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The Vertical Assignment of Functions and Expenditure Responsibilities



LPSI Working Paper – May 2015

THE VERTICAL ASSIGNMENT OF FUNCTIONS AND EXPENDITURE RESPONSIBILITIES

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Cover photo credit: Students of Rajagaon Government Primary school at Rajagaon village in Thakurgaon Sadar Upazila (Bangladesh) attend classes under a makeshift shed as the school building was declared abandoned in June last year after cracks developed on its walls and floors. (The Daily Star, June 9, 2014).

EXECUTIVE SUMMARY

This working paper provides both a conceptual and practical understanding of “how to” effectively assign functional responsibilities and authorities to different levels of local government (or to different tiers of local administration) in the context of multilevel governance systems. In doing so, it establishes a common vocabulary in discussing functional assignment issues; reviews the concept of subsidiarity; unbundles and dissects the concept of government functions; and considers the role of decentralization as a mechanism to improve accountability and pro-poor service delivery. Consistent with the “second generation theory” of intergovernmental finance, this working paper also tries to place the vertical assignment of functions and expenditure responsibilities in a political economy context that recognizes that central and local political decision-makers do not necessarily try to maximize the well-being of their constituents; instead, the assignment of functions and responsibilities may be shaped by the personal and institutional motivations of political and institutional decisionmakers.

THE VERTICAL ASSIGNMENT OF FUNCTIONS AND EXPENDITURE RESPONSIBILITIES

JAMIE BOEX

1. Introduction

An important challenge for any public sector is to translate its national development ambitions—with respect to a more educated workforce, a healthier population, better access to clean water, a well-developed roads network, and so on—into an improved situation “on the ground” in the cities, towns and villages across its national territory where the people live. In other words, how does a country most effectively “localize” its national policy objectives?

Answering this question involves several parts. The first part of the answer is to recognize that different countries have put in place different institutional or organizational structures at different subnational levels for the public sector to reach the grassroots level. Second, once the territorial-administrative architecture has been decided and has been put in place, a decision needs to be made about “who will do what”: what roles and responsibilities should be assigned to different levels of governments or to different administrative tiers?

In order to ensure that a (global or national) dialogue on improving public services and localizing development is well-informed, all stakeholders that take part in such a discussion should have a common understanding of the terminology and key concepts involved in decentralization and localization. In practice, however, concepts are often poorly defined and key terms are used differently in different countries. There is also disagreement among leading experts on some of the most basic concepts dealing with decentralization.

The absence of a common “vocabulary” on decentralization and localization confuses the debate about the unquestionable need to localize development results. As part of the ongoing efforts of the Local Public Sector Initiative, this working paper seeks to support the emerging global dialogue on the localization of a sustainable development agenda by presenting a theoretical background and conceptual considerations with regard to the roles of local governments and local administration in ensuring efficient and equitable local public services.¹

¹ This working paper is based on Boex (2014), Chapter 2: “The Assignment of Functional Responsibilities in Health and Education: A Conceptual Framework”.

As such, this working paper provides a theoretical or conceptual introduction on six key issues dealing with the “vertical” assignment of functions and expenditure responsibilities across different levels of government or subnational administrative tiers:

1. **Understanding subnational institutions and intergovernmental architecture:** when should local entities be considered (devolved) local governments, and when should we consider them (deconcentrated) local administrations? (Section 2)
2. **The concept of subsidiarity:** in “vertically” assigning responsibilities to different government levels (or administrative tiers), how do we balance the advantage of proximity to the people with the disadvantage of scale economies? (Section 3)
3. **What do we actually mean by “functions” and “functional assignments”?** A deeper understanding of the concept of functional assignments requires us to consider the nature of government “functions” and reflect on the multi-dimensional nature of (*de facto*) functional responsibilities. (Section 4)
4. **Decentralization as a mechanism to improve accountability:** How do intergovernmental architecture and functional assignments interact in efforts to improve responsive and localized public services? (Section 5)
5. **The provision of health and education services in a multi-level governance framework: international practices.** What issues come up when we apply the subsidiarity principle to health and education services in a multi-level governance framework? Section 6 considers international practices with regards to the assignment of functional responsibilities in health and education.
6. **The political economy of functional assignments:** how do politics and institutional incentives play a role in determining functional assignments? (Section 7)

In an attempt to provide a practical overview of the current state of knowledge with regard to the assignment of functions and expenditure responsibilities, this paper covers both what is known as the “First Generation Theory” of expenditure assignments (e.g., Martinez-Vazquez, 1999; McLure and Martinez- Vazquez, 2000; Oates, 1972) as well as the ongoing transition to a “second generation” view of expenditure assignments (e.g., Ahmad and Brosio, 2015; Dafflon, 2015). Whereas the first generation theory focuses largely on the fiscal policy design aspects of fiscal decentralization, the “second generation fiscal federalism” literature explicitly acknowledges the role of institutional decision-making and political economy forces in multi-level governance systems. As such, the second-generation literature recognizes that central and local political decision-makers are not necessarily benevolent rulers that maximize the social welfare of their constituents, but rather, that the assignment of functions and responsibilities—as well as the functioning of the entire intergovernmental fiscal system—is shaped to a large extent by the personal and institutional motivations of political and institutional decisionmakers at all levels (Oates, 2005; Weingast, 2009; 2013).

2. Understanding subnational institutions and intergovernmental architecture

Definition of decentralization. The root of any discussion on the vertical assignment of functions and expenditure responsibilities should begin with a clear definition of decentralization. The rich literature on decentralization presents numerous definitions of the concept, often revealing slight differences in wording between different authors. For instance, a relatively parsimonious “traditional” definition of

decentralization is “the transfer of authority and responsibility for public functions from the central government to subordinate or quasi-independent government organizations” (Litvack and Seddon, 1999: 2).² A slightly longer definition is provided by Professor Dennis Rondinelli (1986), who defined decentralization as the “transfer of [authority and] responsibility for planning, management, resource-raising and -allocation and other functions from the central government and its agencies to field units of central government ministries or agencies, subordinate units or levels of government, semi-autonomous public authorities or corporations, or non-governmental or voluntary organizations”.

For the purpose of the current discussion, it is helpful to follow the second of these two definitions of decentralization for two reasons.³ First, this definition is more explicit about what constitutes a “public function”, by specifying that public functions include “planning, management, resource-raising and -allocation and other functions”. A second reason for preferring the slightly longer definition is that it provides greater guidance on the possible recipients of decentralized authority and responsibility.⁴

Deconcentration, delegation, and devolution. Similarly, the existing decentralization literature offers a number of definitions for the concepts of “deconcentration, delegation, and devolution”. Although there are again considerable differences in the definitions presented by different authors, a careful reading of Rondinelli’s earlier expositions (1986) suggests that the distinguishing feature of these three types of decentralization is the organizational or legal nature of the local entity to which responsibilities and authorities are transferred. In line with this thinking, Boex and Vaillancourt (forthcoming) posit that:

- Devolution is the transfer of authority and responsibility for public functions (as expanded on above) to quasi-autonomous units of local government with corporate status.
- Deconcentration is the transfer of decision-making authority and responsibility for public functions to lower territorial administrative tiers of the central government.
- Delegation is the transfer of authority and responsibility for public functions to semi-autonomous public authorities or corporations, or non-governmental or voluntary organizations.

In this context, devolution, deconcentration and delegation could be classified as three different types of organizational-governance structures of the (local) public sector. Although the amount of authority and autonomy given to devolved local governments is generally greater under devolution than the authority and autonomy given to deconcentrated administrative units under deconcentration, we can observe greater or lesser degrees of political, administrative and fiscal authority and autonomy in different countries within each of these three types of organizational-governance structures. For the sake of clarity, Table 1 presents a contrast between the organizational nature of devolved, quasi-autonomous units of local government and deconcentrated territorial (local) administrative units.

² The original definition of decentralization includes the concept of privatization, which is generally no longer considered to be part of the concept of decentralization. The definition was therefore redacted.

³ This section draws on Boex and Vaillancourt (forthcoming). See this reference for a detailed discussion on the organizational mechanisms within which the public sector interacts with the people.

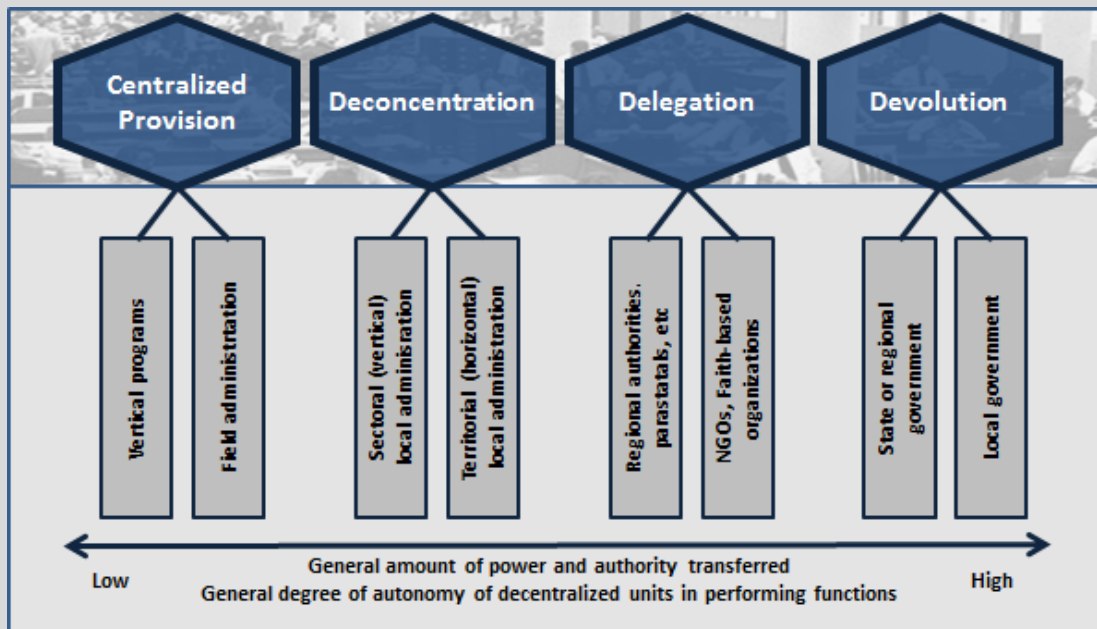
⁴ In addition, it should be noted that the definition makes a subtle distinction between responsibility and authority, recognizing that decentralization is not just about the transfer of responsibilities, but it is equally about the transfer of a meaningful degree of authority or decision-making power to execute these responsibilities with a degree of autonomy.

	Devolution	Deconcentration
Local entity	Local government	Local administration
Legal characteristics	Corporate body (can own assets, engage in financial transactions, sue and be sued in its own name)	Part of national / state administration
Political characteristics	Own political leadership (typically, elected local council and/or local executive); adopts its own budget	No political decision-making power (advisory council, if any)
Admin. characteristics	Local government appoints own officials and has discretion over own human resources	Local staff are hierarchical part of national civil service
Fiscal characteristics	<ul style="list-style-type: none"> • Has its own budget (separate from higher-level government) • Has own budget accounts; can carry forward balance from year to year • Can raise funds and retains own revenues in own budget • Can incur liabilities by borrowing on its own account 	<ul style="list-style-type: none"> • Budget of jurisdiction is part of national budget as (sub-)organization • Budget is approved by higher-level government (e.g., Parliament) • Finances are part of Consolidated Treasury Account • Any revenues belong to central government

In addition to these three decentralized channels of public service provision, however, there is a fourth channel through which the public sector can (and often does) localize public services, namely, direct centralized provision. For instance, if a central line ministry directly funds the construction of health clinics or if a central agency procures medicines and provides to the local level in-kind through a so-called “vertical program” (as opposed to allowing local governments to do the same through their own budgets), this spending ought to be considered part of local public sector spending, since the resulting infrastructure is used in a direct and localized manner in the delivery of local public services (and is likely to have a positive impact on local service delivery outcomes). Similarly, according to this typology, services provided by the field administration of central line ministries should also be considered centralized provision of localized services (instead of “devolved” service provision) if the field administration lacks an organizational or institutional structure that does not hold any meaningful degree of (*de jure* and/or *de facto*) administrative authority over the service delivery process (i.e., some degree of authoritative control over budget resources or specific statutory administrative powers over human resource administration).

Details on the resulting four organizational-governance types of decentralization and localization are presented in Figure 1.

Figure 1: Details on the four organizational-governance types of decentralization and localization



3. The concept of subsidiarity: balancing proximity to the people and scale economies

Understanding the overarching organizational-governance structure of the subnational public sector in a country is a precondition for understanding the assignment of functions and expenditure responsibilities across different government levels. Once we have charted the organizational structure of the public sector in a country, we can ask ourselves: what should the functions or responsibilities be of each government level or administrative tier?⁵

The de jure assignment of functional responsibilities. A country’s constitution or the legislative framework establishing local governments normally gives an important indication what the functional responsibilities of local governments are expected to be. The legal or *de jure* assignment of the “functions”, “responsibilities”, “mandates” or “powers” of local governments is often captured in a list – sometimes included as a separate schedule to the constitution or local government act—which details the specific activities or functions that are to be the responsibility of local government authorities. For instance, a common way in which the *de jure* assignment of functional responsibilities may be assigned is for the relevant law to state that local governments are assigned the responsibility for the “provision and maintenance of primary education” (Nigeria); the responsibility “to operate and manage health centers, health posts and sub-health posts” (Nepal); or the function to “establish, erect, maintain and control slaughter houses” (Tanzania).

⁵ This section relies in part on Boex, Martinez-Vazquez, and Timofeev (2004).

In principle, a legal (*de jure*) functional assignment can be made to devolved local governments as well as to deconcentrated local administrative bodies. In practice, however, the assignment of functional responsibilities (and authority) to deconcentrated entities are often made in a less explicit manner when compared to the *de jure* assignment of functional responsibilities to devolved entities (Box 1).

Box 1. Functional assignment to deconcentrated entities: the case of Mozambique

Functional assignment to deconcentrated entities is often less explicit when compared to the *de jure* assignment of functional responsibilities to devolved entities. In some cases, the constitutional or legal framework may provide general guidance on the assignment of functional responsibilities without providing detailed guidance. In Mozambique, the Law on Local State Administration (known by its Portuguese acronym, LOLE) designates the district level as the “principal territorial unit for the organization and functioning of the local administration” and as the base for planning the “economic, social and cultural development of the Republic of Mozambique”, (Boex et al, 2008).

Although LOLE’s implementing regulations enumerate different responsibilities and tasks to be undertaken by the provincial and district administrations, the delimitation of those responsibilities among different levels of government is not very clear. For instance, while the provincial level is assigned the responsibility (or “competence”) to “monitor the establishment and management” of primary schools and primary health services, the district administration is assigned the responsibility “to guarantee the good functioning of” the educational and health facilities in the district. Such verbiage does not provide clear guidance on which level is responsible what. In other cases where clear guidance is provided, the delimitation is not necessarily adhered to in practice.

Since under sectoral deconcentration, deconcentrated sectoral units are legally part of their respective line ministries, the explicit functional responsibilities of deconcentrated offices and officers may be defined as part of the regulatory framework rather than being explicitly defined in the legal framework (whether the sector law or local government act). In fact, it is possible that there is no formal vertical assignment of functional responsibilities beyond the assignment of functions revealed by central ministry directives and job descriptions.

Musgrave’s economic roles of government. In evaluating whether any particular functional assignment is sound or efficient, it is important to clearly understand why the public sector engages in a certain function in the first place. According to Professor Richard Musgrave (1959), the public sector in any economy has three basic economic roles: first, to ensure a stable economic environment; second, to ensure an equitable allocation of income and resources; and third, to ensure the efficient allocation of resources. These roles apply regardless whether the economy is a planned economy or a market economy. However, in the context of a market-based economy, we expect the scope of government intervention to be much more limited. In addition to the stabilization and redistribution roles, we would expect the government in a market economy to pursue the economic efficiency role only whenever the market fails to allocate resources efficiently due to a particular market failure.⁶

⁶ Three types of market failure are commonly recognized. These are *public goods* (goods that are non-rival and non-exclusionary, such as national defense), *externalities or spillover effects* (situations in which costs or benefits are imposed on third parties, such as in the case of pollution), and *non-competitive market structures* (such as monopolies or cartels). These cases of market failure justify government intervention.

Musgrave's original writing provides only limited guidance with regard to which level of government within the public sector should pursue each of these three basic economic functions. Whereas a champion of centralized service provision might argue that all these functions are best performed by the central government, an unabated proponent of decentralization might argue that the local government level—being the level of government closest to the people—is in the best position to pursue these functions. However, neither extreme position would lead to an efficient allocation of public resources.

The subsidiarity principle. The principle that economists use to guide which level of government should perform a public function is known as the “subsidiarity principle”. The subsidiarity principle states that ***public goods and services should be provided by the lowest level of organization that can do so efficiently.***

As such, the subsidiarity principle balances the arguments and concerns made both by centralists as well as by decentralists. On one hand, the subsidiarity principle suggests we should not automatically assign functions to either the highest or the lowest level, but rather, suggests that we should identify the lowest level that is able to perform the function efficiently. Reliance on the smallest-possible efficient “area” in the provision of subnational government services contributes to achieving overall efficiency in the delivery of public goods and services in a number of ways:

- The smaller the distance between decision-makers and the communities they serve, the better informed the policy makers will be about the preferences and needs of the people.
- The greater the fragmentation of (efficiently-sized) subnational jurisdictions, the greater the potential for ‘allocative efficiency’ due to a better match between the local mix of goods and services provided and the local variations in the preferences and needs for public services.
- Because of the closer proximity to their local government officials, local residents are better informed about the actions of their governments and they can use the quality of service delivery in neighboring jurisdictions as a performance benchmark. Given the appropriate governance mechanisms, local government officials will be more accountable to local voters for the quality of services they provide compared to central government officials.
- Local government provision of public services at a lower government level will make taxpayers more willing to pay for public services, since the link between costs and benefits is strengthened. Efficiency in the provision of public services is enhanced if consumption benefits are linked to costs of provision via fees, service charges, or local taxes.

On the other hand, the subsidiarity principle subjects the assignment of expenditure responsibilities to the important provision that jurisdictions should be able to provide the function efficiently. This provision prevents expenditure responsibilities from being assigned to subnational government jurisdictions that are too small or otherwise not capable to efficiently deliver the public service at hand. This, of course, is the concern of many stakeholders who advocate a more centralized approach to delivering public services.

The most common efficiency concern in decentralized public service delivery is the presence of scale economies; scale economies are the concept that it is more costly to produce a good or deliver a service per person when the number of people served (the quantity produced) is small. Inversely, as the size of a government jurisdiction increases (up to a point, known as the “minimum efficient scale”), it becomes less costly per resident to deliver public goods or services. As such, the subsidiarity principle requires

that the smallest jurisdiction at each government level exceeds the “minimum efficient scale” for delivering the public goods and services that are assigned to that level.

It quickly becomes clear when functional responsibilities are assigned to a local governance level that is “too low”: highly fragmented, weakly capacitated local governments are unable to efficiently deliver public services. There are numerous examples of countries that encountered this problem, especially during the wave of decentralization reforms inspired by democratic transitions in the 1990s, including Hungary, South Africa, and several of the countries of the Former Soviet Union. The average jurisdiction size of local governments in some other these countries was no more than a few thousand residents, often with a significant number of local government jurisdictions with fewer than a thousand residents. In many of these countries, a few years after the onset of decentralization reforms, a wave of local government consolidation or re-centralization set in with the recognition that the lowest-level local governments were simply too small to obtain the necessary capacity to perform their functions efficiently.

The principle of fiscal equivalence. The subsidiarity principle fits well with the principle of fiscal equivalence (Olson, 1969). The basic argument made by Professor Olson is that communities create different levels of government as a mechanism for collective decision-making when joint provision of certain services is preferable over individual provision (for instance, in the case of national defense, or in the construction of a public road). Whereas there are benefits (due to scale economies) from jointly providing certain public goods, as the jurisdiction size increases, there are also disadvantages of joint provision. Depending on the nature of the publicly provided good, congestion costs may arise (Buchanan, 1965). In addition, large groups require a representative decision-making mechanism to make collective decisions, which reduces the responsiveness of decision-makers to the preferences of the community, especially as the size of the government jurisdiction increases. In an ideal situation, the size and composition of the group (local government) is decided so that every individual benefits from being part of the group (in other words, so that their benefits from being member of that group exceed the tax cost of belonging to that group).

Consistent with the subsidiarity principle, the principle of fiscal equivalence implies that government goods and services should be provided so that the boundaries of the “benefit area” of each collective good or service are the same as the boundaries of the government jurisdictions that provides the good or service. For instance, the lowest level at which solid waste collection can be provided is the local level. At this level, the benefits area for household garbage collection is equal to the local jurisdiction where garbage is collected, so in accordance with the principle of fiscal equivalence, this service should be provided (i.e. delivered and paid for) at the local government level. This structure will allow each local community to determine their preferred level of garbage collection, as they consider both the costs and benefits of the local public service.⁷

The subsidiarity principle applied to Musgrave’s roles. In addition to applying the subsidiarity principle to a list of specific government functions (as is typically done in legislation), it is useful to discuss how the subsidiarity principle applies to Musgrave’s three main economic roles of government. In other

⁷ It can be show that if the benefits area is smaller than the jurisdiction, the provision choice made by local voters and their representative would be inefficient. Similarly, if the benefits area is larger than the jurisdiction, the provision choice made by local voters would be inefficient.

words, according to the subsidiarity principle, which level of government should be responsible for economic stabilization, for achieving equity, and for assuring efficiency in the economy?

Achieving a stable economic environment. Economic stability (including stable prices, stable growth, and so on) is generally achieved by ensuring the rule of law, enforcing property rights, pursuing a stable macroeconomic environment and managing external trade relations. One of the dominant policy instruments involved in achieving a stable macroeconomic environment is monetary policy. This functional area is generally best assigned to the central government (possible through an independent central bank), because the benefits of sound macroeconomic policies are enjoyed by the nation as a whole and because monetary policy conducted at the subnational level would likely result in inefficient outcomes. For instance, whereas a central government has to balance the implications of financing its budget deficit through monetary expansion (printing money) with the negative impact of higher inflation on the economy as a whole, allowing municipalities to determine a country's money supply by printing money would clearly result in inefficient outcomes.

Assuring an equitable allocation of resources. Likewise, the pursuit of a more equitable allocation of resources across the national population is hard to decentralize to a subnational level, and should therefore often be assigned to the national level. There are two basic reasons why it would be inefficient to assign redistributive functions to subnational (especially local) governments. First, it is simply impossible for local governments to equalize across the national territory, so that poor jurisdictions simply do not have access to the necessary fiscal resources in order to engage in redistributive programs. Second, it is highly likely that if redistributive programs are undertaken subnationally, that wealthier households and firms over time would seek to avoid regional and local jurisdictions that engage in such redistribution by locating outside such equalizing jurisdictions.

Pursuing economic efficiency (when markets fail). Whether, under the subsidiarity principle, public actions undertaken to enhance economic efficiency should be pursued in a decentralized manner ought to be decided on a case-by-case basis, since the answer depends on the particular nature of the market failure. In case a market failure is local in nature, then the corrective action can often be efficiently taken at the local level as well. For instance, the market mechanism may not provide a small public park since the park is (in the strict economic sense of the word) a 'public good' that is non-rival and non-excludable, and therefore cannot be profitably operated by a private business. However, a local park can be efficiently provided by a local government, who may charge the local residents a nominal amount through the local tax system as a quasi-user charge. Assignment of this function to the local level would therefore be consistent with the subsidiarity principle. However, if the market failure is national in nature (for instance, a national port or national defense), then it would be inefficient to assign the responsibility to a subnational level, and the function should be assigned to the national level.

In this light, it is important to recognize that many of the government services typically provided by subnational governments are not 'public goods' in the strict sense of the term. Instead, local governments generally provide many 'club goods', which are typically either excludable or rival (or both) to some extent. For instance, consider the nature of public swimming pools, local libraries, or fire-fighting services. These goods and services are more efficiently delivered by 'clubs' of people, rather than by individual households. In this case, the local government simply acts as a club to provide certain goods to the local community in the least costly manner possible.

4. Understanding the multi-dimensional nature of functional responsibilities

Up to this point, we have discussed the topic of functional assignments without actually addressing a critical question: what is a government function? We have generally equated “government functions” with key public services, such as public education, public health services, or solid waste management. How would we more formally categorize or break down these functions or activities of the public sector into different policy areas or functional dimensions? Breton (2015: 72-73) frames the issue as follows:

The Fiscal Federalism literature generally calls the ‘objects’ that are to be assigned to governments inhabiting different jurisdictional levels ‘functions’ and/or ‘responsibilities’. The functions are then identified as ‘allocation’, ‘redistribution’ and ‘stabilization’ as these terms are understood in Welfare Economics ... To my knowledge, the bridge that would allow passage from these ‘functions’ to the ‘objects’ that one finds in real world constitutional documents and jurisprudence, which are called ‘powers’, is not provided... A power is the authority granted to, or acquired by, a public or private body to legislate, regulate, and/or have a general capacity to act in particular areas or domains.

Breton (2015:73) continues his argument by pointing out (a) that powers are multi-dimensional; (b) that some degree of power is assigned to all government levels or tiers for most government functions; and (c) based on the legal functional assignment alone, it is normally impossible to say how powers are actually subdivided among the among the various bodies in which authority to act may have been vested. The current section will explore these issues in greater depth.

The Classification of Functions of Government (COFOG). The Classification of Functions of Government (COFOG) is a detailed classification developed by the IMF (2001) of the functions that government units aim to achieve through various kinds of expenditures or outlays. By providing a standard classification of government functions and expenditures across countries, statistics on expenditures for health, education, social protection, and environmental protection can be used to study the effectiveness of government programs in those areas and permits examination of trends in government expenditures on particular functions over time. Although the classification was mainly developed in order to classify public expenditures by function, the IMF’s GFS COFOG is the most commonly used classification of government functions.⁸ The COFOG contains ten main divisions:

01 General public services	06 Housing and community amenities
02 Defense	07 Health
03 Public order and safety	08 Recreation, culture, and religion
04 Economic affairs	09 Education
05 Environmental protection	10 Social protection

Within each division, there are several groups, or three-digit categories, such as hospital services (073). In turn, within each three digit category, there are one or more classes, or four-digit categories, such as

⁸ The IMF Government Finance Statistics Manual—including its COFOG classification—is revised from time to time. It should be noted that the OECD has a similar COFOG classification scheme.

nursing and convalescent home services (0734). All three classification levels and detailed descriptions of the contents of each functional class are provided in the IMF (2001) Government Finance Statistics Manual. Table 2 presents an overview of functional classes for health and education.

Table 2. COFOG Functional Classes for Health and Education.	
Health (07)	Education (09)
<p>071 Medical products, appliances, and equipment 071 Medical products, appliances, and equipment 0711 Pharmaceutical products 0712 Other medical products 0713 Therapeutic appliances and equipment</p> <p>072 Outpatient services 0721 General medical services 0722 Specialized medical services 0723 Dental services 0724 Paramedical services</p> <p>073 Hospital services 0731 General hospital services 0732 Specialized hospital services 0733 Medical and maternity center services 0734 Nursing and convalescent home services</p> <p>074 Public health services 075 RandD Health 076 Other Health (not elsewhere classified)</p>	<p>091 Pre-primary and primary education 0911 Pre-primary education 0912 Primary education</p> <p>092 Secondary education 0921 Lower-secondary education 0922 Upper-secondary education</p> <p>0930 Post-secondary non-tertiary education</p> <p>094 Tertiary education 0941 First stage of tertiary education 0942 Second stage of tertiary education</p> <p>095 Education not definable by level 096 Subsidiary services to education 097 RandD Education 098 Education (not elsewhere classified)</p>

The basic functional classifications contained in the IMF COFOG treat the assignment of functions and expenditure responsibilities as a one-dimensional choice. However, if functions are considered one-dimensional then the entire responsibility for each public sector function (whether at the level of a division, group or class) would seemingly have to be assigned in whole to the same government level. In reality, however, many publicly provided services are more complex in nature. Similarly, the reason for public provision of these goods and services is equally complex.

Let us take, for instance, the example of primary education. The provision of public primary education is a relatively simple activity, which in most countries can be—and has been, for many centuries—provided and produced at the local government level. At the most basic level, primary schools are operated by the government in many countries because the cost per pupil of collectively providing public primary education to a community with, say, 500 children is lower than the cost per pupil if each pupil would have to be schooled individually. Based on such analysis, a simplistic or naïve approach to functional assignment would assign the responsibility for primary education fully and exclusively to the local government level.

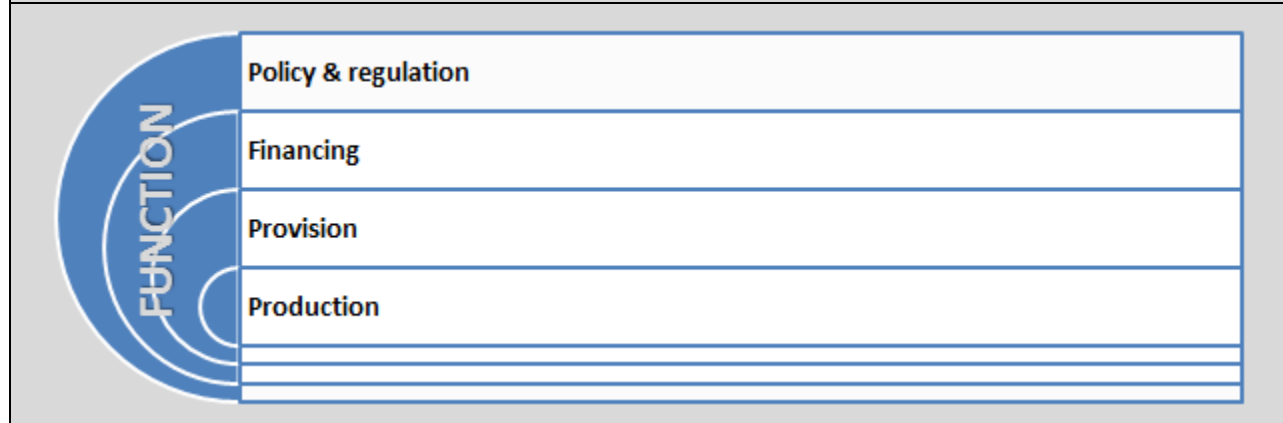
However, assigning the responsibility for primary education wholesale to only one level of government would fail to recognize that the delivery of primary education is multi-faceted and that the responsibility for actually operating the primary schools is only one dimension of the responsibility for primary education. For instance, beyond the efficiency argument made above, primary education has an important equalizing element: many societies perceived it as a citizen's right to have access to a minimal level of primary education. This argument would not have been taken into account if the entire responsibility for delivering primary education was assigned to the local government level, as poor local governments may not be in a position to deliver an equitable or minimal level of education. In addition, the process of education may involve inter-jurisdictional spillovers or externalities: the nation as a whole may benefit from this child's education, among others, because an educated citizen is typically wealthier and pays more (central government) taxes. Based on the logic that redistributive activities and those involving nationwide market failures should be pursued by the central government, does this mean that (following the subsidiarity principle) the entire responsibility for the provision of primary education should be fully assigned to the central government level instead? Answering the question requires us to deconstruct or unbundle functions such as public education in a number of dimensions. Doing so will then allow us to assign the "unbundled" dimensions of a specific function to different government levels in accordance with the subsidiarity principle.

Functional responsibilities are multi-dimensional. Before proceeding, it is important to clarify that the responsibility for delivering primary education –as well as any government function- can be subdivided into four different dimensions, namely (i) the responsibility for policy-setting and regulation, (ii) the responsibility for financing, (iii) the responsibility for provision, and (iv) the responsibility for production. This is the common approach to "unbundling" public sector functions in the fiscal decentralization literature (Figure 2):

- In assigning the responsibility of a public function, the responsibility for determining the policies and regulations that are associated with that function can be separated from the other dimensions of delivering that good or service.
- Likewise, which government level should finance the delivery of a public good or service is an element or dimension of the expenditure assignment decision that can be assigned separately from the other dimensions.
- In the expenditure assignment decision, provision refers to the administrative or governance responsibility for ensuring that a good or service is provided.
- Finally, production in this case can be defined as the responsibility to ensure that the good or service is physically delivered or produced.⁹

⁹ For instance, in the case of solid waste collection, the responsibility for provision may be assigned to the local government level. However, the local government may choose to contract out the production of residential garbage collection to a private firm. In that case, the local government *provides* the services, whereas the contractor *produces* the service.

Figure 2. Unbundling the responsibility for a function: four main functional dimensions



Rather than treating public services such as primary education as one-dimensional (and thus trying to assign the entire function to a single government level), we can apply the subsidiarity principle separately to each of these four dimensions. What we find is that while in some cases it is prudent to assign all dimensions to the same government level, in many cases, we might assign different dimensions of a good or service to different government levels. In the case of primary education, for instance, the responsibility for:

- the policy and regulation dimension (including determining the curriculum and education policy and standards) may be assigned to the central level;
- the financing of the service may be assigned to the central level, in order to ensure that education resources are distributed equitably across the national territory;¹⁰
- the provision and production may be assigned to the local government level (or the production may be outsourced to public “charter schools” or non-public school (e.g., faith-based schools or other independent non-for-profit schools)).¹¹

If all the dimensions associated with the delivery of a good or service are assigned to the same government level, this is referred to as an “exclusive” central or local government function. In contrast, when the dimensions associated with the delivery of a publicly provided good are assigned to different government levels, this is referred to as a shared, joint or “concurrent” function.

Further unbundling functional responsibilities: the elements of the provision of a function. In addition to determining which government level or administrative tier is responsible for the four different dimensions of a specific function (i.e., policy and regulation, finance, provision and production), it is often useful to consider the fact that—not unlike private sector production of goods and services—the

¹⁰ This does not necessarily mean that education funding should necessarily be controlled by central government, or that the central government should make the final expenditures or outlays for primary education. For instance, in most countries where the provision of education is a devolved function, central responsibility for primary education funding is realized by the central government providing local government level conditional or unconditional grants that are sufficient to provide a certain level of educational services,

¹¹ The assignment of responsibility for different dimensions of a function is explored in greater detail below.

provision of a public service is achieved by combining a number of different types of inputs in order to deliver a specific public sector output.¹² Similarly, five different types of service delivery inputs are often used in the delivery of public services:

- **Functionaries.** Which entity (or entities) has actual responsibility for local service delivery staff? Who is responsible for the hiring and firing of health workers, teachers, and other local officials? Who is responsible for local human resource management and paying their salaries and benefits? To whom do they report?
- **Operation and maintenance.** In addition to wage expenditures, the provision of a function typically requires a series of other (non-wage) recurrent expenditures. Which entity (or entities) has actual responsibility for service delivery operation, maintenance and related expenditures?
- **Supplies.** Who is responsible for procuring and providing the supplies (e.g., the medical supplies, school books, learning materials, and other inputs) that are provided directly to clients as part of the service delivery process?
- **Facilities.** Which entity (or entities) has actual responsibility for service delivery infrastructure (school buildings and health facilities)? Who procures them? Who is the legal owner of the buildings? Who maintains or rehabilitates them?
- **Coordination, monitoring and community mobilization.** Which entity (or entities) has actual responsibility for coordinating the other four input streams, for performance monitoring of front-line services, and for community mobilization?

It should be noted that in the real world, different governance levels or entities are often responsible for providing each of these different inputs into the service delivery process. Different inputs frequently flow from the central public sector to the local level and/or that are controlled and managed separately from each other. For instance, it is not unusual in developing and transition countries for the (national) Civil Service Department (or an equivalent agency) to determine the staff establishments not only of central government ministries (and their deconcentrated offices), but also the number of local staff that each local government is permitted to hire. At the same time, central line ministries may be involved in providing (in-kind) supplies such as school books or medical supplies, while a National Planning Commission may be involved in setting the parameters for local government capital (infrastructure) investments.

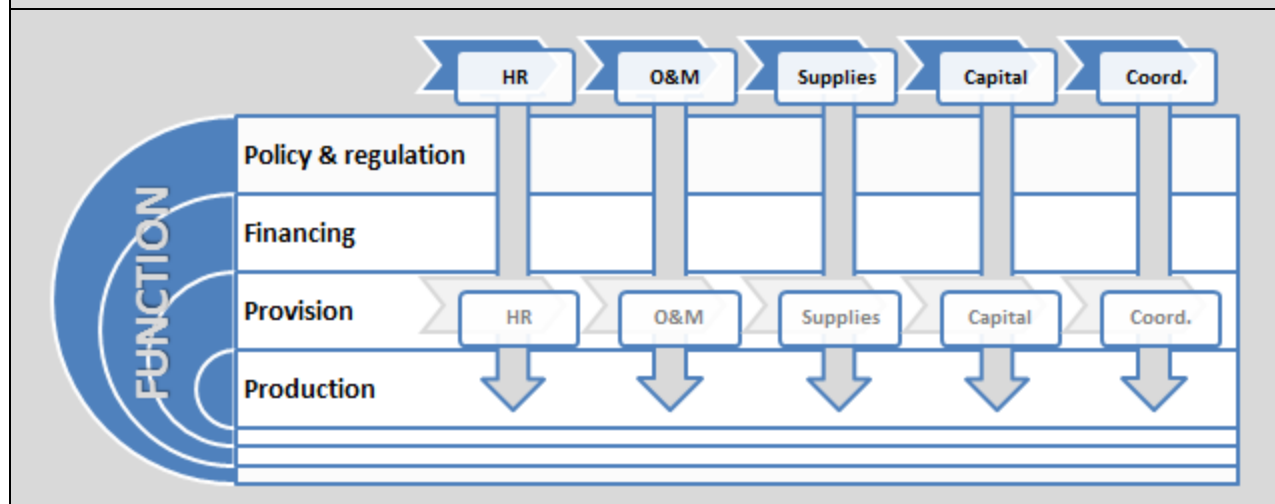
The breakdown of functional responsibilities by the economic nature of the inputs noted above generally follows the IMF GFS expenditure classifications (IMF, 2001), as three out of the five different types of service delivery inputs noted above have economic budget classification categories that are clearly associated with them.¹³ As shown in Figure 3, not only may the responsibility for providing each of these inputs be assigned to a different government level or administrative tier, in fact, a whole separate legislative assignment of powers and functional responsibilities may exist for different types of

¹² For instance, when a factory produces shoes, it uses labor inputs, raw materials and intermediate inputs, land and capital goods (buildings and machinery) and entrepreneurship and managerial inputs.

¹³ In addition to the IMF economic classification of expenditures, this classification builds on the mantra that decentralization reforms are said to revolve around three F's: functions (the *de jure* assignment of functions and expenditure responsibilities, which requires some degree of organizational or political decentralization), functionaries (administrative / human resource decentralization) and funds (fiscal decentralization). IMF's (2001) main expenditure categories include wage expenditures (spending on functionaries); spending goods and services (O&M and supplies), and capital expenditures (spending on facilities).

inputs. For instance, the institutional assignment of responsibility for the unbundled aspects of “functionaries” or “HR” (e.g., policy and regulation, financing, provision and production of local health staff) typically relies not only the country’s Decentralization Law or Local Government Act, but also on the country’s Public Service Act.

Figure 3. Unbundling the responsibility for a function: the elements of the provision of a function



Identifying who has authority over each of these different elements of the function (along with the respective funding flows) allows us to say with some degree of certainty which entities (government levels or deconcentrated administrative bodies) actually (*de facto*) have functional control over the different elements of sectoral service provision.¹⁴

Measuring the *de facto* assignment of functional responsibilities. As noted above, a country’s legal or *de jure* assignment of functional responsibilities can be found in the constitution or in the legal framework. However, in many countries, there is a substantial difference between the legislated functional responsibilities and the actual or *de facto* assignment of functions.

In line with Breton’s (2015) observations noted earlier, the gap between the legal situation and the actual situation arises since just because a local government level or a local administrative tier is assigned the *responsibility or mandate* over a particular service or function this does not necessarily mean it has the *power, authority or discretion* over the (human and financial) resources to actually deliver the service.

The degree of *de facto* responsibility that a level or tier has over a function corresponds closely (although not perfectly) to the degree to which each level or tier has budgetary control over the

¹⁴ Ahmad (2015: 207) and Dafflon (2015: 186) develop similar categorizations of functional responsibilities. Ahmad takes the analysis one step further by proposing a gradual hypothetical assignment of functions in a typical decentralizing country.

expenditures related to that function.¹⁵ In fact, we would argue that ***a government entity or administrative tier does not have effective responsibility (or functional control) over a service or public function unless the entity has control over the resources needed to perform that function.*** Thus, the pattern of local public sector expenditures—which administrative tier or local government entity funds what—often provides important insights into who is *de facto* responsible for the delivery of public services in a country.

For instance, imagine that in Country X the Local Government Act states that primary education is the responsibility of local governments. When we examine the budgets of local governments in Country X, we indeed find some level of spending on the construction, operation, and maintenance of primary schools. However, upon examination of the central government budget, we find that the salaries of all teachers and school administrators—which turns out to be 70% of all primary education spending in the country—are paid directly from the Ministry of Education budget at the central government level. In addition, we may discover from further budget analysis that the Ministry of Education is also responsible for procuring all textbooks and school materials, and provides these learning materials in-kind to the local governments (who in turn, is instructed to provide them to the school level).

This scenario provides a pretty clear example of a situation where, in spite of the legal provisions, the central line ministry retains a very important *de facto* role in provision of primary education. In fact, the share of expenditures under the control of each level or tier can be used as an indicator of the relative share of responsibility that each level or tier has over the delivery of public services.

In fact, when we view the assignment of functional responsibilities and authority in a *de facto* manner, we find that public services are often provided and funded through a combination of four different ‘vertical’ or intergovernmental mechanisms at the same time. For instance, the provision of health services at the clinic level may be brought about by a combination of deconcentration (a deconcentrated District Health Office may be authorized to manage and oversee local health facilities, including the facilities’ staff); devolution (support for the rehabilitation of a health facility may be provided by elected local governments that operate in parallel to the deconcentrated structure); delegation (an NGO supported by the Ministry of Health may engage in health promotion in local jurisdictions); and direct provision of service delivery inputs by the central line ministries (e.g., the in-kind provision of medical supplies).

In accordance with the concept that *de facto* functional responsibilities are revealed by the proportion or share that each entity budgetary discretion over sectoral expenditures (and as further discussed in Section 6), DeLoG (2015) presents vertical public sector expenditure profiles for the health and education sectors in selected developing and transition countries.

An important caveat should be placed with the assumption that *de facto* functional responsibilities are proportionate to the degree to which each government level or administrative tier engages in sectoral expenditures for that function, as this approach may actually overstate the level of decentralization in a

¹⁵ A higher-level administrative level may direct a lower-level administrative tier to coordinate the implementation of one or more of its responsibilities, but unless the lower-level entity is granted a degree of autonomy and discretion and is given some degree of control over the financial resources to perform the tasks or deliver the service, the lower-level entity cannot be held responsible for the functions assigned to it.

country (Ebel and Yilmaz, 2002). Consider the case in which (i) local governments pay all teacher salaries within their jurisdiction, (ii) these salaries are financed by a fully earmarked grant provided by the central government; and (iii) all human resource decisions with respect to these teachers (hiring, firing, salary level, promotion, and so on) is made by central government officials. Even though the local government in this case essentially functions like a post office and lacks any discretion over these resources, the local public sector expenditure methodology counts these “decentralized-in-name-only” expenditures as real local government expenditures. As such, any assessment of functional assignments should be done together with an assessment of the political, administrative and fiscal discretion and accountability that local governments have over their resources and operations (Boex and Yilmaz, 2015).

Unbundling of sector-specific operational decisions. Public service delivery—including the delivery of education and health services—involves a large number of operational decisions that are, taken together, critical for the effective delivery of localized public services. In addition to unbundling the responsibility for a function on the basis of functional classes and based on the nature of the inputs that together combine to form the “provision” of a services, it is also possible to “unbundle” the assignment of functional responsibilities based on the assignment of operational decision-making powers. Because each different public service or function has its own unique characteristics, each service delivery sector tends to have its own ideas about “unbundling”.

For instance, within the health sector, the multifaceted nature of health systems and the spread of direct and indirect responsibilities across multiple actors and facility levels poses unique challenges in the management of systems health. In response, over the past several years, the World Health Organization (WHO) and its partners have worked to reach a broad-based consensus on key indicators and effective methods and measures of health systems capacity, including “inputs”, “processes” and “outputs”, and to relate these to indicators of “outcome”. The resulting WHO (2010) framework describes health systems in terms of six core components or “building blocks”: (i) service delivery, (ii) health workforce, (iii) health information systems, (iv) access to essential medicines, (v) financing, and (vi) leadership/governance.¹⁶

Within the education sector, the categorization of operational decisions prepared by OECD (2004) as part of its “locus of decision-making” in education can provides one of the sector’s main standard for discussions surrounding functional assignment. The “locus of decision-making approach in education (OECD,2004) considers that the delivery of basic education involves 38 key issues (grouped into four main categories) over which operational decisions need to be made, including decisions about:

- (i) the organization of instruction—bodies determining the school attended, decisions affecting school careers, instruction time, choice of textbooks, grouping pupils, assistance of pupils, teaching methods, assessment of pupils’ regular work;
- (ii) personnel management—hiring and dismissal of staff, duties and conditions of service of staff, fixing of salary of staff);
- (iii) planning and structures—creation or closure of a school, creation or abolition of a grade level, designing programs of study, selection of subjects taught in a particular school, selection of

¹⁶ Alternative classifications of functional responsibilities within health service delivery exist. For instance, see WHO (2001) and WHO (2004).

- programs of study offered in a particular school, setting of qualifying examinations for a certificate or diploma, credentialing; and
- (iv) resource allocation and use—allocation of resources, use of resources.

While these sectoral lists of “unbundled” operational decisions play an important role in ensuring that functional assignments are effectively operationalized, these detailed task assignments are not necessarily an obvious starting point for a discussion surrounding the decentralization and localization of public service delivery. Before detailed decisions about the operationalization of service delivery tasks can be made, it is necessary to first reach agreement about the overall structure of the sectoral service delivery system and the general assignment of authority and responsibility over the key inputs that combine to form service provision. Only then will it become important to decide how specific parts of service delivery should be operationalized.¹⁷

Functional assignment in the context of multi-dimensional expenditure responsibilities. As noted above, when all the dimensions associated with the delivery of a good or service are assigned to the same government level, we refer to an “exclusive” central or local government function. In contrast, when the dimensions associated with the delivery of a publicly provided good are assigned to different government levels, we refer to this function as a shared, joint or “concurrent” function.

At one extreme are exclusively central government functions, where all facets of the public service should be in central government hands (e.g., national defense); it would be inefficient to assign any dimension of these central government services to the subnational level. At the other extreme lie exclusive local government services, such as local solid waste management and the operation of local markets, where under the subsidiarity principle, all dimensions of the service can efficiently be assigned to the local government level.

In between these two extreme cases lie a number of different “concurrent” functions or functions that are jointly assigned to two or more government levels, which can take on numerous forms. A typical example of a concurrent function is basic education, where responsibilities for policy and financing are typically assigned as central government responsibilities (which is usually considered a national policy area due to the redistributive nature of education and due to its impact on economic growth), whereas provision and production of basic education in most countries is assigned to the local government level (since the local level is typically the lowest government level that can provide and produce basic education).

Applying the subsidiarity principle to each of the four main dimensions of a functional responsibility allows important observations regarding what dimension of service delivery should be dealt with at which government level:

Policy and regulation. The development of policies, regulations, and service delivery standards often requires a high degree of scale economies. It would be duplicative and inefficient for each local

¹⁷ An obvious risk of reversing the order of this sequence is that in the absence of an overarching assignment of functional responsibilities, it is likely that local officials simply will be relegated to “participating” in the planning and delivery of local services, rather than being capacitated and assigned the responsibility to actual “own” the planning and delivery of local services.

government to come up with their own policies and regulatory framework. For most sectors and public services, defining policies and developing regulations is best done at the central level; where necessary, the center may simply leave room for local flexibility. Besides, for reasons of equity, national governments often have an interest in ensuring a certain degree of uniformity in service delivery standards across the nation (such as primary education and basic health services).

Financing. Once local governments are assigned the responsibility to provide local services, local governments will choose to provide an optimal level of public services when there is a close relationship between the benefits derived from these services and the cost of providing these services. This relationship can be achieved when citizens residing in a particular jurisdiction that enjoys the benefits received from the public services provided by their local government also pay for these locally provided services.

However, the benefits from public services often spill over outside the jurisdiction of a single local government. For instance, as already noted earlier, in addition to the individual student and the local government in which he or she resides, the country as a whole derives benefits from a more educated populace. Similarly, to the extent that public services are provided for equity reasons, there is an important role for the central government in ensuring equitable access to financial resources. When a substantial share of benefits befall the country as a whole, the central government can either deliver the service uniformly across the national territory, or it can provide intergovernmental grants to ensure that local governments are able to afford to deliver services up to a certain standard. As such, the optimal funding mechanism for local expenditures depends critically on the nature of the service being provided. This is captured by the concept that “finance should follow function” (Box 2).

Box 2. Finance should follow function: The conceptual framework for subnational government finance

Expenditure assignments are understood to form the first pillar of any decentralized fiscal system. Once these expenditure assignments have been determined, the next challenge is to determine how each of the functions and responsibilities assigned to subnational levels is financed. The three available alternatives include, first, own (regional or local) revenues sources; second, intergovernmental fiscal transfers; and third, subnational borrowing.

Each of these funding modalities play important but distinct roles in the system of subnational government finance. Thus, a critical question in designing a local government finance strategy is: what determines how each local government activity should be funded? The short answer to this question is the mantra that “finance should follow function”.

The notion that “finance should follow function” could be considered an extension of the subsidiarity and fiscal equivalence principles, when these principles are applied to the financing of subnational government services. These principles, when combined, suggest that subnational government services should be financed by the financing mechanism that most closely maintains the link between the benefit of public services and the cost of delivering the service, that can do so in an efficient manner. Following this principle, we can broadly classify four types of local government expenditures:

	Type of local government service	Appropriate revenue source
1	1. Rival and excludable local services (e.g., electricity or piped water) without social impact	User fees
2	Non-excludable local services with local spillovers (e.g., solid waste collection, local parks, street lighting)	Local taxes, e.g. property rate (quasi-user fee)
3	Non-excludable local services, with inter-jurisdictional spillovers (e.g., main urban roads)	Combination of local taxes and intergovernmental fiscal transfers
4	Locally delivered services with extensive inter-jurisdictional externalities or equity impact (e.g., basic education, local health services, agricultural extension, pro-poor urban and rural programs)	Intergovernmental transfers
5	Capital infrastructure	Local government borrowing; capital grants

Provision and production. Unless a good or service is technically highly complex or has a large minimum efficient scale, production and provision of many publicly provided goods or services can often be done at the local level. From a technical standpoint, local governments in most countries are able to efficiently operate and maintain primary schools, health clinics, agricultural extension offices, and so on. In fact, in some cases the provision may be efficiently assigned to the local government level, but it might be hard for every local government jurisdiction to efficiently produce the service. In these cases, the production of such goods or services may be placed in the private sector (through out-sourcing), or through alternative production arrangements (see Box 3).

Box 3. Scale economies and alternative modes of producing local government goods

The existence of scale economies is often used as an argument (or a pretense) to prevent devolution of an expenditure responsibility to a lower level of government. Since subnational government units at any local level typically vary in size, it is not uncommon for opponents of decentralization reform to argue that, especially the smaller, local governments are not able to take on the burden of government services that display a certain degree of scale economies. Such concerns have unnecessarily hindered the implementation of decentralization reform since there are several ways in which jurisdictions (particularly smaller ones) may circumvent the negative consequences of scale economies.

The crux of the argument here is that just because local governments have been assigned the responsibility to fund and provide a certain government service, this does not necessarily mean that they have to produce this good or services themselves. There are three ways in which a local government jurisdiction can provide a good or service without producing it on its own and still retain the benefits of local policy discretion and accountability:

- **Contracting with the private sector.** A local government may choose to contract with a private provider to produce a certain local government service, such as garbage collection or the operation of the local market. By doing so, the benefits from fiscal decentralization (including better a match between service provision and local preferences, as well as increased local accountability) are retained, while also being able to capture the scale economies and experience brought to bear by large, specialized private service providers.
- **Contracting with other local governments.** Another possibility to avoid the trappings of scale economies is for two smaller jurisdictions to collaborate on the production of a certain public good. For instance, one

local jurisdiction that is too small to provide secondary schooling in a cost-effective manner on its own might contract with a neighboring local government and send its students to the neighboring district. Alternatively, the two districts might establish a covenant to jointly run a secondary school for the education of children from both jurisdictions.

- **Special service districts.** In certain cases, special service districts could be formed for the provision of certain local public goods. This is particularly the case in situations in which several local governments are inextricably linked by the provision of a certain local government good or service, such as a water district that covers several local government jurisdictions. Again, special districts allow a system of intergovernmental relations to resolve problems with scale economies without altogether abandoning the benefits of a decentralized system of local government.

As shown in Box 3, there is a clear distinction between “provision” and “production” in service delivery, which helps us to address the misconception that local governments are not capable of providing a service merely because they lack sufficient economies of scale to do so. Therefore, recognizing the conceptual separation between provision and production allows local governments to be responsible for the provision role in service delivery (thus benefiting from demand-responsiveness in service delivery through local decision-making) while still capturing the benefits from scale economies by permitting the production of the service to be handled by the private sector, or for the service to be delivered by two or more local governments together (acting as voluntary service delivery clubs).

The pros and cons of centralization and decentralization: real world examples from the education sector. In his recent book, *The Rebirth of Education* (2013), Professor Lant Pritchett argues that increases in the quantity of schooling for students in poor countries over the past 10-15 years have not necessarily translated into proportionate gains in education, learning, or achievement. This situation is due to poor incentives and weak accountability in the top-down educational systems around the world. School reforms that imitate successful systems fail to take into account the organic nature of successful school systems that cause the attributes of successful schools to translate into successful outcomes. The degree to which functional responsibilities are assigned in a decentralized manner plays an important part in this discussion.

In his book, Professor Pritchett argues that education systems can be like ‘spider systems or like ‘starfish systems.’ The basic distinction is between a top down organization—following the metaphor of the spider—and the starfish as a metaphor of a decentralized system, where individual units respond to local conditions.

In a “spider system”, all of the resources of the spider web, however spread out they are, merely serve to transmit information to one spider who synthesizes that information and responds with the resources of the system. So, if a bug gets caught in the web, the spider crawls out and gets it. But the entire web is in fact an ancillary to the brains of the spider, who is at the top of the system. The danger of a spider system is that when the spider gets disrupted or dies, the whole system falls into dysfunction. In addition, the functioning of the spider system is limited depending on who the spider is.

In contrast, the starfish is a creature that actually has no brain. It is neurally connected, but a starfish moves because the individual units of the starfish sense something and if they sense more food they try to pull in that direction. And if the other side is not pulling as hard, the starfish moves in the direction of

food. So the starfish is really a metaphor of a decentralized system, where individual units—by responding to local conditions—create the properties of the system. And the beauty of a starfish is that if you cut a starfish up into 5 bits, you get 5 starfish.

Professor Pritchett notes that centralized (“spider”) systems do some things well. In the history of schooling, spider systems have done two things very well. One thing spider systems do well is logistics: for instance, constructing school buildings and posting teachers. If the local level does not really require anybody to think, but rather only to implement—say, to build 100,000 identical schools—, then designing a program that dictates exactly the design of the schools, and then relies on the local level only to implement it, works well. Similarly, central governments are very good at hiring plenty of teachers. In fact, the expansion of schooling is one of the triumphs of our time, and it was carried out mostly logistically. In fact, schooling in poor countries has expanded so rapidly that the average Haitian and Bangladeshi had more years of schooling in 2010 than the average Frenchman or Italian had in 1960.

The second thing that a “spider” does well is to control what goes on in the schools, which has coincided with governments seeking control over the socialization of children. As they sought to control the socialization of children, many governments in developing countries adopted a very spiderlike system in which all the key decisions got forced to a higher and higher level, in order to provide the control that newly nationalizing states and others felt that they wanted.

Something that “spider systems” are typically not very good at, however, is to ensure accountability. In his book, Professor Pritchett cites the example of several school visits he made in India, in 1995, where he found that nearly all the teachers in the schools weren't actually the people hired to be in the schools. They were all subcontractors. In other words, the wage of the teacher was so much higher than the wage it really took to put someone in the classroom, politically connected individuals would get the job and then they would basically subcontract out the job to others. The top-down systems failed to detect and correct this problem. Similarly, Professor Pritchett cites visiting schools in Egypt, where secondary schools have a very high-stakes test. However, he found that the teachers would primarily be interested in their much more lucrative night job, which was providing individual or group tutoring lessons.

Other studies confirm these accountability challenges at the local level. Chaudhury, et al. (2006) analyze results from surveys in which enumerators made unannounced visits to primary schools and health clinics in Bangladesh, Ecuador, India, Indonesia, Peru, and Uganda, and recorded whether they found teachers and health workers in the facilities. Averaging across the countries, about 19 percent of teachers and 35 percent of health workers were absent. The survey focused on whether providers were present in their facilities, but since many providers who were at their facilities were not working, even these figures may present too favorable a picture. For example, in India, one-quarter of government primary school teachers were absent from school, but only about one-half of the teachers were actually teaching when enumerators arrived at the schools.

5. Decentralization as a mechanism to improve accountability at the local level

Whereas decentralization of power and responsibilities to local levels was one of the dominant themes in the development policy literature during the decade of the 1990s, the hypothesis that a more decentralized public sector is by definition more efficient, more responsive, and will achieve higher economic growth is increasingly being challenged where evidence is lacking.

This does not mean, however, that decentralization as a development issue is no longer relevant. Policy issues such as governance, corruption, transparency, and participation are all increasingly popular topics in the development practice and literature, albeit often under the broad header of “accountability.” While some of that emerging literature on accountability is devoted to the accountability of central governments, the topic is equally relevant at the sub-national level where most public services are provided (Schroeder, 2003). A second-generation fiscal federalism literature has emerged that argues, amongst other points, that, “institutions matter” in achieving the benefits of decentralization (Weingast, 2009; 2013).

In fact, the United Nations, through UN-HABITAT, adopted a series of international guidelines on decentralization and strengthening of local authorities in 2007. These guidelines recognize that the subsidiarity principle constitutes the rationale underlying decentralized governance and reaffirms that public responsibilities should be exercised by those elected authorities closest to the citizens, which are capable of performing these responsibilities efficiently (Box 4). These guidelines specifically recognize that devolution (“political decentralization”) to the local level is an essential component of an effective local governance system, as a combination of representative and participatory democracy is required to ensure that local authorities are responsive and accountable. Similarly, the European Charter of Local Self-Government (Council of Europe, 1985) mandates that European Union member states to adhere to the subsidiarity principle in their intergovernmental structure and functional assignments.¹⁸

Box 4. International Guidelines on Decentralization and Strengthening of Local Authorities

In 2007, UN Habitat adopted guidelines on decentralization and strengthening of local authorities. These guidelines address four dimensions of effective decentralization by devolution: governance and democracy, powers and responsibilities, administrative, financial resources and capacities of local authorities.

- Political decentralization to the local level is an essential component of democratization, good governance and citizen engagement; it should involve an appropriate combination of representative and participatory democracy (art. 1)
- Local authorities should be acknowledged in national legislation, and, if possible, in the constitution, as legally autonomous sub-national entities...(art. 28)
- The principle of subsidiarity constitutes the rationale underlying to the process of decentralization. According to that principle, public responsibilities should be exercised by those elected authorities, which are closest to the citizens (art. 15)

¹⁸ Article 4(3) of the Charter reads: “Public responsibilities shall generally be exercised, in preference, by those authorities which are closest to the citizen. Allocation of responsibility to another authority should weigh up the extent and nature of the task and requirements of efficiency and economy.”

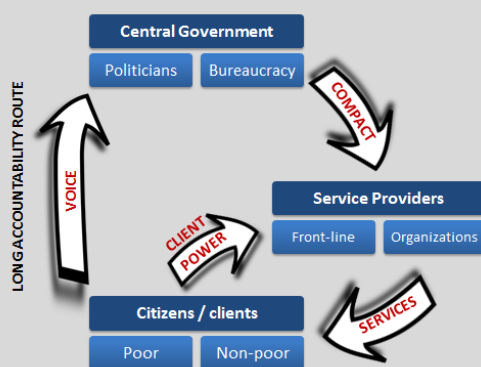
- Local authorities should freely exercise their powers, including those bestowed upon them by national or regional authorities, within the limits defined by legislation. These powers should be full and exclusive, and should not be undermined, limited or impeded by another authority except as provided by law (art. 33)
- Local authorities should be allowed to determine as far as possible their own internal administrative structures... and should have full responsibility for their own personnel (art. 43 and 44)
- Effective decentralization and local autonomy require appropriate financial autonomy. Local authorities' financial resources should be commensurate with their tasks and responsibilities and ensure financial sustainability and self-reliance. (art. 48 and 49)

Source: UN Habitat (2007).

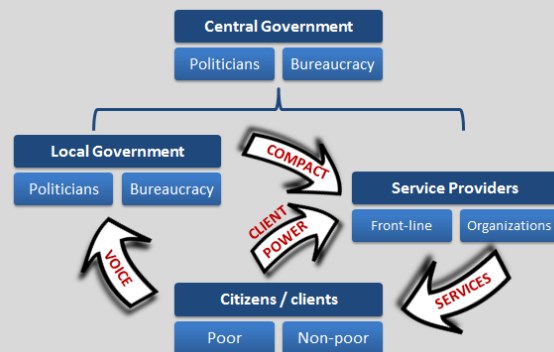
The World Development Report 2004, entitled “Making Services Work For Poor People” investigates how countries can accelerate progress towards the Millennium Development Goals by making services work for poor people (World Bank, 2003). It notes that “[s]uccessful services for poor people emerge from institutional relationships in which the actors are accountable to each other” (World Bank 2003:46). Thus, to the extent that decentralization provides a space for greater accountability at the local level, decentralization offers an opportunity to improve service delivery outcomes at the subnational level. Decentralization (especially devolution) may enhance accountability in a number of ways. Decentralization can enhance social accountability by increasing the contestability of public sector decisions and by improving the degree of transparency of the public sector. In addition, devolution introduces the potential greater local checks and balances by introducing oversight by elected representatives at the local level, and greater top-down oversight and accountability may be achieved when a vertical separation of power is introduced.

Figure 4. Accountability for the delivery of localized services: centralization versus decentralization

Panel A: Centralized accountability system



Panel B: Decentralized accountability system



Source: Prepared by author based on World Bank (2003) and Schroeder (2003).

The long accountability route. In a centralized accountability system (Figure 4, Panel A) individuals and households have two distinct roles: as citizens and as direct clients. As citizens they participate in political processes that define collective objectives; they also strive to control and direct public action in accomplishing those objectives (World Bank, 2003). As direct clients of service providers, individuals and households also exert direct pressure (“client power”) on service providers to get clean water, have their children educated, and protect the health of their family.

According to the World Bank (2003), the direct link of client power is frequently missing in public sector production, so successful public production relies on “long-route” accountability.¹⁹ What does that take?

The main way citizens have *voice* in a democratic country is through the elections of popular representatives, such as Members of Parliament. In most representative democracies, a degree of separation exists between the legislature and the executive branch, resulting in a system whereby Members of Parliament act on behalf of their constituents not only as legislators, but also by monitoring the performance of the national executive (particularly in their constituency) and by providing a check on the power of the executive branch. The checks and balances provided by parliament are more pronounced in presidential systems than in a Westminster system.²⁰

The expression of voice does not necessarily result in better public services in a centralized system (World Bank, 2003:55). At the central level, legislators and policymaker must care about localized service delivery outcomes, including those for poor people. That concern needs to be transmitted effectively to the public agencies that receive public resources to provide these services. And the public agencies must hire technically qualified providers motivated to provide the services. Service delivery failures result when any of these links in the long accountability route are weak or broken.

A failure of the compact between central-level policy makers and local-level implementers occurs in a centralized system when the central administration fails to assign and communicate clear responsibilities for outputs or outcomes to the public organization in charge of localized delivery of services, and when the center fails to properly enforce any responsibility (World Bank, 2003:56). One common reason for such compact failure is excessively long bureaucratic chains of power (discussed below). In addition, compact failures often arise because of a lack of separation of responsibilities: central line ministries often have the dual responsibility of setting sectoral goals and implementing these goals. It should come as little surprise that central line ministries are not necessarily objective when they monitor the performance (failures) in localized service delivery by their own ministry.

Introducing local government to shorten the accountability route. One obvious way to shorten the “long accountability route” is to bring the elected representation closer to the people (Figure 4: Panel

¹⁹ Client power is much greater in private provision, where clients pay a fee for service. Public services can equally achieve a higher degree of responsiveness to client need by relying on fee-for-service payments. However, since the poor are unable to pay such fees, their client power is typically quite limited. Schemes such as “results-based finance” in health services can restore a degree of client power and enhance the motivation of health workers to serve the poor. For instance, see Gruber, Hendren and Townsend (2013) for the case of health services in Thailand. For a general background on the topic, see <http://www.rbfhealth.org/>.

²⁰ In a Westminster system, the *de facto* executive branch is usually made up of members of the legislature with the senior members of the executive in a cabinet led by the head of government; such members exercise executive authority on behalf of the nominal executive authority (e.g., the Crown).

B). If service providers are placed under the control of a local government, this would potentially enhance the voice of the people. In addition, the local level council would be in much better position vis-à-vis the national legislature to hold local service providers accountable than national parliament.

It is commonly acknowledged that improving accountability through decentralization is no panacea—there are enormous risks to decentralization that could worsen service delivery (Prichett and Pande, 2006). Indeed, badly designed decentralization has major fiscal risks and missed opportunities, and getting functional assignments, functionaries, and funding properly aligned is difficult.

In addition to the technical challenges of getting decentralized accountability right, World Bank (2003) notes that institutional reforms such as decentralization change power relationships among actors, and that political economy factors generally do not favor reforms that improve services for poor people. Improving localized service delivery through greater accountability require upsetting entrenched interests, which have the advantage of inertia, history, organizational capability, and knowing exactly what is at stake. Policymakers and providers are generally more organized, informed, and influential than citizens, particularly poor citizens. This means that any effort to improve the responsiveness of the (local) public sector should not only focus on public sector reforms, but equally, on creating a greater demand for information and ensuring greater participation by civil society organizations and citizens.

Shortening the bureaucratic chains. As noted above, improved accountability is not just about amplifying the voice of the people to ensure political or legislative oversight over the executive; accountability also requires effective and responsive bureaucratic decision-making and oversight.²¹ As such, it is reasonable to assume that the responsiveness of the public sector is inversely related to the number of official levels or tiers that a complaint or a concern has to travel before it reaches a decision-maker who is able to fix the problem.

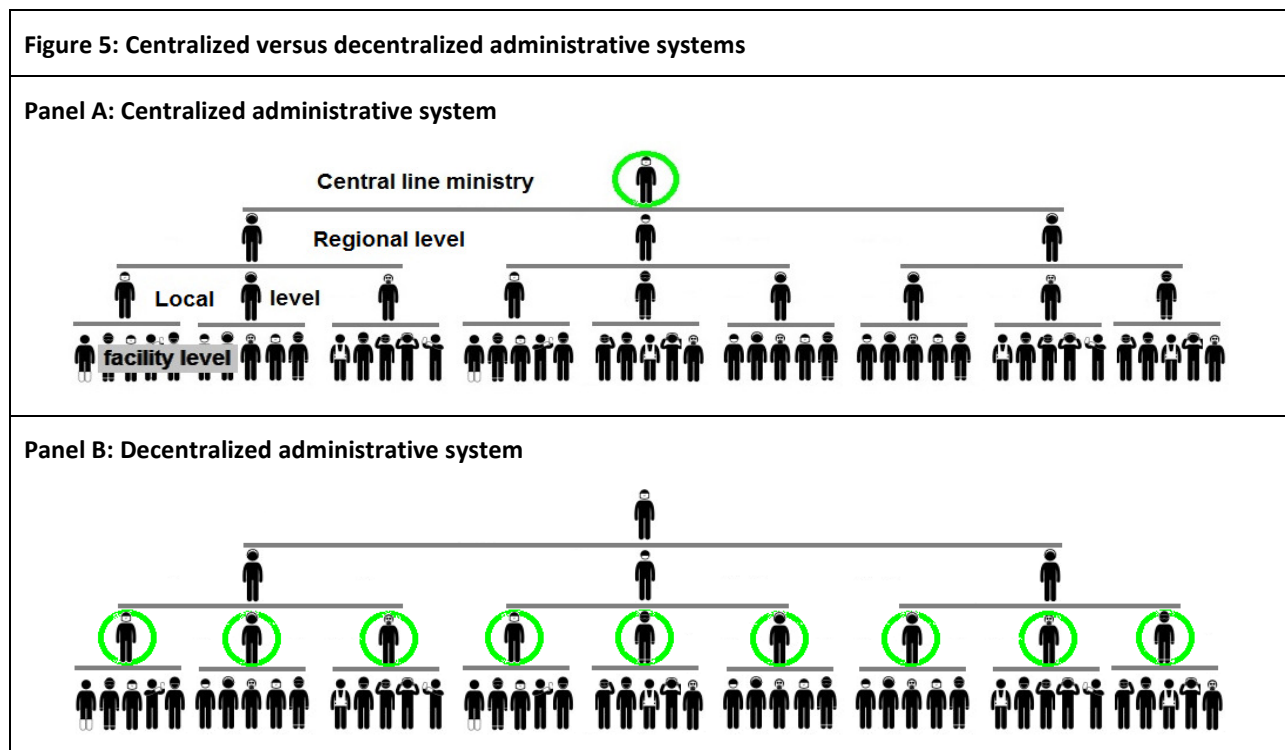
While highly effective, colonial administrative structures were constrained by limits on transportation, communication, and information technology, which complicated control and oversight between different tiers in the administrative structure. In order to ensure appropriate vertical controls and oversight, the number of officials that could traditionally be placed under a single supervisor at the next-higher administrative level was limited by the ability of the supervisor to ensure direct, personal oversight. This resulted in a high degree of vertical and horizontal fragmentation of the subnational governance structure, as each administrative level was typically divided up into no more than 10 jurisdictions below it.

Figure 5 (Panel A) illustrates a traditional bureaucratic structure, where central government instructions flow top-down and where local problems or citizens' complaints have to generally climb up the hierarchy up to key decision-makers whom are authorized to make operational decisions, before they can be implemented at the lower level (e.g., a school roof is damaged and needs urgent repair; or a teacher is chronically absent). While centralized bureaucracy is highly effective in transmitting the

²¹ The term "bureaucracy" refers to administration by a multi-tiered hierarchy of trained, nonpolitical professionals guided by written rules (thus minimizing discretion). The bureaucratic hierarchy is formed by a succession of tiers from the lowest-level worker in the organization to the highest executive, where each level has clearly defined authority and responsibilities. Invariably, bureaucratized institutions are large and complex—too large and complex for face-to-face contact involving informal oral instructions to be a feasible alternative to the formal methods of communication and command that characterize bureaucracy.

instructions from the central decision-maker down to the local level, the structure is more suitable for top-down control than for bottom-up responsiveness: while messages travel downward efficiently, messages that travel upward through the hierarchical system have a tendency to overwhelm the bureaucratic structure.

As already noted in Section 4, delivering basic services (including education and health services) involves a large number of operational decisions that are, taken together, critical for the effective delivery of localized public services. On that score, centralized bureaucratic processes are at a considerable disadvantage when compared to public sector structures that allow more decentralized decision-making. Not only do centralized political systems form too long of a route for voice and accountability, equally, centralized bureaucratic systems limit client power by providing an administrative structure that does not facilitate a flexible and responsive public sector. In contrast, the impact of a decentralized (let's say, deconcentrated) administrative structure is highlighted in Panel B.



An example might be a situation in which a school building is damaged during the budget year and needs urgent repair: how close are the citizens to the decision-maker who can actually remedy the situation and therefore be held responsible for addressing the situation? A similar example might be a teacher who is chronically absent; how many steps up in the public sector does when have to go within the public sector hierarchy to meet the actual decision-maker? As illustrated in Panel B (and discussed further in Box 5), empowering lower-level officials to make more of these operational decisions without obtaining further approval from higher levels will enhance their ability to be responsive and effective in delivering services. It also frees up the higher cadres from day-to-day operational management to engaging in and supporting more policy-focused improvement of service delivery.

Box 5. The impact of information and communication technology on the nature of bureaucratic institutions

The effectiveness of a bureaucratic system depends, among others, on the integrity and capacity of each officer to execute his or her functions, and on the integrity and capacity of each level to properly supervise the level below it. Miah (2013) argues that the ineffectiveness of the state bureaucracy in developing countries (such as Bangladesh) can be attributed in part to the fact that the country's bureaucratic structures have not evolved adequately since the pre-colonial period. The state bureaucracy in developing countries often continues to be patrimonial in nature and based on personal interests. Miah (2013) argues that politicians and bureaucrats collude in various ways, preventing the achievement of a democratic (responsive and accountable) system. At the same time, in many developing countries, the impact of fragility and militarism still exists in the state bureaucracy.

As technology evolves, it is possible to transition away from personal supervision under hierarchical structures. For instance, in many European countries, direct bureaucratic supervision has been replaced with more autonomous operating units at the lower level of the hierarchy, and with systemic performance monitoring (based on advancing information technology) higher up the chain. For instance, a single spreadsheet with school-level performance indicators for a whole district can more easily reveal (and enable an effective response to) under-performing schools than a hierarchical system of supervision and control through a hierarchical system of Assistant Education Officers. Likewise, a spreadsheet with district-level education performance indicators can more easily reveal (and enable an effective response to) under-performing local education management than a hierarchical system of supervision and control from the top down through a regional administrative level.

What is the state of knowledge on accountability and local service delivery outcomes? Promoting participation through community development projects and decentralization of services has become a central tenet of development policy (Mansuri and Rao, 2013:ix). However, some observers feel that policy making in the area is conceptually weak and that project design is informed more by slogans than careful analysis. There have also been questions about whether participatory development is effective in reducing poverty, improving service delivery, and building the capacity for collective action. Despite (or perhaps because) an overwhelming amount of research on the issue of accountability, it is hard to summarize the literature's key findings.²²

The current state of knowledge on accountability and local service delivery outcomes is still in flux. It does appear that—under certain circumstances—increased transparency, participation, and accountability can result in improved service delivery outcome. Recent studies, however, suggest that there are limitations to the effectiveness of social accountability or bottom-up (horizontal) accountability. In contrast, increased accountability through the vertical separation of powers and responsibilities appears to have made an important contribution to improved accountability.

However, it does not appear that there is a one-size-fits-all solution. An important lesson from Mansuri and Rao (2013) is its recognition of the difference between “organic” and “induced” participation and accountability. Organic participation is organized by civic groups outside government, sometimes in

²² For instance, see Mansuri and Rao (2013), and Rodden and Wibbles (2013).

opposition to it; induced participation attempts to promote civic action through bureaucratically managed development interventions. As of yet, it is unclear what the ingredients are for sustainably inducing participation and accountability through outside interventions.

Weak capacity and weak local accountability as obstacles to decentralization? In many countries, weak local capacity and weak local accountability are often cited as reasons why public services cannot be delivered efficiently at the local level. However, it should be recognized that capacity forms a “chicken-and-an-egg” problem: what comes first, the local administrative capacity, or the functional responsibility to deliver a certain service? Naturally, it is nearly impossible to build the capacity of an entity or an official to deliver a certain service in the absence of giving the entity or official a meaningful degree of discretion (along with accountability and incentives) over the performance of the particular function.

In reality, it is not unusual for local capacity and local accountability mechanisms to be constrained by a lack of political will at the central level to truly empower local government bodies (or local administrative units).²³ Dafflon (2015) suggests that responsibilities should not be taken away from local jurisdictions simply because of a lack of managerial capacity as long as the assignment of responsibilities is in line with the subsidiarity principle. In other words, functional responsibilities should not be taken back from local jurisdictions as long as local jurisdictions are of a sufficient size and scale for them to be able to acquire the necessary managerial capacity and exercise it in an efficient manner. Instead, appropriate local systems need to be put in place and meaningful capacity building efforts should be supported by central authorities before any conclusion is drawn about the inadequacy of local managerial capacity.

6. The provision of health and education services in a multi-level governance framework: linking conceptual guidance to the real world

If we applied the conceptual guidance provided in the preceding sections to the real world, how would the assignment of functions play out, and what would be able to observe in order to determine whether or not a function has been decentralized effectively?

Although several attempts have been made to establish multi-country datasets on functional assignments, these attempts have often focused on providing a catalog of the “de jure” assignment of functional responsibilities in different countries. This approach has been of somewhat limited use, as general knowledge on *de jure* functional assignments provides limited actionable guidance on how to improve the localized delivery of public services. For instance, knowing that Local Councils in Sierra Leone are legalised responsible for operating primary schools is of limited use if we subsequently find out that in reality, all teachers actually report to the Ministry of Education and their salaries continue to get paid by the central government (Edwards, Yilmaz and Boex, 2014). As such, the challenge will be to

²³ For instance, in one particular African country, a committed Minister of Local Government ordered the transfer of all directors and assistant directors from its own ministry to the local government level to become senior administrative officers accountable to the local councils. Despite the obvious increase in managerial capacity at the local level, the Permanent Secretary continued to insist that local governments lacked the capacity to administer the local functions that the same individuals previously managed at the central government level.

consider the *de facto* assignment of functional responsibilities. Although it is an imperfect metric, a useful entry point into the analysis of the *de facto* assignment of functional responsibilities is the extent to which funding for these services is funneled through the budgets of local governments or local administrative bodies.

In order to explore the *de facto* assignment of functional responsibilities in the real world, let's consider the localized delivery of health and education services in the context of a multi-level governance system. First, at what level or tier would we expect health and education services to be delivered, and second, how does this mesh with what we know about the vertical assignment of functional responsibilities in these two sectors?

Decentralized provision of health and education services: the conceptual expectation. If we were to apply the subsidiarity principle to the provision of health and education services in a country with a "typical" subnational governance structure, which government level or administrative tier in a country would be responsible for health and education services?

In line with the discussion in Section 4, the first thing that should be noted in answering this question is that the functional responsibility for these services should really be broken out into different sub-functions: for instance, the provision of public education should distinguish between the provision of pre-primary, primary secondary and tertiary education, as well as other education-related functions (e.g., teacher education). In addition, for each of these sub-functions, we should distinguish between (i) the responsibility for managing human resources (and paying teacher salaries); (ii) the responsibility for managing operation and maintenance (and related O&M expenditures); (iii) the responsibility for the provision of supplies (such as medicines and school books); (iv) the responsibility for providing capital infrastructure; and (v) the responsibility to ensure community oversight and community mobilization. As such, there most likely is not a single answer to the question "who is responsible for the local delivery of health services"?

Indeed, given the multitude of sub-functions and facets of service delivery, in fact, we would expect that different elements of each service delivery (sub-)function are assigned to different government levels. This transforms the main question from "which level or tier is responsible?" into "to what extent is each level or tier responsible for the provision of local health services and local education services?"

Before reviewing the real-world evidence on this revised question, let us consider this question in the context of "typical" developing economy and an organizational-governance structure that has a village level (average population: 10,000); a typical district level (average population: 200,000); a regional level (average population: 2 million); and a national level. For the sake of argument, let us say that our country has a total national population of 20 million.

Applying the subsidiarity principle requires us to ask whether it would be possible to efficiently deliver local health services (e.g., the construction and operation of health posts, health clinics and small local hospitals) and local education services (e.g., the construction and operation of primary and secondary schools) at the village level, which is the lowest level of organization.

Based on conceptual arguments, the answer would be that while it would be *possible* to manage all facets of health and education service delivery at the village level (whether under the auspices of a

village administration or a village council), it would be highly *inefficient*. After all, if the functional responsibility for managing teachers and health workers would be assigned to the village level (along with the responsibility for the operation and maintenance of schools and clinics), each village would likely have to hire a Department Head for each service; one (or possibly more) Human Resource Officer to ensure proper administration of the local human resources required to deliver these services, including the local payment of teacher and health staff wages. In addition, each village would likely require one or more Financial Officers, Procurement Officers, as well as Monitoring and Evaluation Officers to ensure that the services are properly administered, monitored and reported upward. In short, while it would be *possible* to manage health and education services close to the people, the high cost of such administrative overhead—relative to a relatively small population base at the village level—means that it would likely be much more *efficient* to assign the management of these functions to the next higher level.

Due to scale economies involved in the management of human resources, procurement, and the management of operations and maintenance, most countries assign the responsibility for the provision of basic public services—such as health and education—to the next higher level of the public sector—in our case, the district level—as a result of the scale economies involved. This is consistent with the finding in many countries that the district level (or a local government level with populations roughly in the range from 100,000-300,000) is the lowest government (or administrative) level that can deliver health and education services efficiently.

Three elements of local (health and education) services bear special attention. First, it is often argued that the procurement of supplies—such as textbooks and medicines—can be done more efficiently at the central level than it can be done at the local level, due to the fact that the central line ministry is able to obtain bulk discounts on large, centralized procurements of textbooks or medicines. As a result, procurement of textbooks and medicines is often done centrally. While it may be true that the central line ministry may be able to negotiate a better price, the advantage of such discounts should be balanced with the loss of efficiency and accountability that typically results from “procuring on behalf of someone else” and the added costs that are incurred when centrally procured supplies are transferred “in-kind” to the local level.²⁴

A second element that requires attention as part of the delivery of local (health and education) services is the procurement of capital infrastructure (e.g., school buildings, clinics, and so on). Similar to supplies, an argument is frequently made (especially by line ministry officials) that central line ministries are in a better position to efficiently procure infrastructure. This point is not always supported by empirical evidence, as again, there is a balance between the greater potential technical efficiency of the central government versus the inherent inefficiencies due to the distance between the central government and the location where the infrastructure is built. Depending on the specific support provided, decentralized procurement by local governments (and even by School Committees) can, in fact, result in lower cost and higher quality than centralized procurement of school buildings.

²⁴ Alternative procurement arrangement may result in greater overall efficiency. For instance, it is possible for the central government to negotiate bulk discount from one or more suppliers on behalf of all local government authorities, but to allow the local governments themselves to procure the supplies. This results in the bulk discount being realized while at the same time avoiding the accountability loss from in-kind transfers of medical supplies or education supplies.

A final element of service provision that requires specific attention in the discussion of functional assignments is the provision of community oversight and community mobilization. In many analyses of functional responsibilities, this function is overlooked and under-studied. However, the relationship between the service delivery unit (whether the school or the clinic) and the community cannot be overlooked: if the community is unaware what service are provided (and at what cost, if any); if the community is not mobilized to send their sons and daughters to school, or if they are not mobilized to inoculate their newborns, then the provision of public services will not have any impact on the desired sectoral (or MDG) outcomes. Likewise, if teachers of health staff are not at their designated posts during their regular hours of business, services cannot be provided.

Although the introduction of community participation and accountability sounds easy, in fact, building an enduring relationship of trust and cooperation between the public sector and local communities is in fact quite hard. It requires that the front-line service providers and local officials recognize and present themselves not only as representatives of the government with superior education and knowledge, but at the same, that they are able to position themselves as public servants who provide services to the community in a way that responds to the demands and needs of the communities that they service. In addition, it requires local service delivery units to operate with a degree of transparency about their performance and outcomes that allows not only their administrative superiors to hold them accountable for their performance, but that also allows a meaningful degree of social accountability.

Functional assignments in health and education: comparing seven country experiences. Not much research has been done to verify whether (or the extent to which) this conceptual guidance holds true in the real world. A simple approach might be to narrow our functional scope to a specific sub-function that is comparable across different countries, and to limit ourselves to identifying the primary government level or tier that is primarily responsible for each aspect of provision (HR, O&M, and so on) in different countries. For the sake of convenience, let's look at primary or elementary schools and primary health services (up to the health clinic level), and let's consider seven specific countries: Bangladesh, Cambodia, Mozambique, Sierra Leone, Kerala (India), the Philippines and Indonesia.²⁵

Table 3 presents a different comparison of the degree of localization and decentralization, based on the assignment of functional responsibilities and the degree of localization or institutional discretion. First, each function (health, education) is divided into its five implementation elements (functionaries or HR; non-wage recurrent spending or O&M; supplies; capital development; and coordination, monitoring, and community engagement). Next, different colors or shades are used in the table to indicate different degrees of subnational discretion or control over each of these elements of functional responsibility: light grey indicates centralized assignment of provision responsibility (or administrative deconcentration); medium gray indicates budgetary deconcentration; and dark grey indicates assignment of provision responsibility to devolved local government. Shaded cells indicate areas of joint responsibility between two levels. The letters in each cell coincide with generalized level of decentralization, notably village (V), district (D) or region (R).

²⁵ Brief descriptive overviews for the expenditure assignments for six of these seven countries are provided in the appendix. The case of Bangladesh is described in detail by Osman et al (2014).

Table 3. A comparative overview of country cases: decentralization and localization of health and education

	Primary Health Services					Primary Education				
	HR	O&M	Suppl	Cap	Coord	HR	O&M	Suppl	Cap	Coord
Bangladesh					V					V
Cambodia	R	R			R	R	R			R
Mozambique	R	D			D	R	D			D
Sierra Leone		D					D			
Kerala				V					V	
Philippines	D	D	D	D		D	D	D	D	
Indonesia	D	D	D	D	D	D	D	D	D	D

Source: Based on Boex (2014).

The ordering of countries in Table 3 reflects a loose ranking from more centralized service delivery approaches (least localized discretion) to the most decentralized approaches to service delivery (most local discretion). However, the table does not intend to imply that devolved systems are necessarily superior to less decentralized systems; nor does the table intend to suggest that devolved systems always or automatically provide greater discretion, incentives or accountability. We might make the casual observation, however, that there does seem to be a general positive correlation between public sector effectiveness and the degree of decentralization in this sample of countries.

Table 3 confirms an important finding that was already made in a somewhat different context earlier in this chapter: in delivering health or education services, few (if any) countries rely exclusively on one localization approach or another: most countries rely on a combination of devolution, deconcentration and centralized (“direct” and/or “delegated”) local service delivery. In other words, the question is not to choose between a textbook case of devolution versus a textbook case of deconcentration, but rather: what combination of systems and approaches works best to achieve a meaningful role for local actors to improve local service delivery?

Although Table 3 presents a useful overview of different country practices, the limits of the comparative approach are also quite apparent: for each service delivery aspect, the table is only able to associate a single government level with each aspect of service delivery, and therefore, says little about the actual extent of the involvement of each of the respective levels or tiers in the delivery of a particular service. For instance, in the case of Bangladesh, while most local health workers are centrally employed by the central line directorates which manage different health programs, the salaries of physicians are contained in the budgets of the district-level Civil Surgeon’s Office, while the operating cost of the Upazila Health Office (which contains the salary of the Upazila Health and Family Planning Officer, and related costs for the administration of local health services) is budgeted at the Upazila level (Osman et al, 2014). The way in which functions and expenditure responsibilities are presented in Table 3 thus hides the extent of the role played by each level or tier.

Analyzing the role played by different levels or tiers in delivering localized services: vertical expenditure profiles. A different way to approach the question to what extent different government levels or administrative tiers contribute to the delivery of localized services is to construct a vertical

expenditure profile. Such a profile would consider all expenditures in a functional area (in this case: health and education, respectively) and assess to what extent sectoral expenditures are managed or controlled by each level.^{26,27}

In line with this concept, Table 4 presents the descriptive statistics for the relative size of decentralized spending in the health sector and education sector, respectively, in 29 developing and transition countries for which data was collected by the Development Partner Working Group on Decentralization and Local Governance (DeLoG, 2015).

Variable	Average	Standard Deviation	Coef. of Variation	Min.	Max.
Health sector					
Devolved health expenditures	26.3	29.9	1.138	0.0	98.5
Non-devolved health expenditures	52.7	29.6	0.563	0.6	98.1
Total decentralized health expenditures	79.0	16.2	0.206	25.8	99.1
Central (non-local) health expenditure	21.0	16.2	0.772	0.9	74.2
Education sector					
Devolved education expenditures	30.7	31.2	1.018	0.0	90.6
Non-devolved. education expenditures	54.0	30.8	0.571	1.9	96.1
Total decentralized educ. expenditures	84.7	12.6	0.149	52.5	99.2
Central (non-local) educ. expenditure	15.3	12.6	0.825	0.8	47.5

Source: Computed by the author based on DeLoG (2015).

For each sector, Table 4 shows the share of sectoral spending that was made by devolved local governments, as well as the share of non-devolved sectoral spending at the local level (i.e., the sum of deconcentrated local spending, delegated spending, and direct central funding of local services). The table further shows the total amount of decentralized local public sector spending in health and education, as well as the share of sectoral expenditures devoted to “truly central” activities.

²⁶ For the sake of simplicity, a vertical expenditure profile simply captures at which level or tier a final expenditure is made. Since local spending may be funded from earmarked funding sources and/or maybe subject to other controls by higher-level governments, the share of local-level spending does not necessarily mean that the local level has effective control over these resources. A next step would be to analyze a country’s local governance institutions to determine the extent to which local political, administrative and fiscal systems constrain local-level bodies in the delivery of their functional responsibilities.

²⁷ It should be noted that in order to be comprehensive and consistent, “localized spending on health service” includes not only spending on primary health facilities (health centers, clinics or dispensaries) which are traditionally provided at the grassroots level. In addition, the definition of the localized health spending includes the provision hospital services (including national hospitals, regional hospitals, specialized hospitals, reference hospitals and so on), to the extent that these are provided or funded by the public sector. Likewise, a sectoral analysis of spending on education services considers at all levels and types of education services, from pre-school to university education.

The table reveals that local governments often play an important role for service delivery in these sectors: an average of 26.3 and 30.7 percent of total public expenditures are channeled to elected local and regional governments for the delivery of local health and education services, respectively. When all types of local public sector expenditures are considered, however, countries are seen to actually spend a much greater share of sectoral resources—an average of 79.0 and 84.7 percent—at the local level for health and education services.

Figure 6 and 7 present the vertical expenditure patterns in the health and education sectors, respectively, for these same 29 developing and transition countries on a country-by-country basis. In the graphs, the share of devolved expenditures in each country is indicated by the dark segment of each bar,²⁸ while other (non-devolved) local public sector expenditures are reflected by the incrementally lighter segments. Non-devolved sectoral expenditures include public spending by deconcentrated local administration entities and delegated entities, as well as central-level spending that supports public service delivery in a directly and localized manner. For presentation purposes, countries in Figures 6 and 7 are sorted by the share of total public sector expenditures that are decentralized or localized to the local level through any mechanism (whether devolution, deconcentration, delegated, or direct central-level support of local services).

A first striking observation based on Figures 6 and 7 is that ***there is a lot more “local” spending in the health and education sectors than was previously considered.*** In much of the previous literature on decentralization, only devolved local government spending was considered to be part of the local government sub-sector. When we consider *all* public sector expenditures that are directed towards the local level in the delivery of health and education—not just *devolved* local government expenditures—it becomes clear that in virtually all countries, a much larger share of public sector expenditures is directed towards localized service delivery in health and education than was previously considered. In many countries, this category includes centrally-procured pharmaceuticals (drugs), medical supplies and medical equipment, which constitute an important (in fact, critical) input into improving development outcomes.

A related observation is that ***countries that spend less on health and education through devolved local governments do not necessarily spend less on health and education at the local level.*** An important finding from this analysis of vertical expenditure patterns is that countries that engage in less devolved spending through elected local governments tend to compensate for this by spending more in a deconcentrated manner, or by central line ministries spending more on localized front-line services. As a result, countries that are less devolved do not necessarily spend less at the local level.

²⁸ Where relevant, devolved spending combines devolved spending at local and regional government levels.

Figure 6: Health sector expenditure patterns in selected countries, 2010

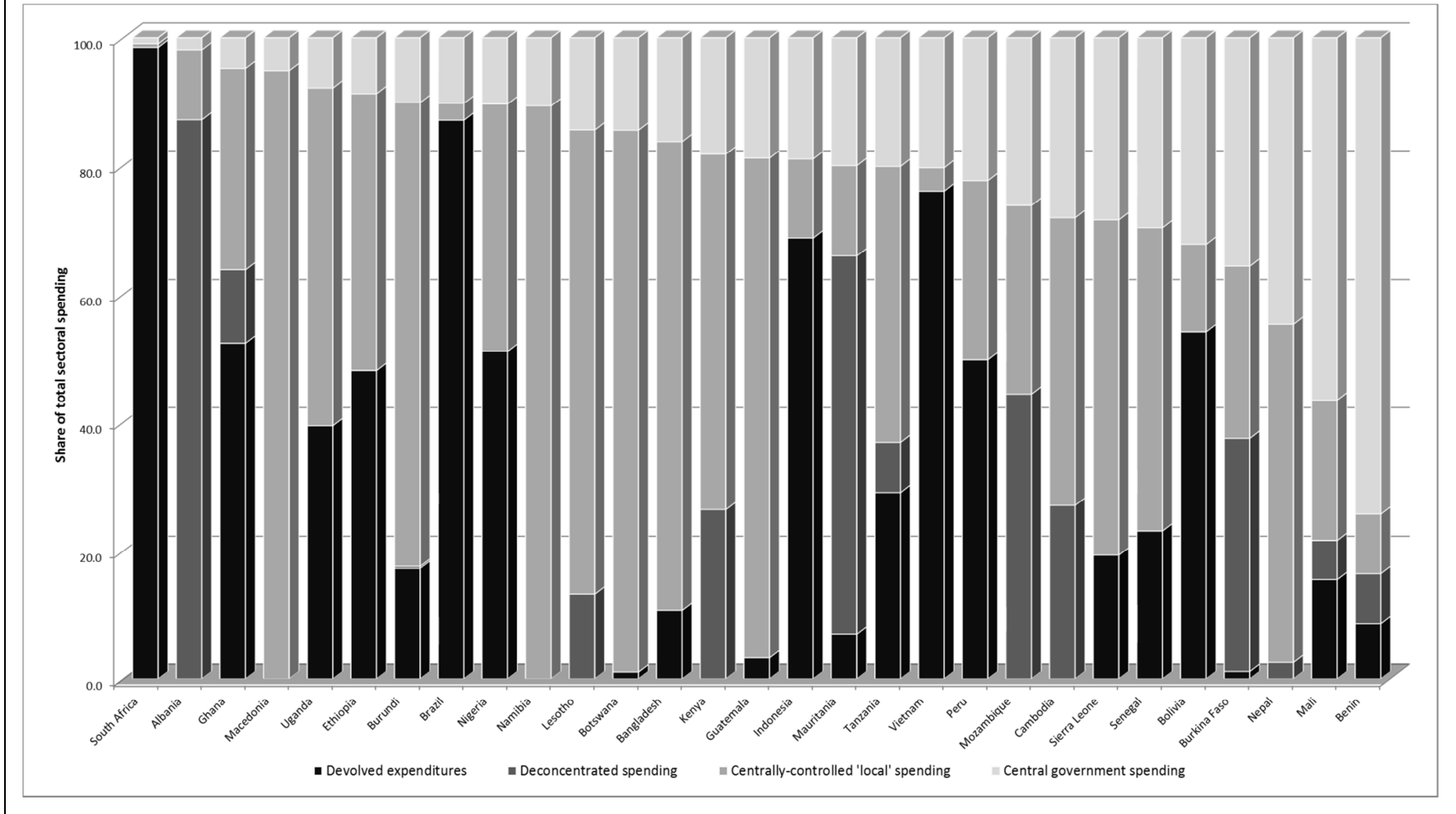
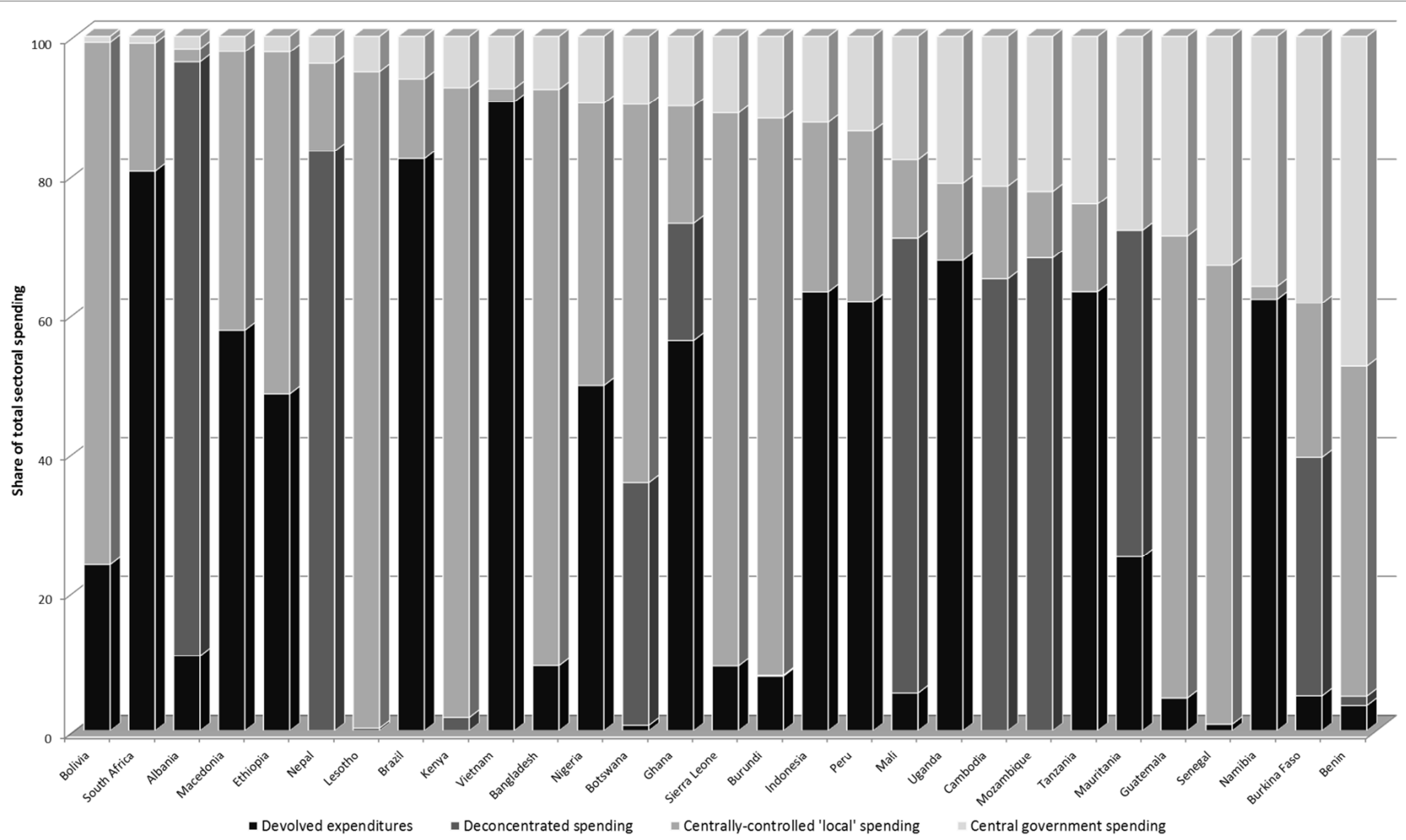


Figure 7: Education sector expenditure patterns in selected countries, 2010

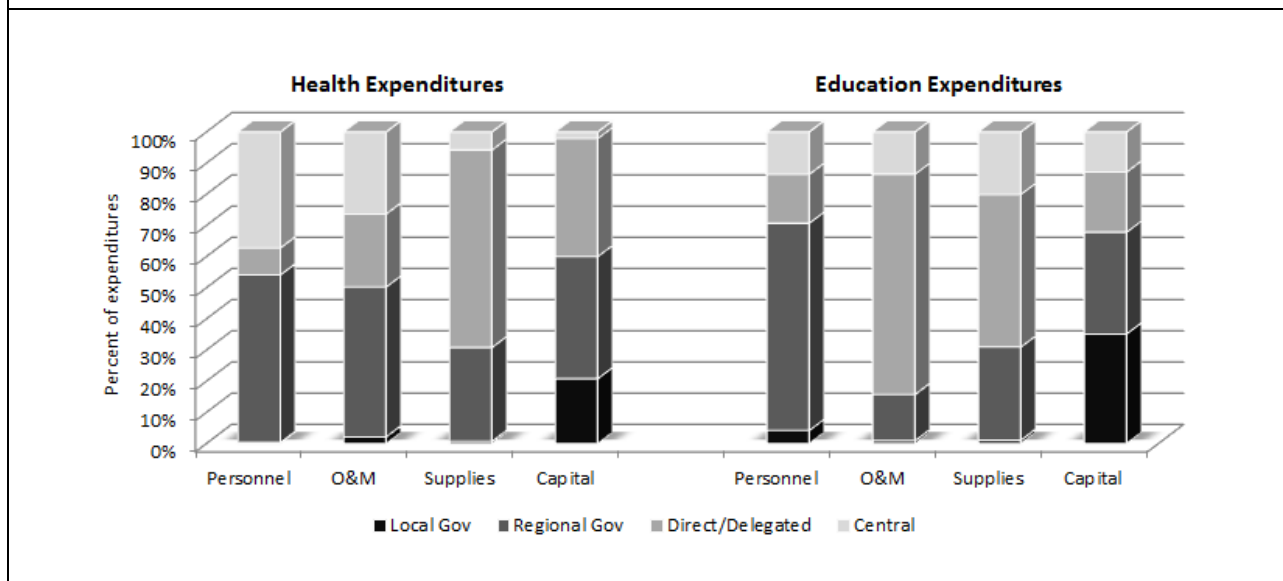


A third observation based on Figures 6 and 7 is a confirmation of the fact that ***the delivery of local public services in different countries follows a multi-level approach to governance and service delivery.*** The figure suggests that countries rarely follow a single model or type of decentralization or localization within the health sector; instead, stakeholders at all levels of government and administration are typically actively involved to support inclusive and universal access to public services at the local level.

In fact, it would both be possible and useful to apply the same approach used in Figures 6 and 7 at the country level in order to analyze vertical expenditure patterns within a single sector by type of spending (i.e., wage expenditures, O&M expenditures, spending on sectoral supplies, and capital (development) expenditures). Such more granular analysis allows for a much deeper understanding of the question “who does what” in terms of functions and service delivery responsibilities in a country.

As an illustration, Figure 8 provides disaggregated vertical expenditure profiles for the health and education sectors in Peru.²⁹ As such, the figure shows not only the total breakdown for sectoral spending in each sector, but also the vertical expenditure pattern broken-down by expenditure type. For instance, the figure shows that in both education and health, regional governments contribute the largest share to salary spending, whereas local governments’ main contributions in both sectors is on capital expenditure items. In terms of non-wage recurrent expenditure, the central government is extensively involved in operation and maintenance expenditures in the education sector, whereas in the health sector, the central government appears to play a leading role in the procurement of medical supplies.

Figure 8: Vertical Expenditure Profiles for the Health and Education Sectors in Peru (example)



²⁹ Note that Figure 8 does not reveal the relative size of each spending category. For instance, in education, two-third of all sectoral spending is on salaries and wages, while supplies (school books, etc.) only account for about 3 percent of sectoral spending. In health, salaries and wages account for about 40 percent of sectoral spending, with the remaining three spending categories accounting roughly for 20 percent each.

General lessons from international experience. Since countries rarely rely exclusively on one model of decentralization or another, even in the delivery of a single service, it becomes hard to assess whether—or the extent to which—a country “follows the subsidiarity principle”. Indeed, if we recognize the complex and granular ways in which multi-dimensional powers and functions are actually assigned across different levels or tiers of a multilevel governance system, then this “first generation” question may not be terribly relevant anymore. Instead, the analysis of vertical expenditure patterns can help to inform policy reforms which try to find “ways to improve capacity and co-ordination among public stakeholders at different levels of government to increase efficiency, equity and sustainability of public spending” (Charbit, 2011).

Although it is difficult to generalize from a limited set of comparative international experiences and case studies, the international experience reviewed in this working paper allows us to draw a number of general conclusions with regard to decentralization and/or the localization of health and education services:

- Decentralization and “bringing the public sector closer to the people” is generally a popular reform. Numerous governments around the world claim to be pursuing decentralization reforms. At a minimum, governments around the world pay lip service to pursuing it.
- In reality, there is no “one-size-fits-all” solution to the challenge of localizing health and education services. Although the subsidiarity principle provides useful guidance on how to assign functions and expenditure responsibilities, and although devolution in theory is a more responsive and appropriate way to assign functions, there is not a universal single-best approach to assigning functional responsibilities in the real world.
- The state of knowledge in the current literature does suggest that certain features are associated with more effective assignments of functional responsibility. First and foremost, a clear assignment of responsibilities is paramount, as is the need to minimize the gap between the *de jure* assignment of responsibilities and the *de facto* assignment. Furthermore, it appears that ensuring that adequate resources flow down to the local level; creating a degree of discretion at the local level (in a way that is balanced with accountability); providing incentives for local officials to perform; measuring service delivery performance; and ensuring local transparency and ensuring accountability (when local officials fail to perform) are all important ingredients into more effective and responsive local service delivery.
- Deconcentration is often seen as an intermediate step on the way to devolution (e.g., Cambodia; Mozambique). If done right, and in the right political context, deconcentration can be a major improvement over more centralized systems (which typically lack any discretion and accountability at the local level). At the same time, effective deconcentration seems to be a necessary ingredient for sound localization of service delivery benefits (as well as a precondition for possible devolution).
- Large-scale (or drastic) devolution reforms are often more politically driven (the desire to empower people and to distribute political power vertically), than focused on immediate service delivery improvements. Nonetheless, the long-run trajectory of decentralization seems to be toward greater devolution and localization. It is difficult to predict when political pressure could build to a boiling point where drastic intergovernmental reform (e.g., devolution) is demanded.
- In most countries (in the absence of a major political sea-change), decentralization tends to be gradual process that takes decades of iterative reform, rather than a reform that can be accomplished in years.

- International experience suggests that different parts of service delivery within health and education are provided through different mechanisms at the same time. Within one sector, salaries, non-wage recurrent spending, development spending, and supplies (medicines or textbooks) may be provided through different combinations of devolution, deconcentration, delegation to NGOs, or direct provision of localized services by central line ministries.
- Due to the different nature of health services and education services, education and health have their own sectoral dynamics. In fact, they are not always delivered in the same way (e.g., the Philippines). The payment and accountability arrangements for teachers (and sometimes, medical officers and health workers) are politically sensitive issues, which evoke strong institutional reactions not only from their respective sectoral line ministries, but often also from the unions representing these workers.

7. The political economy of decentralization and functional assignments

The assignment of functions and expenditure responsibilities across different government levels or tiers of the public sector is a multi-faceted technical process. At the same time, however, it is important to recognize that the vertical organization of the public sector and the assignment of functions across different levels and tiers is not just a technical process, but also inherently a political process. Indeed, political economy forces and institutional interest are critical in determining virtually every aspect of the multi-level governance and service delivery systems.

As noted at the beginning of this paper, the “second generation” of intergovernmental finance theory places intergovernmental relations in an institutional and political economy context, recognizing that public sector decisions are not necessarily made by benevolent rulers and governments but rather by personally motivated politicians and the associated institutions.³⁰ Indeed, it could be argued that the assignment of functional responsibilities—including the determination of the legal assignment of functional responsibilities as well as the *de facto* vertical assignment or transfer of authority and resources—is actually driven by political economy considerations. Although not yet fully explored, it is reasonable to argue that the entire decentralized structure of the public sector is determined by political and institutional forces, including:

- The subnational organizational structure of the public sector: How many levels and tiers does a country have? What is the average jurisdiction size at each level? At what pace are new jurisdictions being generated? Which levels are formed by elected local governments versus deconcentrated administrations?
- The legal assignment of functions and services: what powers and responsibilities will be legally assigned to different local government levels or local administrative tiers?
- The actual (de facto) assignment of functions and resources: After a local government act is passed, what actual powers and responsibilities are actually transferred to the local level?³¹

³⁰ See Weingast (2009; 2013) for a synopsis of second generation fiscal federalism. Second generation fiscal federalism builds on the work of Douglass North on institutions (North, Wallis, and Weingast, 2005).

³¹ The political/institutional dynamics for a line ministry to support sectoral decentralization in a *de jure* and *de facto* mechanism are different. A central line ministry may support (or at least, not oppose) the adoption of a

- The political organization of local governments: to what degree are local governments granted political discretion and autonomy to respond to the needs of their constituents, versus the degree to which local governments are expected to serve the political interests of the center? To what degree are local electoral arrangements and local political structures organized to be downwardly responsive and accountable?
- The degree of local administrative control: to what degree are local governments or local administrations granted administrative control over the functions assigned to them? For instance, even when local governments are entitled to hire, fire, and manage the human resources necessary to deliver a certain service, central controls may be imposed which limited the degree of local discretion and control over local service delivery. For instance,
- The degree of local fiscal autonomy: to what degree are local governments given the appropriate revenue instruments, fiscal autonomy and transfer resources to fund the delivery of local services?

Each of these policy decisions about the structuring and functioning of the local public sector fundamentally impacts the political and institutional interests of stakeholders at different levels. As such, decentralized service delivery is as much (if not more) a political economy process as it is a technical process.

The direct impact of “second generation theory” on functional assignments: institutional incentives. It is beyond the current study to provide a full overview of the emerging literature on the political economy of decentralized public service delivery. However, it is useful to highlight the hypothesis put forth by Eaton and Schroeder (2010) that central government officials seldom have a real incentive to support decentralization as long as the proposed reforms undermine the direct power, discretion, and resources of one or more entities at the central level.³² In particular, decentralization of functions is often (implicitly or explicitly) opposed by central government line ministries who have most to lose in terms of control over budgetary and human resources when their functions are transferred to the local government level (Bahl, 1999).³³

To the extent that there is a political benefit to be gained from paying lip service to decentralization, one would expect a pattern of decentralization by which governments adopt promising legislation in support of decentralization (i.e., “de jure” decentralization of functional responsibilities), but then to “go slow” during implementation (sometimes to the point of complete inaction). Such a discrepancy

decentralization law if it knows that it can hinder the implementation of the law (as applied to its own sector) with minimal political/institutional damage later on.

³² Clearly, there are limits to which central authorities have an ability to capture the subnational political, administrative and fiscal powers. It is likely that central governments in countries that are “open access orders”—as per the terminology used by North, Wallis and Weingast (2005)—are either unable to capture all state powers centrally or have recognized the advantages of a degree of vertical power sharing.

³³ The argument being made here does not exclusively apply to devolution and devolved local governments: the same political economy forces are present when an attempt is made to deconcentrate organizational authority and budgetary resources within the same line ministry. Although the deconcentration of functions and resources might be seen as somewhat less threatening to line ministries (because the line ministry would continue to maintain some degree of control over the functions and resources within the sector), there is a strong institutional interest for central line directors to retain direct control over certain functions and sectoral resources, rather than yielding control over the relevant staff and financial resources to deconcentrated staff within the same ministry.

between *de jure* and *de facto* expenditure assignments was already noted, and is indeed a pattern commonly observed in decentralization reforms, particularly across Africa and Asia.

The lack of central institutional support for decentralization (particularly within sector ministries) often becomes a death knell for efforts to localize public services through devolution: if local governments have weak institutional capacity and the relevant sector ministry is uninterested in building the technical capacity of local government to take on sectoral functions, the lack of capacity will never be resolved and serve as a pretext for a perpetual lack of progress on decentralization.

Another—equally destructive—strategy to prevent meaningful decentralization of functions is to be vague and unspecific about the exact functions and powers to be devolved, or to allow central line ministries to be in charge of formulating the regulations that guide the specific transfer of functions (thus “putting the fox in charge of the chicken”). Another approach for “talking the talk without walking the walk” is to subject the decentralization of sectoral functions to specific capacity conditions which are unattainable for most—if not all—local governments. In these instances, bad technical practices are good institutional politics.

The direct impact of “second generation theory” on functional assignments: political forces. Another example of how sound functional assignments can be thwarted by political economy forces is when political—rather than technical—considerations guide the government level or administrative tier to which functions are assigned. For instance, in the decentralization reforms in Pakistan spearheaded by Pervez Musharraf, significant functions were assigned to the Tehsil (sub-district) level. It could be argued that local jurisdictions at this government level were too small to efficiently manage the delivery of public services. Instead, it has been argued that the transfer of functions and resources to the Tehsil level was primarily driven by the desire of the non-elected central authorities to bypass the political power of provincial elites through the establishment of direct administrative and political links with local governments and representatives at the Tehsil level, thus ensuring the center’s grip over the local level, where elections could be more easily rigged and manipulated through intimidatory measures and the cultivation of patron-clientelistic networks (Mezger, Aftab, and Yusuf, 2010).

Indeed, international practice is rife with examples where functions and funds are directed to the lowest local government level in what appears to be little more than a ploy to ensure political buy-in of local-level officials for the next election.³⁴

“Second generation thinking” and the impact of intergovernmental finance on expenditure assignments. Beyond the direct impact of institutional incentives and political economy forces on functional assignments, it is important to recognize indirect impacts that might arise once one accepts “second generation thinking” about decentralization and intergovernmental (fiscal) relations. For instance, local governments’ ability to perform its *de jure* responsibilities and to deliver public services is often *de facto* limited by the availability of financial resources at the local level.

³⁴ A related politically-driven strategy to limit (rather than enhance) effective local government is to establish a non-elected regional administrative tier or to rely on appointed regional executives (rather than fully elected regional governments) in an effort to prevent the creation of competitive political space in which an opposition might thrive. The reversal to appointed Regional Governor in the Russian Federation under President Putin might be a case in point.

In many countries, there is often limited support at central government level to expand the revenue instruments which local governments are allowed to collect. While there are numerous technical constraints on local revenue administration (particularly in developing countries), political economy forces and institutional interests are typically an equally important—if not dominant—factor in constraint revenue decentralization and local revenue autonomy. In particular, central governments (represented by the Ministry of Finance in this regard) are typically loathed to assign high-yielding own revenue sources to local governments.³⁵ Despite the fact that own source revenues are typically highly centralized, it is not unusual for central officials to proclaim their support for decentralization as local governments can deliver as many services as they can afford with their own revenues (see Box 6). At the same time, however, central line ministries are quick to lay claim to the revenues collected by local governments themselves, insisting that local governments should support service delivery within *their* sector from own sources, without taking into account the multiple demands being made by other line ministries (let alone the priorities of the local taxpayers themselves).

Box 6. The false paradigm that "functions should follow funds".

As discussed in Box 2 above, the common understanding in public sector finance is that in a well-designed intergovernmental fiscal system, "finance should follow function". Functions are assigned first, and then, each function is funded from an appropriate funding source, whether it is from own sources, from intergovernmental fiscal transfers, or from local government borrowing.

However, it is not unusual for central government officials to assign minor revenue instruments to the local level; proclaim their support for decentralization based on the fact that "local governments can deliver as many services as they can afford with their own revenues"; and to then blame local governments for their failure to deliver adequate services because they do not collect adequate revenues from the limited, inefficient and unpopular revenue sources assigned to them.³⁶ This notion that "functions should follow finance" is a false paradigm.

In fact, some observers suggest that in reality, finance does not follow function, but rather that "finance follows politics". This observation suggests that revenue decentralization to local governments, as well as the (vertical and horizontal allocation of) intergovernmental fiscal transfers, is predominantly politically driven. To the extent that the availability of financial resources at the local level is a binding constraint on their exercise of functional responsibilities, the inadequacy of financial resources is a major constraint—imposed by political economy forces—on the effective assignment of functional responsibilities.

Following the same logic, the distribution of public resources through intergovernmental fiscal transfers between the central government level and the local government level is often determined through political and institutional processes that are heavily slanted in favor of the central government level.

³⁵ Furthermore, in election years, it is not unusual for Members of Parliament to discourage local officials from collecting local taxes. Likewise, it is not unusual for central government to slash or abolish local revenue sources ahead of an election (which allows it to cut taxes without suffering the revenue implications on its own).

³⁶ It is beyond the scope of this study to discuss the difficulties typically encountered in local revenue collection. As an illustration of the challenges, it is helpful to identify that the property tax—which is typically the largest (if not the only) "major" revenue source assigned to local governments is regularly identified by taxpayers as the least popular tax. In addition, there are numerous economic and administrative reasons why the potential yield of the property tax in the context of developing countries is considerably less than in industrialized economies.

There is equally considerable evidence that the horizontal allocation of grant resources is driven by political considerations, which typically results in wealthier and/or politically better-connected local jurisdictions receiving greater resources (Boex and Martinez-Vazquez, 2004). This raises the critical—and the as of yet, unresolved—policy question: if we know that some or all local governments are going to be under-funded for the functions that would be assigned to them, what implications should this have for the (*de jure* and *de facto*) assignment of functional responsibilities?

The impact of weak political and administrative decentralization on functional assignments. It is not only by the central government’s actions to limit local government access to financial resources that efficient and responsive functional assignments are undermined. Eaton and Schroeder (2010) suggest that as long as central governments are able to retain control over at least one dimension of decentralization for themselves (i.e., political, administrative or fiscal decentralization), then central officials are effectively able to retain their power and control over local-level decisions (and thereby effectively frustrate the local-level decision making power which—when combined with accountability—results in the intended benefit of decentralization).³⁷

Following the hypothesis posited by Eaton and Schroeder, it is not unusual to observe local political systems that seem to have been purposely designed to provide ineffective checks and balances at the local level, consistent with the notion that the local political system was primarily designed in order for the central government to retain its political control over local government authorities. Ethiopia’s subnational governance system is a case in point, although by no means an isolated example. As long as local politicians and local political candidates are pressured to place the priority of the national political party ahead of the true needs of their local constituents, and as long as the central political party is able “punish” candidates who fail to “follow the party line” by putting the needs of their constituents first (for instance, by not supporting his or her candidacy for the next round of elections), the primary accountability and responsiveness of local politicians will be to the top rather than to the electorate.

Likewise, in many countries, central government maintains a high degree of control over local government officials. It is not unusual—even in the context of “devolved” local governments—to have central government officials appoint the chief administrative officer or department heads at the local government level. Similarly, in many countries, local governments require central government approval to create new establishments (staff positions), even when these positions are funded from own revenue sources. While these systems are likely to limit the authority of the elected council over its own operations and staff, and may hinder effective local management of public services, it has proven to be an effective mechanism for central government to continue to control local staff and local service while being able to take political credit for supporting the objective of decentralization.

Given the fact that local politicians are often oriented upward and that the degree of administrative control at the local level is often limited, it is not unusual for local governments to only have a limited ability to respond to demands or needs from below. Under such conditions, it should come as little surprise that—despite the increasing recognition and importance of social accountability mechanisms—

³⁷ At the extreme, a country may assign *de jure* (and even *de facto*) functional responsibilities to elected local governments without decentralizing the concomitant political, administrative and fiscal authority. Boex and Simatupang (forthcoming) refer to this situation as “devolution in name only” or DINO.

local participation and accountability mechanisms and citizen complaint mechanisms are ineffective or anemic at best, since local governments are not able to respond to service delivery failures anyway.^{38,39}

Again, the question arises: if the political and administrative aspects of a local governance system are designed to respond to the political and institutional interests of the center—rather than allowing local governments an appropriate degree of discretion and accountability over their own operations—, does it still make sense to pursue decentralization by devolution? Or given the absence of effective public (electoral and social) accountability mechanisms, should deconcentration (or even, centralized provision) be considered as a viable alternative to devolution until the political economy dynamic has evolved to a point where central state capture is reduced and where the center is politically or economically motivated or compelled to devolve powers and resources?

The vertical assignment of functions: the last mile of service delivery. A final aspect of functional assignments and local service delivery is the political economy context of the “last mile” of service delivery. This issue refers to the vertical power dynamic—and the potential principal-agent relationship—between sectoral officials at the local government/administration level on one hand (e.g., local sectoral department heads and/or local sectoral officers) and front-line service delivery staff on the other hand (e.g., headmasters, clinic managers, and so on). This “last mile” is typically an overlooked aspect of the vertical service delivery (and governance and finance) chain and can be one of the weakest links in the service delivery chain.

Facility-level discretion varies considerably between different countries, even among developed economies (OECD, 2011). For example, in the Netherlands, over 90 percent of students attend schools that have the authority to hire and dismiss teachers, while in contrast, over 80 percent of students in Italy attend schools that have not have this authority. An analysis of the locus of decision-making in education in OECD countries and transition countries suggests that students tend to perform better in countries where schools have a degree of operational and budgetary discretion in combination with greater transparency and accountability requirements (OECD, 2011). The study finds that in countries where schools have greater autonomy in resource allocation in the absence of school-level accountability arrangements, students tend to perform worse.

Local-level “capture” over resources at the last stage of public expenditures—the allocation of resources from the local level to the facility—can have a major negative impact on local service delivery outcomes. As part of their analysis of local-level health spending in selected districts in Tanzania, Boex, Fuller and Malik (2015) found that roughly half of all local health resources is spent on local health administration (Council Health Management Team) and the District Hospital, both of which are under the direct personal supervision of the District Medical Officer. This means that only half of all local health resources trickle down from the local government level to dispensaries and health centers, which are the front-line service delivery facilities closest to the people, where the vast majority of rural residents receive their health services.

³⁸ See, for instance, Boex, Lane and Yao (2013) with regard to urban public services in South Asia.

³⁹ In fact, even if local governments are able to respond to service delivery complaints, residents may not even use the available complaint mechanisms under the assumption (based on previous experiences) that complaints are not responded to and do not result in improved services.

Concluding remarks. First generation theory on fiscal decentralization provided clear-cut guidance on how to organize a multilevel governance system, guided by the efficiency criterion. In a binary way, it simply divided the world into devolved regional and local governments and central government (which included “everything else”), thus leaving out the nuances of deconcentration or other approaches to localization. In accordance with the subsidiarity principle, economic theory assigns allocative expenditure activities to lower government levels based on the principle of territorial benefit, while distributional and stabilization functions require central intervention (Dafflon, 2015).

In contrast, once political considerations are permitted to enter consideration, the neat structure imposed by economist dissipates, as multilevel governance shifts from being an organizational form that maximizes efficiency to defining the overarching framework for societal power-sharing, defining the distribution of power both between the public sector and the people, as well as among different groups of people and among different government entities, levels and units.

Because reality is not as clear-cut as first generation theorists may like the world to be, the state of knowledge on the topic of functional assignment is still evolving. First-generation information and guidance on the topics was generally limited to tables that cross-tabulated government functions with legal expenditure assignments in different countries, and tables that revealed the theoretically optimal assignment of functional responsibilities.

What the previous literature failed to do was to effectively capture the *de facto* assignment of functional responsibilities by looking at granular expenditure patterns in a multilevel framework. This seems to have been driven in part by practical considerations, and in part by long-held convictions about the true nature of decentralization. First, only extremely limited data are available on devolved expenditures in different countries, especially for developing countries, with, with the IMF’s Government Finance Statistics Yearbook being the “only global database with fiscal data for several levels of government” (Dziobek et al 2010: 2). Second, potentially even more problematic is that the empirical literature on fiscal decentralization and expenditure assignments acknowledged and measured devolution as the only pathway to decentralization, thereby ignoring any non-devolved approaches to assigning functions to the local public sector.

Given the very selective measurement of the assignment of functions and expenditure responsibilities it should come as no surprise that the considerable empirical literature on the topic is inconclusive about the impact of decentralized functional assignments on a variety of development outcomes (Smoke 2013).

The first empirical analysis based a comprehensive measure of *de facto* functional assignments and local public sector expenditures suggests that better sectoral development outcomes in education indeed *do* (with statistical certainty) go hand in hand with greater localization of public expenditures (DeLoG, 2015). The finding that “localization matters” can be seen as a general affirmation of the idea embedded in the subsidiarity principle that—under most condition, and with certain general restrictions—it is better to direct resources and assign functions to the local level .

The initial results on the role of the local public sector in achieving development outcomes, however, do not find with statistical certainty that devolved expenditures are better—in terms of their development impact—than non-devolved local public sector expenditures. This contradicts the black-and-white

distinction made in the first-generation literature between functions and expenditures assigned to devolved local governments as being “good” and functions and expenditures assigned to deconcentrated or delegated local entities as being inferior. Indeed, even in the second generation literature, the role of deconcentration and other non-devolved local public sector expenditure continues to be largely overlooked.

Where does that leave us in terms of policy prescriptions for the assignment of functional responsibilities? In an attempt to answer this question, Dafflon (2015) concludes that a country’s social preference, rather than economic theory, should be the major guide in determining the appropriate assignment of functions and the associated level of expenditure decentralization. The concurrent assignment of functional powers and responsibilities to different government levels and tiers has resulted in real world multi-level functional assignments that are fragmented and intermingled, reflecting political and institutional realities more than the adherence to a single coherent policy framework. As such, beyond accepting a number of guiding principles—such as the need to balance discretion and accountability at each level, and that spending “closer to the people” is generally better as long as certain minimum conditions about efficient scale and accountability can be met—there cannot be a technically-determined single ‘right’ answer to the assignment of functions and responsibilities between different government levels. Instead, there can merely be more or less technically efficient policy compromises about the way in which public services are localized in the context of a multilevel governance framework.

Appendix: The assignment of functions and expenditure responsibilities for health and education in six countries

In order to supplement the largely conceptual discussion on the assignment of functions and expenditure responsibilities in this paper, the current appendix seeks to provide some descriptions of “real-world” functional assignments.⁴⁰ The situation in six countries is outlined below, include the assignment of functions in **Cambodia** (a sectorally deconcentrated system); **Mozambique** (a territorially deconcentrated system); and **Indonesia** (as an example of a devolved system). In addition, examples of three hybrid systems are presented. In **Kerala, India**, responsibilities for the recurrent aspects of public service delivery are assignment to the state level, while the responsibility for capital infrastructure (and to some extent, operation and maintenance) is devolved to Panchayat Raj Institutions. In **the Philippines**, the responsibility for local health services is devolved, while the provision of basic education is a deconcentrated function. Finally, **Sierra Leone** follows a hybrid system, in which local government administration and sectoral O&M resources are devolved, but where local sectoral staff and sectoral capital infrastructure remain centralized).

A. Country Case: Cambodia

Cambodia’s public sector provides an example of a sectorally deconcentrated system in South East Asia, where the responsibilities for recurrent health and education services are generally assigned to the provincial level.⁴¹ The responsibility for providing capital infrastructure for health and education services (and the responsibility for providing capital infrastructure across other sectoral services) is generally retained by the central line ministries. The only “real” local government level in Cambodia, the Commune level, is primarily responsible for community development and small infrastructure schemes, with little or no role in health or education service provision.

Why did Cambodia decentralize? Cambodia’s policies regarding decentralization and subnational governance since World War II can be divided into several phases (Chandler, 2008; Niazi, 2011). Prior to independence from the French, there was some interest in establishing national democratic institutions through the election of a National Assembly but with no corresponding moves at the subnational level (subnational jurisdictions were managed through appointed district governors). Following the first post-independence national elections in 1955, the National Assembly was led for 15 years by Prince Sihanouk’s Sangkum Party. This period was characterized by autocratic rule of the territories through strong centrally appointed governors and tax collectors. The second half of the 1970s witnessed the gradual emergence of Cambodian People’s Party (CPP) and a communist state, followed by the atrocities of the Khmer Rouge and Pol Pot. While Vietnamese intervention in Cambodia in 1978 was a turning point in the conflict, the subsequent period of Vietnamese single-party control continued the long history of centralized control and neglected the development of decentralized democratic institutions.

Mr. Hun Sen has been the guiding force for decentralization in Cambodia over the past three decades. Hun Sen first became prime minister in 1985 and, apart from the brief United Nations period of 1991–1993, has remained the country’s prime minister. From 1993, Hun Sen has been the leading figure of the

⁴⁰ This appendix draws on Boex (2014). Country cases are presented in greater detail in Boex and Simatupang (forthcoming).

⁴¹ This section draws in part on the Local Public Sector Country Profile for Cambodia, as well as on Niazi (2011).

new Cambodian People's Party. Decentralization and Deconcentration (D and D) has been one of the main reforms pursued by the government of Cambodia as part of the post-conflict democratization process since the early to mid-1990. The slow pace of the decentralization process as well as the limited extent of decentralization being envisioned reflect the political reality that the public sector at all levels is effectively controlled by Hun Sen's Cambodian People's Party (CPP).

Despite (or perhaps because of) the monopoly on power of the CPP, considerable effort is being exerted to promote democratic development through decentralization and deconcentration reforms with extensive international donor support.⁴² This effort is being led by an inter-ministerial mechanism, known as the National Committee for Sub-national Democratic Development (NCDD).

Building on the success of several donor-funded pilot projects supporting decentralization at the commune level (Andersen, 2004), the first serious steps towards decentralization in Cambodia were taken in 2001-02 with the passing of the Commune Law; the election of 1,621 Commune Councils; and the introduction of the Commune-Sangkat Fund. In 2005, the country adopted *the Strategic Framework for Decentralization and Deconcentration Reform*, which was followed by the *Law on Administrative Management of the Capital, Province, Municipality, District and Khan* (widely known as the *Organic Law*) in 2008. Although the Organic Law forms a key element of the legal framework for implementing the Strategic Framework, the full implementation of the law will require a long-term process of capacity building and institutional reform.

What is Cambodia's territorial-administrative governance structure? Cambodia's territorial-administrative structure is formed by the top-down state administration on one hand (formed by various deconcentrated tiers of the central government, dominated by the provincial level) and by the "bottom-up" mechanism that starts at the commune (village) level, which forms the government level closest to the people.

The first major step towards democratic, decentralized management at local levels was made in 2001, when the *Law on Commune and Sangkat Administrative Management* (2001) recognized communes and sangkats as local government entities with their own directly elected leadership and legislative and executive powers.⁴³

In 2008, the Organic Law provided the administrative basis for further deconcentration by formalizing the organizational structures and roles of the provincial level (including provinces and the capital) as well as a district level (covering provincial districts as well as municipalities).⁴⁴ In practice, the provincial level (24 Provinces and Capital, with an average population of around 500,000 residents) dominates the subnational governance and service delivery structures. Provinces are effectively deconcentrated jurisdictions, where all main central line ministries are represented by sectorally deconcentrated offices. Provincial Governors act as chief executives of the provinces as well as supervisors of the provincial departments of national ministries within the provincial jurisdiction.

⁴² Even though the NCCD promotes "democratic development through decentralization and deconcentration reforms", in reality, the envisioned public sector structure is primarily a deconcentrated state structure, albeit with some features of devolution (e.g., subnational decisions guided by elected councils).

⁴³ Sangkats are roughly equivalent to urban communes or neighborhoods.

⁴⁴ There are some differences between the organizational-governance arrangements for urban versus rural jurisdictions, while the Capital, Phnom Penh, has its own unique administrative structure.

Provincial and district-level jurisdictions have indirectly elected councils. Councils at these higher levels are indirectly elected from the bottom up by Commune Council members within their respective jurisdictions. In reality, all local jurisdictions are dominated by the ruling party. Although the Organic Law envisions subnational councils at each level to have broad roles, duties, and the authority to make legislative and executive decisions, for the time being, provinces basically continue to operate as deconcentrated entities.

The Organic Law defines the district level as the territorial level below the province. While the district level has the potential to become an effective local government level at some point in the future, district-level jurisdictions (especially outside of urban areas) are currently only nascent/emerging local government entities.

Despite the ongoing decentralization reforms, the central government continues to retain a high degree of top-down political, administrative and fiscal control over the local public sector in Cambodia. For instance, although provincial officials have some degree of *de facto* discretion over the delivery of public services within their jurisdiction, provinces lack their own political leadership, have only limited administrative discretion, and rely almost exclusively on financial resources received from the center. Similarly, even though Communes have directly elected Councils, the degree of responsibility, discretion and accountability at this level is also quite limited.

What is the functional assignment for health and education? Although roles and functions of different tiers of government are not well defined by law, the *de facto* functional assignments in Cambodia's public sector are quite centralized. In practice, Communes and Sangkats focus largely on providing community-level infrastructure and services.

The provincial level is *de facto* the only functioning subnational administrative level, with responsibility for the delivery of key front-line social services, including primary and secondary education services as well as basic health services. Even in these functional areas, however, central line ministries retain the responsibility (and resources) for development expenditures, although provincial governors have a small discretionary cross-sectoral budget at their disposal (the provincial *salakhet*) to promote provincial development. Central line ministries also directly support national and referral hospitals, tertiary (university) education institutions.

How are these functions funded? Since Cambodia's public sector primarily relies on (sectoral) deconcentration, all health and education funding is provided through the national budget. The national budget is vertically (sectorally) deconcentrated up to the provincial level. Each central line ministry's organizational budget structure (including the budgets for the Ministry of Health and the Ministry of Education) identifies central line department expenditures separately from provincial line department expenditures. The deconcentrated provincial line department budgets contain the main recurrent spending items (include wages and O&M spending) used within a province to deliver health and education services. This allows for considerable transparency in the budget process. It reveals the (vertical) share of national (recurrent) budgetary resources that flow down to the subnational level, as well as how different sectors distribute their recurrent resources across different provinces (Boex, 2009).

The fact that provincial line departments are secondary budget units (or budgetary sub-organizations) within their respective line ministries gives the heads of provincial line departments some degree of discretion and autonomy. While during budget formulation, provincial line departments are formally supposed to submit their budget requests to the Ministry of Economy and Finance through their respective central ministries (which then prioritizes sectoral spending needs across provinces), it was reported that well-connected provincial department heads may approach the Ministry of Economy and Finance directly to lobby for a relatively greater budget allocation.

Only about one-third (33.4 percent) of total public expenditures (across all government functions) fall within the realm of the local public sector. This total amount (across all sectors) includes about 15 percent of total public sector expenditures, which take place in a deconcentrated manner at the provincial level. In addition, central government spending on 'local' services accounts for another 15 percent of public spending. Only about 2 percent of public sector expenditures in Cambodia take place at the commune level, whereas district-expenditures account for less than 1 percent of public sector spending. The remainder of public expenditures (66.6 percent) is retained at the central government level for national functions and central government administration.

Since health and education are both services that require direct and localized interaction with the recipient (student or patient), we would expect health and education expenditures to be much more localized than overall vertical allocation of resources suggests. Indeed, about 70 percent of health expenditures and approximately 80 percent of education expenditures find their way down to the local level, either through budget deconcentration or through direct central funding of front-line services. Although the degree of localization of sectoral expenditures in Cambodia is relatively average (and not dissimilar to Bangladesh), its sectoral outcomes in the health and education sectors are somewhat better than one might expect based on the share of localized spending alone.⁴⁵

B. Country Case: Mozambique

Mozambique is a good example of a highly transparent, territorially deconcentrated public sector.⁴⁶ Its territorial-administrative structure has similarities to Bangladesh's subnational governance structure with deconcentrated provinces (similar to Zilas) and deconcentrated district administrations (akin to Upazila administrations). Urban public services in urban areas are delivered by elected municipal governments. However, Mozambique's budget structure is quite transparent, and allocates a relatively substantial share of sectoral resources (in health, education, as well as in other sectors) towards the provincial and district level. Provincial and district-level sectoral officials are involved in subnational budget planning and execution.

Why did Mozambique decentralize? Prior to the adoption of its 1990 Constitution, Mozambique was governed in a highly centralized manner as a result of the centralized administrative structures inherited from its period of (Portuguese) colonial rule (which ended in 1975) as well as its own post-independence socialist experiment. The Rome Peace Accords, which ended Mozambique's civil war in 1992, stipulated

⁴⁵ Among different possible explanations, it is possible that the relatively strong sectoral outcomes in Cambodia are caused by the relative effectiveness of deconcentrated provincial departments. An alternative explanation could be that the lack of transparency in the use of central budget resources has caused us to underestimate the level of direct centrally-controlled spending in support of local front-line services.

⁴⁶ This section draws in part on the Local Public Sector Country Profile for Mozambique, as well as on Boex, et al., (2008).

that the country would pursue devolution of powers and functions as the basis for the envisioned vertical and territorial sharing of political power by the former combatants: the ruling party, Front for Liberation of Mozambique (FRELIMO), and the Mozambique Resistance Movement (RENAMO).

Devolution was never pursued across the entire national territory as envisioned within the Peace Accords. Instead, the country has embarked on a decentralization process that combines the deconcentration of key public services to provinces and districts (governed by the *Law on the Local Organs of the State*, 2003) with the simultaneous process of devolution of urban services to elected municipalities in the country's urban areas. The shift towards deconcentration versus devolution has favored the ruling party, FRELIMO.⁴⁷ The main challenge to more fundamental reform has been the tendency of the dominant-party state to pursue a gradual approach to decentralization.

What is the Mozambique's territorial-administrative governance structure? The *Law on the Local Organs of the State (Law 8/2003*, also known as *LOLE*) sets forth the organization, competencies and functioning of Provinces, Districts, Administrative Posts and Localities as deconcentrated state organs, following a territorial approach to deconcentration.⁴⁸ Provinces have elected councils, but they have little or no real authority over the functioning (or financing) of state organs within their province.

While Law 8/2003 designates the district level as “the principal territorial unit for the organization and functioning of the local administration” and the base for planning the “economic, social and cultural development of the Republic of Mozambique”, the ability of district officials to make decisions continues to be low. In contrast, the country's municipalities (which increased over time from 33 in 1997 to 53 in 2013) have their own elected leadership and -in principle- have a considerable degree of political autonomy and discretion to deliver urban public services.

As deconcentrated levels of public administration, provinces and districts in Mozambique do not enjoy any significant degree of political or fiscal autonomy. Likewise, even though they are responsible for delivering key public services, the degree of administrative discretion that they have is rather limited.

What is the functional assignment for health and education? Despite attempts to clarify the relative responsibilities of different administrative level in LOLE, the division of functional responsibilities between different levels is somewhat unclear in Mozambique, and not always followed. Particularly on the development side of the budget, there has been a desire on the part of some line ministries to retain control over capital infrastructure spending and development projects despite the fact that some of the functions may have been legally assigned to the provincial or district level.

In practice, the recurrent provision of localized public services, including basic education, health, agriculture, and rural water supply, is the responsibility of provincial and district-level departments. In fact, functional control over recurrent functions (resources) within these sectors is gradually being shifted from the provincial line departments to the district-level departments.

⁴⁷ By the 2013 local elections, RENAMO had been almost fully marginalized. FRELIMO won the mayoral races and council majorities in 50 urban areas, but lost three of the four largest cities to the opposition MDM (a break-away from RENAMO) who also gained council seats throughout the country.

⁴⁸ Note that in Mozambique's terminology, “state” refers to the “nation state” (i.e., central government).

Central-level line ministries often play an important role in providing capital infrastructure across these services, while provincial-level departments (for now) retain control over the administration of local-level public servants. Municipalities are assigned a number of statutory responsibilities related to urban public services and urban infrastructure development, although urban drinking water is provided by urban water authorities under control of the central ministry. In Maputo, the responsibility for key public services (including basic education and health services) has formally been “delegated” from the state administration to Maputo Municipality—although in practice, services continue to be delivered through the state administration.

How are these functions funded? As a predominantly deconcentrated country, most public services (including health and education) are funded through the national budget. Mozambique's national budget has an extremely transparent structure, which clearly identifies all central and deconcentrated budget allocations by organization and sector, as well as by administrative level and jurisdiction (province and district). As a “territorially deconcentrated” country, the primary breakdown of the budget is by administrative level. Therefore, provincial line department budgets are grouped by province (into a “provincial budget”) rather than being included into their respective line ministry budgets. Similarly, district-level budgets and expenditures are grouped by district jurisdiction at the district administration level. Since municipalities are elected local governments, the national budget does not include (or provide information on) municipal expenditures or revenues (beyond the level of grant funding provided to municipalities).

When we look at total public spending in Mozambique—across all government functions—almost half (44.1%) of public sector expenditures in Mozambique take place within the local public sector. Despite the fact that Mozambique is deconcentrated rather than devolved, this places the country among the most “localized” public sectors in the world. In fact, the share of public resources spent at the local level in Mozambique exceeds that of many devolved countries in the region, such as Tanzania or Uganda.

In aggregate, about one quarter (26.8%) of total public expenditures take place at the provincial level (through provincially deconcentrated budgets); 6.5% at the district level (through district-level budgets); and 1.9% of public expenditures spent by municipalities. These proportions are a reflection of the respective *de facto* functional responsibilities assigned to local government. In addition to these deconcentrated and devolved expenditures, roughly 8.9% of total public expenditures are made by central government ministries for public services that are delivered at the local level. This mostly reflects spending on hospitals and universities supported by central line ministries, as well as centrally-controlled development projects. Across all government functions, the national government retains 55.9% of public sector resources for national functions and activities that fall outside the local public sector (such as central policy formulation, oversight and regulation; national defense; and so on).

Localized health and education spending in Mozambique represent 74 and 78 percent of total sectoral expenditures, respectively. As in the case of other countries, the contribution of direct centrally-controlled spending is relatively limited (close to 10 percent) while the central contribution to localized health expenditures is larger (close to 30 percent).

As a deconcentrated system, revenues collected by provinces and districts are not retained subnationally and flow into the national treasury. Municipalities are permitted to collect several municipal taxes and other local revenues. However, these revenue sources are under-utilized, and are

generally not spent on health or education, with the exception of some spending on public health services (i.e., solid waste removal and sanitation). In addition to own source revenues, municipalities receive some formula-based recurrent and capital grants from the central government, known as grants from the Municipal Compensation Fund and the Investment Fund for Municipal Initiatives, respectively.

C. Country Case: Indonesia

Indonesia is among the most well known examples of decentralization reforms in the world. After over half a century of highly centralized (and mostly, authoritarian) governance, Indonesia switched to a devolved system in 2001. Decentralization was introduced to prevent the disintegration of the state in the middle of a severe economic and governance crisis.

Why did Indonesia decentralize? The current structure of Indonesia's public sector is defined by the 'Big Bang' decentralization reform that was adopted in 1999 and introduced on January 1, 2001. Whereas up to this point all public services had been delivered in a centralized or deconcentrated manner, in 2001, almost all functions were devolved to the district level (*kabupaten/kota*). These reforms fundamentally changed the source of accountability and responsibility for governance and service delivery across the country.

There were numerous forces that drove Indonesia to this “big bang” approach, after having been governed by an autocratic regime since its independence. These factors include the country's structure as a multi-ethnic and multi-cultural island nation, a prevailing distrust in central government due to its corruption, collusion, and nepotism (*Korupsi, Kolusi, dan Nepotisme* or KKN), the resurgence of regional (ethnic and religious) identities that resulted in calls for regional autonomy and even independence in different parts of the country (Aceh and West Papua) (Mietzner, 2013).

Since the ‘big bang’ in Indonesia, significant progress has been made towards greater democracy and decentralization, although not all vestiges of the previous centralized regime have been fully eliminated. There has been strong public satisfaction with decentralization, while progress on human development indicators and service delivery quality has been relatively moderate since 2001. Regional identities have flourished, while careful electoral engineering and detailed attention to equalization have limited regional calls for further autonomy and independence. While subnational governments now have the authority and responsibility for many public services, they still face constraints in capacity, autonomy, and accountability in fulfilling their duties under the law.

What is Indonesia's territorial-administrative governance structure? Indonesia's public sector consists of three main government levels: the central, provincial and district levels. The country is divided into 33 provinces, which in turn are composed of regencies or districts (*kabupaten*) and cities (*kota*). At each of these levels, the political leadership is elected by popular vote every 5 years. Three provinces -Aceh, Papua, and West Papua- have a special status granting them a higher degree of autonomy, whereas Jakarta and Yogyakarta are also recognized as Special Regions.

Kabupaten and *kota* are further broken down into 6,694 sub-districts (*kecamatan*), which are administrative sub-units of the district level. Below the sub-district level, there are 69,249 villages (*desa*) and 8,216 urban villages (*kelurahan*). *Desa* leaders are elected and have authority over local people in

accordance to local traditions whereas kelurahan have less power and are comprised of civil servants directly responsible to the head of their kecamatan.

Kabupaten/kota governments are semi-autonomous subnational government bodies with their own elected political leadership, elected every 5 years. Whereas local councils have been directly elected since 1999, the local executive (head) of the local government was not directly elected before 2004. Instead, he or she was appointed by the local council. Concerns about indirect political accountability triggered local government electoral reforms toward direct elections under Law No. 32/2004. This reform made the local head more directly accountable to the people by stipulating that (s)he would be directly elected by citizens, and provided a clearer definition of the head's political functioning.

While national electoral legislation prevents the emergence of separatist regional political parties, provincial and local government elections are quite competitive. Local governments have a considerable degree of discretion over their own administration, such as the ability to recruit, hire, and dismiss staff, and the authority to procure their own capital infrastructure. In addition, provincial and kabupaten/kota governments prepare, adopt, and implement their own budgets and control and manage their own bank accounts. While local governments can collect their own revenues, they remain heavily dependent on transfers from the national government.

What is the functional assignment for health and education? As part of Indonesia's 'big bang' approach to decentralization, the Regional Autonomy Law (Law 22/1999) assigned responsibility for 26 functions to the local government level. While the national government retains exclusive jurisdiction over national functions (such as national defense, public order, social protection and policy standards), the responsibility for most social and economic services (including basic education and health services) was transferred to the kabupaten/kota level. Provinces mainly function as an intermediate government level, but are also responsible for certain services that are provincial in scale or concern, such as regional health services.

How are these functions funded? Indonesia's decentralization reforms have been successful not only in achieving a *de jure* reassignment of functions and responsibilities, but by matching the legal reforms with the *de facto* transfer of functions by reallocating the resources needed to deliver services to the local government level. In fact, about half (48.3%) of public sector expenditures in Indonesia take place within the local public sector. Just under one-third (29.1%) of total public expenditures take place at the local (kabupaten/kota) level while another 9.5% of public expenditures are made at the provincial level. This reflects the functional responsibilities assigned to local government. In addition to these provincial and local expenditures, 9.7% of total public expenditures are made by central government ministries for public services that are delivered at the local level. The national government retains 51.7% of public sector resources for national functions and activities that fall outside the local public sector.

The high level of decentralization in Indonesia also translates into an above-average degree of localization of health and education expenditures. In the health sector, 81 percent of sectoral expenditures are made within the local public sector, whereas 88 percent of education expenditures are spent at the local level. In both sectors, the vast majority of these expenditures represent devolved expenditures made by local governments. Centrally-controlled localized spending only represents a relatively small share of sectoral expenditures in the health sector (12 percent), while centrally-

controlled funding for higher education causes the corresponding percentage to be larger in the education sector (24.4 percent).

Despite the high degree of devolved spending in Indonesia, the central government continues to play an important role in funding public services at the provincial and local levels. The majority of local government funding (77.8%) comes in the form of intergovernmental fiscal transfers, with 71.1% of local government funds being contributed by the central government in the form of general purpose transfers (revenue sharing and equalization grants, known as the DAU). In addition, 6.7% of local government finances is provided by the central government in the form of earmarked transfers (including capital grants, known as the DAK). Revenues from property taxes, income taxes and natural resource revenues are shared between the central and local level on a derivation basis. Own source revenues account for 22.3% of funds at the local government level.

D. Country Case: the Philippines

The Philippines is one of the earliest and best-known cases where decentralization was pursued in Asia as a successful democratization strategy following the overthrow of Ferdinand Marcos.⁴⁹

Why did the Philippines decentralize? The geography of the Philippines—composed of numerous islands—makes travel and communication difficult, time-consuming, and costly. As such, a highly centralized form of government would be ineffective in dealing with contingencies in far-flung parts of the country; in addition, concentration of political and administrative power in Manila would result in inequitable development among the different regions. These arguments notwithstanding, the imposition of martial law in 1972 abolished local elections and gave the regime the power to appoint local officials that were beholden to it.

Decentralization reforms in the Philippines were prefaced by the overthrow of Marcos in 1986 and the installation of Corazon Aquino as President.⁵⁰ A year later, the 1987 Constitution was promulgated, which included specific provisions guaranteeing autonomy to local governments. Among the major state policies articulated in the constitution was the premise that “The State shall ensure the autonomy of local governments”. Additionally, Article X, Section 3 of the Constitution provides:

The Congress shall enact a local government code which shall provide for a more responsive and accountable local government structure instituted through a system of decentralization with effective mechanisms of recall, initiative, referendum, allocate among the different local government units their powers, responsibilities and resources, and provide for the qualifications, election, appointment and removal, term, salaries, powers and functions and duties of local officials, and all other matters relating to the organization and operation of local units.

In accordance with the provision stipulated in the 1987 Constitution, the Local Government Code (also known as the Local Autonomy Act) was enacted in 1991. It is considered the most radical and far-

⁴⁹ The country case is based in part on Brillantes and Moscare (2002) and Capuno (2008).

⁵⁰ The interim “Freedom” constitution gave President Aquino the power to “control and exercise general supervision over all local governments.” It was this provision that enabled Mrs. Aquino, through the Minister of Local Government, to remove local officials throughout the country whose loyalties were questionable.

reaching policy, which addressed the previous centralized political administrative system which had most significant political and administrative decisions concentrated in Manila. It radically transformed the nature of the power relationships between the central government and the thousands of local governments in the countryside by transferring the responsibility for the delivery of basic services to the local government units, including appropriate personnel, assets, equipment, programs, and projects.

What is the Philippines' territorial-administrative governance structure? Local government in the Philippines is divided into four levels: (1) Autonomous regions;⁵¹ (2) Provinces and cities independent from a province; (3) Component cities and municipalities; and (4) Barangays. With the exception of autonomous regions, all subnational jurisdictions (i.e., provinces, cities, municipalities and barangays) are all referred to as Local Government Units (LGUs).

The provincial government takes care of the functions that affect the people of a certain province, and forms the largest subnational political unit in the country. At present, there are 81 provinces in the Philippines, further subdivided into component cities and municipalities. The municipality is a public corporation created by an Act of Congress and is governed by the Local Government Code, which defines its duties and powers. Being public corporations, municipalities can sue or be sued in court; enter into contracts; acquire and hold real and personal properties for municipal purposes; and exercise such other powers as are granted by law. Municipalities are classified according to their average annual income for the last four fiscal years. There are close to 1,500 municipalities in the Philippines. They are autonomous units of government and have elective and appointive officials.

What is the functional assignment for health and education? The Local Government Code devolves to local government units the responsibility for the delivery of various aspects of basic services that earlier were the responsibility of the national government. These basic services include local health services; social welfare services; certain environmental functions (including community-based forestry projects), agricultural extension service and on-site agricultural research; public works funded by local funds; some education functions (including school building program); tourism (facilities, promotion and development); telecommunications services and housing projects (for provinces and cities); and other services such as investment support.

Although LGUs play a role in both local health services as well as basic education services, LGUs were assigned greater health functions than education functions. The national Department of Health Education and the Department of Health are the relevant line ministries for these two sectors in the Philippines. In particular, the Department of Education (as well as the Department of Health, albeit to a much lesser extent) continues to play an important role in the delivery of localized services.

In the case of health service provision, the functions that were devolved to the local level included the provision of primary, secondary, and tertiary care services, most of the hospitals, health facilities, and personnel involved in the delivery of the three levels of care. The estimated Department of Health (DOH) budget allocation for the devolved function was nearly one billion pesos or approximately 39 percent of its total budget in 2002. The nearly 46,000 devolved health personnel constituted about 61 percent of the total DOH manpower. An important feature of the Code is that each LGU is mandated to establish a Local Health Board. Comprising local officials and private sector representatives, the Local

⁵¹ Currently, only one autonomous region exists: the Autonomous Region in Muslim Mindanao (ARMM).

Health Board is a mechanism for constituents and service clients to directly influence the local health budget and advise the LGU on health issues and concerns.

The Code also devolved education functions to LGUs, albeit to a much lesser extent than in the case of health services. Specifically, the municipalities and cities were given the responsibility of constructing and maintaining school buildings and other facilities. However, the core responsibility for providing primary, secondary and tertiary education (including hiring, firing, and managing teachers) remained with the central Department of Education. In order for municipalities to finance these expenditures, the LGUs are allowed to collect an additional one percent in real property taxes, called the Special Education Fund (SEF), mobilize resources from other sources, or both. The disbursement of the Special Education Fund (SEF) should be based on the annual education budget developed by the Local School Board. Like the Local Health Board, the Local School Board is also a mandated consultative body and venue for direct participation of the private sector representatives in local service delivery.

While the Department of Health devolved more functions than the Department of Education, the latter deconcentrated more functions than the former. In line with the Governance of the Basic Education Act (1991), subnational offices of Department of Education have considerable powers and responsibilities. Specifically, the subnational education offices are required to develop their own regional education plan and formulate and execute the corresponding annual regional budget. They are also assigned full management of human resources for education, and the monitoring and evaluation of the education outcomes.

More importantly, however, the school heads are now assigned both as instructional leaders and managers. As instructional leaders, the school heads such as principals are responsible for implementing the curriculum and accountable for the education outcomes of the school. As managers, they can introduce education programs and improvement plans for the school's physical set up and human resource complement. The national office of Department of Education formulates and implements the national education policies, plans, programs and projects. It also tracks and evaluates national learning outcomes, and undertakes the educational RandD activities.

How are these functions funded? The Local Government Code provides a range of financial resources to local government units, including (1) their own taxing powers as well as revenues from local fees and charges; (2) revenue sharing from the national wealth exploited in their areas (e.g., mining, fishery and forestry charges); and (3) allocation to LGUs of a share from the national taxes.

When the responsibility for health transferred to the local level, the financing of the devolved health functions also became the responsibility of the LGUs (Capuno, 2008). LGUs received a substantial increase in the share of the internal revenues of the national government and in the proceeds from sale of natural wealth (like mineral resources), and from other locally sourced revenues.

All or nearly all of the revenue that a local government has to spend comes from their IRA, which is allocated among LGUs based on an objective resource allocation formula. Own and shared revenue sources typically form a smaller share of LGU finances. For municipalities, the IRA typically accounts for around 90% of total revenues. Since cities generally have a larger economic base for local taxation, internal revenue allotments for cities typically account for 50 - 70% of their total budgetary resources.

The IRA is automatically released to each local government unit and may not be held back by the national government for any reason, except in extreme cases.

E. Country Case: Kerala

Unlike the other country cases in this chapter, Kerala is a state in India, rather than an independent nation-state.⁵² Its decentralization reforms were driven by a combination of endogenous political forces as well as by reforms to the Constitution of India.⁵³ The 73rd Constitutional amendment passed in 1993 aimed to improve the limited democratic participation below the state level by granting local rural governments new powers and making them more accountable to citizens. Kerala is often cited as one of the most progressive states (if not, *the* most progressive state) within India in terms of decentralization. Although state-to-local decentralization in India under the Panchayat Raj system is enshrined in the Constitution and promoted by the central (Union) government, the implementation was left up to the states and adoption across states in India show a high degree of variability.

Why did Kerala decentralize? According to Heller, Harilal, and Chaudhuri (2007), the most determined effort at democratic decentralization—in line with the 73rd Constitutional amendment—has been in the state of Kerala. In 1996, a coalition of leftist parties led by the Communist Party of India returned to power and immediately fulfilled one of its most important campaign pledges by launching the “People’s Campaign for Decentralized Planning.” All 1,214 local governments in Kerala were given new functions, powers of decision-making, and were granted discretionary budgeting authority over 35–40% of the state’s developmental expenditures.

In addition to devolving resources, state officials sought to directly promote participatory democracy by mandating structures and processes designed to maximize the direct involvement of citizens in planning and budgeting. In both its scope and design, the campaign represents the most ambitious and concerted state-led effort to build local institutions of participatory democratic governance ever undertaken in the subcontinent.

What is Kerala’s territorial-administrative governance structure? Kerala’s territorial-administrative structure in the rural areas recognized three government levels: 14 rural district governments (zilla panchayats); 152 intermediate rural government (or block panchayats), and 999 village governments or gram panchayats (Sanu George, 2007).⁵⁴

What is the functional assignment for health and education? Decentralization in Kerala has been most effective at the level of village panchayats (Varatharajan, Thankappan and Jayapalan, 2004). Already prior to the devolution reforms, own sources of income at the village level form a considerable share of their total income (44% in Kerala, against the Indian average of 10% in 1993–94). Each village panchayat covers an average population of around 25,000 (ranging roughly from 5,000-70,000 residents). The village government exercises control over government institutions within the village, including schools and primary health centers. Kerala’s relatively high-density population helps the institutional structure of the government in serving the population more easily.

⁵² India consists of 29 states, seven Union Territories, and one National Capital Region.

⁵³ This section draws in part on Heller, Harilal and Chaudhuri (2007) and Sanu George (2007).

⁵⁴ Urban local government institutions include 5 City Corporations and 53 municipalities.

Apart from the important role played in local health services by panchayats in Kerala (when compared with the other Indian States), the organization of government-provided health-care delivery in Kerala does not differ much from the rest of the country. The primary health center (PHC) is the core institution in the rural health care infrastructure. Each PHC is staffed by a medical doctor, nurse, pharmacist, field supervisor, nursing assistant, clerk, five junior public health nurses, three junior health inspectors, three attendants, a peon, and a sweeper. District Hospitals and Community Health Centers (CHC) usually serve as its referral units. Kerala has 944 PHCs each catering to an average population of around 25,000 and a radial catchment area of about 3.5 km (Varatharajan, Thankappan, and Jayapalan, 2004). Each PHC has five or six sub-centers below it, each serving an average 5,000 people.

As part of the decentralization reforms, PHCs were brought under the (managerial and part disciplinary) control of village panchayats in 1997. Panchayats can appoint temporary staff (against existing vacancy), assign any work related to their area of specialty to the PHC staff, review staff performance, give required directions, and impose minor penalties or suspension if warranted. State government retains the authority to create new posts.

In educational matters, the panchayats at each level are expected to function according to powers delegated by the Kerala Panchayati Raj Act of 1994. Kerala's education system has a 10 + 2 + 3 structure: 10 years of basic education followed by 2 years of upper secondary and 3 years of higher education (Mukundan and Bray, 2004). The cycle of basic education is subdivided into four years of lower primary (Standards I–IV), three years of upper primary (Standards V–VII), and three years of lower secondary education (Classes VIII–X). Schools are classified into three groups: government, aided, and private. In 2003, Kerala had 6,726 lower primary schools, of which 37.4% were government, 60% were aided, and 2.5% were private. The state also had 2,968 upper primary schools and 2,580 secondary schools. However, many of the secondary schools also had primary sections. Basic education up to Standard VII was made the primary responsibility of the village panchayats, whereas upper primary and secondary education became the responsibility of district panchayats. Accordingly, the responsibility for school management and oversight for the different types of school was transferred to different types of panchayats between 1996 through 1999.

Despite the devolution of health and education facilities to the local level, there was very little change in the administrative system and functioning of schools at the district and local levels. Although school authorities and teachers were to a certain extent required to implement instructions given by the administrative bodies of the local governments when implementing or participating in educational projects, the responsibility for the management of human and physical resources at the school level remained largely vested with the departmental bureaucrats and controlled by them based on the Kerala Education Rules and Kerala Service Rules (Mukundan and Bray, 2004).

In fact, despite the widely touted decentralization reforms in Kerala, the reforms mostly took place on the development side of the budget. For instance, within the education sector, the departmental bureaucratic administration at the field level (district and below) continues to operate as a part of the deconcentrated line ministry structure, and controls over all aspects of education in the district. These education staff are state government employees and accrue all service benefits sanctioned by the state government and the General Education Department. Similarly, the appointment, promotion, transfer, and service benefits of head teachers and teachers in government primary schools continue to be determined by the deconcentrated administration based on state-level norms. Their salaries are paid by

the state government. Likewise, head teachers and teachers in “aided” primary schools also continue to be promoted, appointed and transferred by their concerned management with the ratification of officers in the (deconcentrated) education department and paid by the state government.

As such, the bulk of recurrent responsibilities for the delivery of education services continues to be delivered in a deconcentrated manner under state control. These responsibilities include distribution of responsibilities of head teachers and teachers; admission of pupils; appointments, staffing, salaries and other service benefits; sanctioning of leave; suspension and dismissal of teaching and non-teaching staff; curriculum and assessment; inspections and auditing; and the role of statutory bodies including Parent–Teacher Associations.

How are these functions funded? The decentralization process in Kerala has resulted in a major devolution of resources, particularly on the development side of the budget. The advantage of Kerala’s decentralization is the dynamism that it has brought into the resource allocation mechanism. Financial devolution to panchayats is such that each village panchayat in Kerala, on average, commanded control over Rs.9.8 million (around US\$200,000) in development resources in 2001–02.

Nevertheless, the health sector has failed to attract development funding from panchayat resources, partly because of the State Planning Board directives and partly because of the health sector’s lukewarm response to the entire decentralization process (Varatharajan, Thankappan and Jayapalan, 2004). In the absence of active lobbying and technical expertise to convert health care needs into fundable projects, the panchayats were helpless and allocated insufficient funds to health.

Equally, there is some degree of disillusionment with the degree that decentralization has brought to the education sector (Mukundan and Bray, 2004). Perhaps the most important factor explaining the gap between rhetoric and reality lies in the nature of the *People’s Campaign for Decentralized Planning*. State-level planners overestimated the capacity of administrators and community members at the local level, and policy-makers mistakenly assumed that the participants in the Grama Sabhas could, with assistance, rise to the challenge fairly easily. In practice, when the Grama Sabhas did identify needs, they tended to focus on capital works and on familiar schemes such as noon-day feeding.⁵⁵ The ‘softer’, qualitative sides of education proved much more difficult to address.

In addition, it bears repeating that even though decentralization on the development side of the budget has been substantial, decentralization on the recurrent side of the budget has been trivial. Salaries for all subnational staff—including front-line service delivery staff—continue to flow through vertical (deconcentrated) channels. This means that, in effect, the potential positive impact of decentralization on service delivery outcomes should not be over-estimated.

F. Country Case: Sierra Leone

Sierra Leone is in the middle of an interesting decentralization trajectory (Edwards, Yilmaz, and Boex, 2014). Although by law, elected Local Councils are fully responsible for the decentralized delivery of key public services—including health and education—in practice, the implementation of the devolution

⁵⁵ It was noted that when village panchayats did develop projects in the education sector, only a minority, most of them related to construction of buildings and toilets, and were implemented as planned.

reforms has lagged behind the law. This has resulted in a hybrid situation where Local Councils have *de facto* control over the operation and maintenance expenditures for localized services, while the local staff of sectoral departments continue to report to (and get paid by) their respective central line ministries. Although decentralization is still incomplete, partial control of Local Councils over local service delivery is giving local politicians an opportunity to contribute in a positive way to improving local public services, without the risks of wholesale devolution.

Why did Sierra Leone decentralize? Sierra Leone began its transition towards decentralized government in 2002, following the peace process that ended over a decade of civil war and strife. Although the country's Constitution does not specifically provide for a decentralized system of local government, Parliament passed the Local Government Act in 2004 (re-)establishing an elected local government level.

Since 2004, considerable progress has been made in devolving public service delivery functions from the central line ministries to the Local Councils. Despite considerable progress in the devolution of political powers and functional responsibilities, Local Councils remain seriously constrained by limited administrative devolution, as all 'local' public servants—such as teachers and health workers—in practice remain staff of their respective line ministries. In addition, limits of local own-source revenues as well as limits on the provision of intergovernmental fiscal transfers constrain the ability of Local Councils to improve the quality and access of local public services.

What is Sierra Leone's territorial-administrative governance structure? Sierra Leone's public sector hierarchy comprises governmental entities operating at the National, District, and Chiefdom levels. The Local Government Act (2004) established thirteen District Councils, five Town Councils, and the Freetown City Council. The 19 Local Councils are further subdivided into wards, the smallest level of local political organization. Sierra Leone's 149 Chiefdoms overlap with these District Councils, and are governed by Paramount Chiefs and Chiefdom Councils drawn from eligible families. Some governance responsibilities, notably poll tax collection, are shared between councils and chiefdoms, although the precise limits of the authority of Chiefdoms are still being negotiated.

Local Councils have a relatively high degree of autonomy in conducting their political and some fiscal affairs. The degree of administrative autonomy is distinctly split. While Local Councils have substantial administrative authority over procurement and over the management of junior council staff, they have little or no control over the number of establishments, hiring, firing, wage setting or payroll for senior council staff or for the staff of the various local sectoral departments which notionally fall under their responsibility. Extremely limited own-source revenues and the absence of untied grants further constrain the ability of Local Councils to conduct activities outside of those funded by administrative grants, sectoral grants, and the limited cross-sectoral development resources available to them.

What is the functional assignment for health and education? Sierra Leone's Local Government Act (2004) provides for the devolution of all aspects of some 80 functions to Local Councils, with funding for these services to be secured through a combination of Local Council own-source revenues and formula-based grant allocations. The list of devolved functions includes primary and secondary education as well as the provision of basic health services.

The National Decentralization Policy (2010) notes that the assignment of functions and expenditure responsibilities to local councils should be aligned in accordance with the subsidiarity principle. As of

2011, 47 functions had been partially devolved, including the responsibility for basic education, basic health services, agricultural extension services, water provision, solid waste management, fire protection, and other community-level services. Although the responsibility for these functions has formally been transferred to the Local Councils, the sectoral functionaries at the local level continue to be appointed and managed by the central government. Efforts are ongoing to ensure that at a minimum, the performance review of the heads of local sectoral department would be conducted by the Local Council.

How are these functions funded? Given the fact that Local Councils in Sierra Leone only have *de facto* control over the operation and maintenance portion of localized service delivery, Local Councils have direct authority over only 6.9% of public expenditures, consisting chiefly of operation and maintenance expenditures for local health, education, and agricultural activities. Central line ministries, however, spend an additional 39.7% of public expenditures on localized public services, covering the vast majority of local wages and local development expenditures. In total, therefore, local public sector expenditures account for 46.3% of total public spending in Sierra Leone. This relatively large share of spending that is directed towards the local level in Sierra Leone came somewhat as a surprise to most policy analysts.

Within the health sector, slightly less than 72 percent of health expenditures are localized, whereas the corresponding percentage in the education sector is 89 percent. However, it bears repeating that only small shares of these resources (19 out of 72 percent in health, and 9.3 out of 89 percent in education) are actually managed by Local Councils. Although Local Councils have some control over sectoral O&M, they are still unable to either hold local sectoral staff accountable for poor performance or reward them for good performance as all wage expenditures are controlled by the respective line ministries. The poor accountability of local sectoral staff may explain the fact that Sierra Leone ranks near the bottom in terms of its literacy rate (61 percent) as well as its under-five mortality rate (188 per 1000).

Local Councils are highly dependent on intergovernmental fiscal transfers. Sectorally earmarked intergovernmental transfers account for 78% of local financial resources; no unconditional grants are provided. Local own-source revenues, including poll taxes, fees, and all other revenues account for only 1% of national revenue collections. Outside the main urban areas, most locally collected revenues are retained by the Chiefdom Councils. Although the Local Government Act (2004) allows for local borrowing with central government approval, in practice, local governments are currently prevented from borrowing funds.

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