political and administrative. Decentralization is complex and encompasses a wide range of elements (see Parker 1995). Still, evidence from many countries suggests that three conditions must be met if decentralization is to improve governance (see Manor 1999):

- Significant responsibilities and powers for local service delivery should be devolved to local authorities in line with their capacities (political decentralization).
- Sufficient resources—through a combination of local taxes and grants from higher-level governments—are needed to enable local governments to meet responsibilities (fiscal decentralization).
- Proper channels are needed to encourage strong accountability between bureaucrats and elected representatives network and between elected representatives and their electorates (institutional decentralization).

### **The need for mutual support**

Social funds and decentralization have supported each other in important ways. Foreexample, social funds have encouraged decentralization where it has not advanced far. In Cambodia, Malawi, and Zambia central governments were slow to decentralize functions and resources, so local governments could not be relied on to deliver basic services. By channeling resources to community groups, social funds in all three countries demonstrated the feasibility of and potential for participatory planning. In Zimbabwe local governments have been assigned service delivery responsibilities but often lack sufficient resources. Thus the recently created social fund is intended to strengthen decentralization processes and operationalize participatory planning.

In Bolivia and Honduras decentralization has advanced rapidly and local governments are taking on more responsibilities for delivering services. Social funds in both countries have responded by inte-

grating their resources with local budget procedures as part of broader intergovernmental fiscal reforms designed to improve funding for local development. Using decentralized local institutions, such as local governments, to manage social fund operations holds out the opportunity for scaling up activities that social funds might finance.

### **Contrasting approaches**

Despite efforts at working together, the different objectives and focuses of social funds and decentralization efforts have raised questions about how best they can work together to improve poor people's standard of living. As central governments reallocate responsibilities for providing basic services to subnational governments, the potential increases for the community-oriented social fund approach to conflict with constitutionally mandated changes in local responsibilities. Different aspects of governance were studied to examine the nature of this conflict.

#### *Local planning*

Social funds have shifted decisionmaking away from government bureaucrats toward communities that previously had little or no opportunity to influence decisions, especially in countries without decentralized local planning—such as Cambodia, Malawi, and Zambia. But the social fund approach to local planning is limited: it usually focuses on a community's selection of one project from a menu supported by each fund. In Malawi and Zambia about three-quarters of social fund investments were for primary school projects. While these project choices undoubtedly

reflected the poor state of school infrastructure, had communities been free to select any type of development intervention it is not clear that they would always have selected a school. Thus the social fund approach is participatory but restricted, and is no substitute for a local planning process that elucidates the full range of community development needs.

Implementing a complete system of decentralized local planning is much more challenging because decentralization ultimately involves the complete transfer of service delivery responsibilities to local governments. These governments must then try to prepare annual development plans for basic services covering all their jurisdictions in a strategic and coordinated fashion. Local plans are often not prepared in a participatory way, so the preferences of poor communities may not be reflected. But local governments are learning from social fund operations—especially ways of interacting with communities—and are adopting more participatory approaches.

#### *Financing*

Social funds are one of the few central programs that are national in scope and provide direct funding for community-driven development. Where there are few alternative sources of funding for community development—especially in poor, centralized countries like Cambodia, Malawi, and Zambia—social funds provide an important source of direct funding.

But as decentralization reforms establish fiscal systems that incorporate central grants and local taxes, social funds can end up providing a parallel source of funding

outside official channels. This may help speed project implementation, but it can conflict with the objective of building accountable local governments. This happened in Peru, where the central government was not fully committed to empowering local governments, so the social fund ended up bypassing elected local governments.

For effective financing of local development, the challenge is to find ways for social funds to work with local government institutions while ensuring that poor communities still benefit directly. In Bolivia and Honduras social funds work directly with the political and administrative branches of local governments to increase awareness, provide technical assistance, and coordinate activities.

#### *Accountability*

An important feature of social funds is the promotion of open operations. Communities make their own choices about many elements of the project cycle, including project selection, procurement, and contracting. Many evaluations of beneficiary satisfaction with social fund projects have indicated that this openness has helped restore community faith in the ability of public institutions to provide essential services, and has helped communities appreciate their own roles and responsibilities in these activities.

Accountability is also an essential part of decentralization. Successful decentralization requires mechanisms that hold local governments accountable to their electorates. It also requires that local bureaucrats, whether local officers of central line ministries or local technical staff, are accountable to

elected local governments. But mechanisms for local accountability are often weak: they can be over-ridden by political forces and are subject to subversion by powerful elites. In Peru social fund spending rose significantly just before two recent presidential elections, and projects were funded in provinces where the political impact was likely to be greatest (Schady 1998). Close scrutiny of accountability mechanisms is therefore important to assess the feasibility of having local governments manage social fund resources.

#### *Sustainability*

Real development impact comes only from the sustained provision of basic services over many years. But factors outside the immediate control of social funds and local governments often determine whether social fund investments have a lasting impact.

In some cases social funds have effectively used community institutions to operate and maintain services. In Zambia more than 60 percent of parents pay fees to school committees to cover the cost of routine maintenance of investments supported by the social fund. But as responsibilities for service delivery are increasingly decentralized, local governments are expected to take on a more significant role in the funding and institutional arrangements needed to ensure sustainability. Yet local governments are often constrained by limited capacity and resources, so social funds in Bolivia and Honduras have gone one step further and now require that local governments include the operation and maintenance expenses of their social fund projects in annual development

plans and budgets. Such integration will increase the chances of effective operation and maintenance—though much still hinges on the technical capacity of local governments to provide staff and undertake routine maintenance.

#### **Conclusion**

Decentralization and social funds are closely related. As more countries decentralize, local governments are tapping into the lessons learned through social funds, and many are seeking ways to adopt more participatory planning approaches, more sustainable financing of recurrent costs, and better mechanisms for accountability. In countries with weak local governments, such as Cambodia, Malawi, and Zambia, social funds are not incorporated in local political decisionmaking. Nevertheless, coordination between social funds and local governments is improving in all three countries. For example, in Zambia a window of financing for district council projects is being designed as part of the next social fund project.

Honduras, Peru, and Zimbabwe have varying degrees of decentralization and varying degrees of involvement by elected local governments in social fund operations. In 1998 Honduras incorporated decisionmaking on social fund projects into its system of town hall meetings, though recent events have highlighted the difficulty of maintaining such a broad approach to popular participation, and it is too early to evaluate the impact of these changes on development outcomes. In Zimbabwe rural governments are slowly becoming more assertive, and the social fund is providing resources to address shortages in

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local funding. In Peru, however, the lack of decentralization has restricted opportunities for the social fund to work with local governments.

Bolivia's social fund has come the closest to complete integration with the operations of elected local governments. Sweeping legislative reform, especially the 1994 Law on Popular Participation, established important requirements for community involvement and conferred new responsibilities on local governments. The social fund is an important part of these arrangements, and has promoted closer integration between communities and local governments by financing only

projects that have been identified through participatory municipal development plans.

All the social funds studied are investigating ways to increase the involvement of local governments. Some funds are beginning to transfer more project responsibilities to local governments, especially in Bolivia, Honduras, and Zimbabwe. Such funds will face the challenge of transforming themselves from agencies that manage the direct implementation of projects to agencies that support local capacity building for project implementation. Similarly, local governments face the challenge of learning from social fund procedures that have empowered poor communities.

### Further reading

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