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Strengthening Local Government Budgeting and Accountability

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Abstract

In many developing and middle-income countries, decentralization reforms are promoting changes in governance structures that are reshaping the relationship between local governments and citizens. The success of these decentralization reforms depends on the existence of sound public financial systems both at the central and local levels. This paper focuses on the role of budgeting as a critical tool in reform efforts, highlighting problems that might impede successful local government budget development and implementation. The attainment of effective local government accountability and transparency is not an end itself, but rather it represents the means to support better decision-making on national and local budgeting. Community based schemes for enhancing local government accountability need to combine legal, political, and administrative mechanisms with proactive community involvement. Of particular importance are the legal and budgetary instruments that require input from local community members on certain local government decisions and instruments that increase accessibility for the press or the general public at large to information on government activities.

This paper—a product of the Social Development Department, Sustainable Development Network—is part of a larger effort in the department to study local governance systems and decentralization in the client countries. Policy Research Working Papers are also posted on the Web at http://econ.worldbank.org. The author may be contacted at syilmaz@worldbank.org.

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Strengthening Local Government Budgeting and Accountability

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Strengthening Local Government Budgeting and Accountability

1 Introduction

Across many developing and middle-income countries, reforms are being undertaken to improve governance by introducing new institutional and technical systems intended to increase the transparency and accountability of governments. Most evident are efforts to decentralize government functions to lower tiers of government. Through these reforms, governments are promoting changes to governance structures that are reshaping the relationship between local governments and citizens. However, the success of these reforms depends on the existence of sound public financial systems both at the central and local levels: weak or non-existent or absent public financial management functions and institutions are likely to negate any advantages that might be inherent in bringing public services "closer" to people (Ahmad, Albino-War and Singh 2006). As a primary financial management tool of governments, the annual budget is a logical place to focus reform efforts. Budgets intersect with all aspects of governance reform including fiscal policy, administrative reform, anticorruption efforts, social policy and service delivery.

At the local level, local[1] government budgeting can be described as a series of steps that link policy (people's preferences and needs) to financial planning (budget) to actual budget implementation (service delivery, operations). While efforts on local government budgeting innovations in developing and middle-income countries are relatively new, and few quantitative evaluations have emerged, anecdotal evidence suggests that increased local community involvement in the budget process can lead to improvements in budget efficiency, service delivery and investment in underserved areas.

Local government budget innovations are designed to improve financial accountability, which requires that municipal governments prudently manage their finances to ensure integrity in their financial and non-financial reporting, control, budgeting, and performance systems (Sahgal and Chakrapani 2000). Financial accountability also necessitates reporting comprehensively on what local governments have achieved with their expenditures. Financial accountability of local governments is strengthened by integrating approaches that marry supply-side public sector accountability (i.e. publicly available audit findings) with demand-side social accountability instruments (i.e. accessible local government financial information).

[1] We use the terms subnational, local and municipal interchangeably throughout the text to refer to levels of government below the central government.

The supply side of accountability, which is also known as public accountability,[2] is the hallmark of and a *sine qua non* for good governance (Bovens 2006). Supply side measures to improve downward financial accountability include strong local capacity for budgeting and public financial management; standards for control on intergovernmental transfer revenues (i.e., clean audit reports, submission of financial statements); publication of transfer figures; transparent local public audit systems—with publicly available audit findings, clear rules for responsible local borrowing (including rules regarding defaults), public access to borrowing information, and clearly defined rules regarding hard budget constraints for local governments.

Demand side accountability, also known as social accountability, refers to a broad range of actions and mechanisms beyond voting that citizens can use to hold the state and providers of public services accountable. Demand side measures for financial accountability include publicly accessible local government financial information (including budgets, end-of-year financial statements and periodic implementation progress reports during fiscal year); public involvement in budgetary process through participatory budgeting practices; gender-sensitive planning, budgeting, and resource allocation, reinforced by gender audits; independent budget analysis and participatory public expenditure tracking programs that monitor budget execution and leakage of funds.

The focus of this paper is to outline the role of budgeting as a critical tool of local government finance in developing and middle-income countries; highlighting problems that might impede successful local government budget development and implementation. The paper presents guidelines and suggestions for improvements to strengthen local budgeting practices in developing countries. We assert that local government accountability and transparency is not an end itself, but rather it represents the means to support better decision-making on national and local budgeting. We also provide evidence that community (demand-side) participation is necessary, but not a sufficient condition, for enabling greater local government accountability. Community based schemes for enhancing local government accountability generally need to combine legal, political, and administrative mechanisms with proactive community involvement. Of particular importance are the legal and budgetary instruments that require input from local community members on certain local government decisions and instruments that increase accessibility for the press or the general public at large to information on government activities.

[2] Public accountability refers to the institutionalized practice of account giving—it focuses on public sector managers who spend public money, exercise public authority, and manage a corporate body under public law. Public account giving provides political representatives and voters with the necessary inputs for judging the fairness, effectiveness, and efficiency of their governance system (Manin, Przeworski, and Stokes 1999). The formal doctrine of elected representatives' responsibility rests upon the notion of representative democracy and parliamentary sovereignty. The elected representatives of people—parliament—bring the government—the executive—to account. Parliament enacts administrative laws to enforce accountability. On the other hand, poor governance and lack of public sector accountability may result from a number of factors including civil service incompetence, lack of efficient institutions, and pervasive corruption (Schaeffer 2005).

2 Theory and Evolution of Budgeting

In social sciences a theory is a testable model of human interactions capable of predicting future occurrences or events of the same kind as well as capable of being tested through experiment or otherwise verified through observation. Budgeting does not have a theory in the classical sense of providing an orientation to the field, stating assumptions and pointing to some hypotheses about what causes what (Rubin 1997). According to Rubin, budget theory "is fragmented and incomplete… [it] is in the process of being invented" (Rubin 1997: 185). In other words, the theory of effective budgeting is continually evolving. Scholars see "the study of budgeting as part of a larger research agenda which would ultimately enable prediction of consequences and the comparative analysis of governmental policy" (Caiden 1994: 44). Many budget policies, procedures, and technical practices that we currently associate with modern budgeting were developed during the nineteenth century when major changes in budget practices occurred in France. At the time Napoleon's primary concern was with mastering the military budget. To obtain better information and control on military spending, Napoleon established the Cours des Comptes (Webber and Wildavsky 1986).

Early 19th century France saw the establishment of the words budget and budgetary procedures. By the 1860s, France had developed a uniform accounting system that it applied to all departments and units within departments, a standard fiscal year, conventions on how long encumbrances can be held open after the close of the fiscal year, and a requirement that all departments explain programmatically and account fiscally for all funds which they were allocated. The budget was considered to be one of the government's primary policy documents. Indeed, the control of government expenditures was assured through the scheduling of expenditures by different departments. Expenditure claims that exceeded a budget category would not be honored for payment.

British budgetary practices of the mid-19th century lacked not only many of the technical features of the French budgetary system, but had not adopted the emphasis on consistency and universality of application that was central to the underlying public sector budget process. For example, although most funds under the mid-19th century British system were appropriated by Parliament, there was no singular document reflecting all government expenditures, no comparisons between budgeted expenditures versus actual expenditures, and different accounting mechanisms where used by various departments. Lump sum appropriations were widely used. During the period when William Gladstone was Chancellor of the Exchequer and later Prime Minister, he and other reformers integrated many of the more advanced features of French budgetary techniques as a way of controlling government finances. For example, in 1861 the Public Accounts Committee was created in England. In 1866, the offices of the Comptroller and Auditor General were created. Gladstone emphasized the notion of balancing the budget. This principal became a technical feature of his budgets (Webber and Wildavsky 1986). Thus by the end of the 19th century the framework for modern government budgeting (unity, balance, comprehensiveness, and control) had emerged in Europe.

In contrast to Europe, budget reform in the United States was initially established at the local not national government levels. This was in part due to the fact that the public

had more direct control over local activities. Mass immigration, coupled with increasing industrialization and urbanization, created large demands upon local governments for housing, education, health care and transportation (Rabin 1997; Webber and Wildavsky 1986). To more efficiently manage these increasing demands on government services, standardized accounting, reporting, and auditing practices were introduced.

The budgeting process in the United States was largely impacted by two competing coalitions: (1) The Federalists (Whigs) who supported an active government to promote commerce, build infrastructure necessary for economic activity, and develop the financial institutions necessary to support economic growth; and, (2) The Republicans (Democratic Republicans, then later Democrats) who believed that taxes should be kept low and government kept at a minimum so that small farmers and tradesman could freely pursue their trade without government hindrance (Rabin 1997). Competing coalitions were kept in equilibrium through the norm of a balanced budget. The norm of a balanced budget solidified into a practical limitation on government activity. Rather than developing the technical capabilities to control spending as was occurring in Europe, the United States controlled budgetary outlays simply by keeping the government small (Webber and Wildavsky 1986). Congress itself had no mechanism to ensure that appropriate spending was being implemented without modifications.

To address the problems of mounting debt, the fragmentation of power and the absence of public accountability and control in combating corruption 19th and 20th century budget reformers in the U.S. proposed an array of improvements including uniform accounting and auditing practices, and a series of practices for financial planning and administration that came to be known as the executive budget movement. Central to the reforms in the U.S. of this era was the concept of the responsible executive (i.e., a strong mayor). In effect, reformers were adopting many of the business practices of the day with strong executive authority (i.e. a strong business executive). The first principal of this movement became that budgets should be developed and proposed by the executive to accomplish stated objectives for which the executive would later be held accountable to the voters. For fiscal clarity, budgets would be unified and encompass not only expenditures but also revenues. Public sector budgeting would essentially follow the practice of American corporations by being comprehensive, balanced and annual (Taylor 1911). A uniform accounting system, the establishment of a comptroller, and protocols for both reporting and auditing would aid the development and implementation of the budget.

A key development in budget theory has been the differentiation between micro-budgeting and macro-budgeting and the inherent tension between them (LeLoup, 1988). Macro-budgeting is where high level decisions on spending, revenue and deficit aggregates and relative budget share are often made from the top down. Micro-budgeting is where intermediate level decisions on agencies, programs, and line-items are usually made from the bottom up. Both levels of budgeting analysis are interested in how power is structured in budgetary processes as well as how it is exercised and expressed through budgetary choices. These techniques helped to link budgeting to a larger agenda of improving public sector performance.

The evolution of budget theory and policy-making practices illustrates that undeniable progress has been achieved, often on modest fronts and with reasonably

simple techniques. Budget practices across the globe have been gradually evolving into becoming more uniform with respect to accounting and auditing practices, balance, and control. Lost in the evolution of effective budgeting practices is the identification of demand side (social accountability to the local community) issues of identification of needs (budget planning), managerial efficiency (budget execution), and effectiveness of implementation (budget execution).

In the 1980s and 1990s, both national and subnational governments have witnessed dramatic changes in budgeting. Along the way, decentralization became an important component of public sector reform efforts eliminating the planning bureaucracy's monopoly over the budget. In many countries "[w]idespread interest in democratization encouraged devolution of authority to autonomous municipal governments as counterweights to the centralized governments of the past, and in holding regularly scheduled elections to transfer power from traditional national level ruling elites to accountable elected officials" (Guess 1997:248). In these countries, transition from centrally planned systems to democracies led to a demand for greater accountability, which in return required a transparent financial management system. An ongoing challenge for countries in implementing decentralization programs is to develop coordinated budgetary and financial management reform policies across levels of government to ensure correspondence with national macroeconomic objectives for inflation, growth, fiscal and monetary stabilization (Ter-Minassian, 1997) and linking better budget formulation and expenditure processes to proactive civil involvement and oversight.

3 Connecting Budget with Policy Objectives

Budgeting takes place within a political arena and the outcome is a political document through which money is appropriated according to value judgments by decision makers to reflect the community's values, preferences and priorities (Gildenhuys, 1997). In order to understand the budgeting process it is necessary to understand the accompanying processes of policy and planning. Studying budgeting entails identifying coalitions, understanding the distribution of roles among various stakeholders and the incentive structures to which they respond, and predicting outcomes to be expected in terms of amounts requested and received (Heclo and Wildavsky, 1974).

A local municipal budget is not just a statement of government finances but is the link between the mobilization of funds and attainment of government goals and objectives. A government, both central and local, should have specific policies, plans and programs to achieve its long-term goals. Although developing broad goals could be part of a separate strategic planning process, financing for the achievement of these goals comes from the budget. As a result, local governments need to give adequate attention towards establishing linkages between policy objectives and budgeting exercise and ensuring that those high priority policy objectives are appropriately funded. The budget should be the centerpiece of a thoughtful, ongoing, decision-making process for allocating resources and setting priorities and direction.

Today, many national and local governments across the globe are trying to move away from input-oriented incremental line item budgeting to output-oriented results-driven budgeting practice, such as program budgeting, performance budgeting, and

target-based budgeting. In these countries, budget reform programs intend to break the domination of hierarchies and provide flexibility to public sector managers in decision-making. Experience from many developing countries suggests that establishing linkages among budgeting and planning systems has been a difficult task. In many developing and middle-income countries, planning and programming exercises are ineffective due to various reasons including lack of capacity and data. Evidence so far indicates that there also are significant shortcomings with regard to public financial accountability measures in preventing the misuse of public resources, resulting in fraud and corruption, among others. We briefly explore the gradual evolution from line item to program budgeting at the local municipal government level in the following sections.

3.1 Line Item Budget: The Predominant Method of Local Government Budgeting

Municipal budgets have historically been constructed on the basis of incremental line-item budgeting practice, perhaps reflecting the accounting (or bookkeeping) background of their municipal staff members, and the close relationship of the budget to the audited financial statements required to be submitted by municipal authorities after the fiscal year. However, in many municipalities actual spending may be controlled and managed on a broader, less detailed level. Monitoring and controlling budget expenditures on a broader, less detailed level allows for some degree of flexibility in spending while still exercising substantial control in minimizing any potential for expenditure overruns.

The primary orientation of a line-item budget is that of expenditure control and local administrative accountability. Normally, funds spent on line items and staffing levels are described as budgetary inputs. Accordingly, a certain type of performance measure can reflect the progress of a local government organization with respect to spending in accord with its line item budget. While the simplest budget to prepare, the line-item budget does not provide any information regarding activities and functions of a program, department, or municipality. The line-item budget assists municipal officials in understanding how much they are spending on salaries, supplies, and maintenance, but does not reveal how much is being spent on the actual delivery of services.

The line-item budget however, does not provide any information regarding the achievements of an organization, department or government. Kitchen (2005:156) observes that “the incrementalist (line item) approach …provides no mechanism for assessing the benefits from existing expenditures and, therefore, no rationale for encouraging local officials to allocate their resources in an efficient manner … In essence, control budgeting is important but it often creates a narrow and cumbersome financial system characterized by paperwork, detail, duplication, complexity, and inflexibility.” Knowing how much you are spending for salaries, supplies, maintenance, and utilities does not reveal much about the actual delivery of services such as: How many citizens are being provided with social services? How many kilometers of roads are maintained? What is the cost per kilometer of maintained roads? How many children are in school? What is the quality of education?

Municipal budget reforms of the last two decades have focused on how to inject a long-term perspective into the existing incremental budget practice in order to reorient local budgeting practice on results and outcomes. Traditional line-item budgeting makes

achieving these goals very difficult. The main problem of incremental line item budgeting is that the expenditure items are related to business needs, such as wage and salary, operations and maintenance, rather than achieving a broader program or policy objectives. The line item budget tells nothing about the cost or efficiency of programs delivered, and provides very little information to decision makers and the local constituency on how expenditures were prioritized or which programs/projects should be financed or cut. In order to determine the cost of service delivery, expenditures must be re-arranged into programs or activities. Further, the line-item budget may have a timeframe of a single budget cycle and therefore does not consider the multi-year implications of the decisions made.

Many local municipal governments have introduced process and format reforms reflecting more current thinking about the achievement of goals rather than strictly focusing on cost control. For example, over the last five years, Dubai municipality in the United Arab Emirates has introduced a programmatic budget structure at the local municipal level. While still in its infancy, Dubai municipality's programmatic budget structure has achieved limited success in mapping its programs, outcomes and outputs. The municipality has introduced new budget features in-step with upgrading its financial management systems. However, the complexity of undertaking many overlapping reforms all at once has tempered the success, to some extent, of the movement towards greater budget accountability. Notwithstanding the evolutionary movement to alternative budget format reforms, the importance of cost control as a fundamental feature of the reformed budget is still maintained. As part of an ongoing process, municipalities are increasingly linking their budget formulation and expenditure management efforts to performance measures and greater public sector accountability.

3.2 Program Budgeting at the Local Government Level

Budgetary systems found under the name of program budgeting often vary in their structure as a result of being adapted to local conditions. The general features of program budgeting applied to local governments listed by Bellamy and Kluvers (1995) as: defining objectives and programs to achieve those objectives; appropriation by programs; use of performance indicators to measure program outputs, and in some cases use of cost/benefits or other forms of financial or economic analysis.

A local government program budget differs from the traditional line-item approach to preparing, reviewing, and presenting the budget. In a program budget, revenues and expenditures are linked to multi-year community goals and objectives—establishing political accountability links. The underlying theme of any local government program budget structure is to provide greater clarity to local community as to what the community's shared goals are, the priority of these shared goals and to provide the community with an indication of whether these goals have been achieved or not. Program areas often utilized by local governments include public safety, public works, human services, leisure services, and general government.

The primary point of reference of program budgeting is that it allows municipal leaders and community members to plan a budget in a manner that allows for improved decision-making creating stronger accountability links between local residents and decision makers. The emphasis is on the attainment of long-term local community goals.

A program budget identifies the anticipated results and outputs and outcomes of spending items and helps to address the local government's proper role and responsibility in addressing the needs of the community.

Research on local government program budgets in the United States and Australia indicate that it has become an accepted management tool. Poister and Streib (1989) found that the percentage of cities using program budgeting in the United States had stabilized by the end of the 1980s to about 77 percent of all municipalities. What have been the general consequences of adopting program budgeting at the local government level? Tower (1998) and Kluvers (2001) surmise that costs were better controlled under program budgeting than under line-item budgeting; and, local government program budget practitioners were able to sort out expenditures into direct and allocated costs more efficiently. Although research results offer support for the proposition that local program budgets enable greater cost control, the results are not overwhelming.

Efforts to introduce performance based program budgeting are useful in allowing the local community to examine costs in detail and to connect expenditures to expected outcomes. However, local governments, particularly in developing and many middle-income countries, often face significant human resource constraints in implementing this type of budgeting and the concomitant change in the accounting mechanisms that it requires. While program budgeting systems may be an attractive tool to generate accountability in spending agencies at all levels of governments, many countries often lack the necessary preconditions and preparatory work at the local government level for effective implementation.

Apart from thorough prior planning and capacity building, the introduction of program budgeting requires a relatively advanced state of performance measurement, accounting and financial management systems being in place. These preconditions do not appear to currently exist in many developing and some middle-income country local municipal governments. Moreover, introducing program budgeting before the foundations for ordinary budgeting (i.e. effective accounting, reporting and monitoring) are fully in place risks undermines the overall development of the budgetary and financial management of the government. Without effective budget tracking tools, which in many developing countries are non-existent at the local government level, it would be premature to rush into program budgeting. Nonetheless, even in such countries where subnational government budgeting practices are more fundamental, a performance orientation to budgeting and steps toward managing for performance can be introduced, albeit in a more simple form. With respect to multi- or bi-lateral technical assistance, donors should be prudent in advocating the adoption of performance (program) budgeting simultaneous with more participatory forms of budgeting. If enacted simultaneously, these two reforms may overwhelm local governments and constituents trying to adjust to the new system.

The conditions under which local governments have the right incentive(s) to improve the delivery of basic services have been explored in large volumes of political economy literature. Keefer and Khemani (2005) propose providing citizens with greater information about the resources and responsibilities of their local representatives, so that they are empowered to hold them accountable for the delivery of basic services. The next section describes how the local community can hold municipalities and municipal budget

practitioners accountable for improving the quality of budget presentation and the effectiveness of budget service delivery performance.

4 Achieving Decentralized Accountability

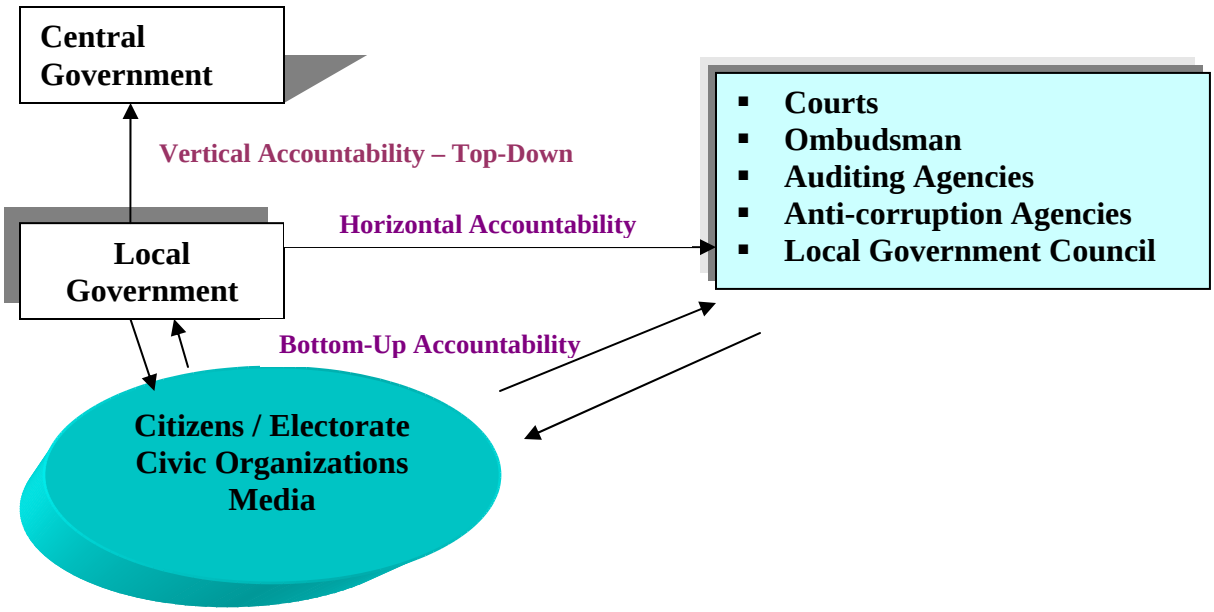
The case for decentralization is fundamentally an argument about improving the process of governance that matches collective (e.g., public) decision-making with respect to subnational (e.g., local) tax and spending decisions to local preferences (Yilmaz, Beris, Serrano-Berthet 2008). The "best" solution is one of an intergovernmental partnership that builds on the platform of fiscally strong local, provincial, and central governments. To make this all work there must be *accountability*; that is, mechanisms (formal systems, institutions, laws, regulations, as well as the informal day-to-day practice of government) must be put in place such that two things occur: political leaders and bureaucrats become answerable to the citizenry for their actions and the citizenry takes on and accepts responsibility for the collective actions that governments make on their behalf.

4.1 Bottom-up Pressures: The Missing Link in Budgeting Reforms

In a well functioning local government budget and managerial structure, a local government is subject to accountability to its citizens, accountability to public agencies and accountability to higher-level governments. These kinds of accountability are referred to as: bottom up—by the local government to local citizens; horizontal accountability—by the local government to various public institutions of accountability; and vertical accountability by the local government to higher-level governments. Bottom-up accountability may include citizens acting through the electoral process or indirectly through civic organizations (i.e. NGOs, civil society) or the news media (See Figure 1).

Horizontal accountability covers the range of public entities in order to check local government abuses and inefficiencies. These agencies may include but are not limited to: electoral commissions, local government councils (or legislature), the court system, ombudsman or public complaints agencies, or various auditing agencies. Local governments are also held accountable to higher-level governments (e.g., central, state). Central (and, state) governments often set the rules under which local governments operate. Additionally, higher-level governments nearly always provide a portion of their financial resources to local governments through fiscal transfers. Thus, there is always some level of financial (budgetary) reporting and accountability by local governments to higher governmental authorities.

Figure 1: Accountability Linkages



Internal administrative accountability must be mirrored by external accountability through feedback from service users and citizens (the social accountability nexus). Strengthening local government accountability is necessary in the context of enhancing initiatives for greater decentralization and for local government managerial autonomy. Effective local budget development requires establishment of expenditure priorities. This process begins with a planning or a preplanning stage during which information flows are both top down and bottom up. Top-down processes establish parameters for budget development in the form of directives to agencies and spending units. These directives should communicate fiscal framework objectives, resource and cost forecast and assumptions, the budget envelope and broad policy priorities. Bottom-up processes should establish linkages with communities to identify people's needs and preferences. Of particular importance are the legal and budgetary instruments that require input from local community members on certain local government decisions and instruments that increase accessibility for the press or the general public at large to information on government activities.

In this process, bottom-up accountability may similarly fall short if elections are dominated by political elites (Mair and Katz 1997), or if the electorate has few other ways to register its views on the quality of governance, or lacks the capacity to organize itself effectively (Mungui-Ppidi 2003). Furthermore, institutional weaknesses (e.g., audit bodies, courts) may create an environment where horizontal and vertical accountability frequently fall short. To strengthen bottom-up accountability there must also be a set of mechanisms (systems, strategies, and institutions), formal and informal, that becomes the "way of doing" government. These mechanisms can be divided into several categories including information; consultation; oversight; and, community participation (See Table 1). The challenge in implementing these mechanisms for public sector accountability lies in creating an enabling political context where such mechanisms can be introduced and be sustained.

Table 1: Mechanisms for Advancing Public Sector Accountability

Accountability Mechanisms	Task	Method
Information	Provision of Information	Mandatory provision of information by the government (e.g., public hearings, annual reports, newsletters); citizen-led sources such as service delivery "scorecard" surveys.
	Financial Disclosure	Timely accounting and budget information (e.g., quarterly reports followed by audited financial reports).
	Financial Management Systems	Use of financial management information systems (which, for example, can provide citizens on-line access to key indicators of performance).
	Competitive Procurement	Local government procurement processes must be transparent, open, and, for larger projects, competitive.
Consultation / Oversight	Notice and Comment on Rule-making	Requirement that draft normative acts be published in public forums prior to their enactment.
	Public hearings	Public hearings may be required by law.
	Administrative Procedure Systems	Administrative procedures should require that citizens receive notice prior to any change in legislation or other action.
	Advisory Committees	Permanent or ad hoc bodies that provide input to government in various policy areas.
Active Participation	Right to Petition	The public has the right to propose the adoption, amendment or repeal of a normative act.
	Consensus/Negotiated Rulemaking	Councils that consult with groups must reach consensus with respect to policy initiatives.
Media—Right to Know	Non-governmentally controlled media (print and electronic)	Require government to inform the independent press of its activities, from procurement practices to budget reports.

Source: Russell-Einhorn (2004); Renikka and Svensson (2004); Authors.

4.2 Central and Local Government Reporting Relationship

A fundamental issue is that of the appropriate role of central government in promoting and ensuring the vertical accountability and the efficacy of local government financial reporting. This can be a tricky matter since the very manner that the issue is phrased as the "role of the central government" not only presumes a hierarchy among governments, but also that the central authority has the capacity and integrity to be in a position to monitor its subnational governments. The complement of fiscal decentralization is the need for regular, timely and comprehensive reporting from local governments to the central government's Ministry of Finance. This should be an accepted norm as the cornerstone of the accountability compact between central and subnational governments. It is entirely reasonable that the Ministry of Finance insist on it as a condition of fiscal decentralization.

Central governments have an important role in monitoring local government financial performance and reporting and collecting intergovernmental (including provincial and local) data. However, if the central government seizes upon this monitoring as a justification for interfering with what is a subnational/local competency then this tension represents a destructive rather than positive or "healthy" sign of robust intergovernmental relations. The central government's role can arguably extend beyond mere monitoring of local government's performance and collection of data if local governments are delivering services for which the central government has the primary

policy responsibility. This is a relatively common situation, in practice, in areas such as education, health and agriculture. Under these circumstances, local governments should be viewed as service delivery agencies responsible to the central government rather than autonomous bodies, and the need for interference or a stronger central government role should be re-evaluated. The accountability relationship under this circumstance is quite complex.

Clearly, the need for improved local government accountability must be balanced by the need for strong and effective control and reporting of fiscal aggregates. Seen from the Finance Minister's perspective, greater decentralization is a mixed blessing: while service delivery may be enhanced, fiscal control and local government financial reporting may be worsened, as spending, revenue collection and subnational borrowing powers are expanded. This is not an idle concern, since weaker aggregate control undermines macroeconomic performance and a country's development capacity.

5 Demand Side Pressures for Downward Accountability

Public accountability mechanisms are for safeguarding against misuse and abuse of budgetary resources; but they have their imperfections. Over the last decade, a number of social accountability mechanisms have emerged in response to the weaknesses of public financial accountability systems. These demand side tools that can be instrumental in identification of needs and preferences of citizens and preventing the misuse and misallocation of public resources including: making local government financial information (including budgets and end-of-year financial statements) accessible to the public; allowing strong public involvement in budgetary process through participatory budgeting practices; and initiating independent budget analysis and participatory public expenditure tracking programs that monitor budget execution and leakage of funds.[3] These new forms of accountability mechanisms, which enable direct engagement of citizens with government, emerge to complement public accountability mechanisms. However, public and social accountability approaches must be bridged to ensure that citizens have the ability and opportunity to demand accountability and local governments have the means and incentives to respond to citizen demands for accountability and better delivery of services (Yilmaz, Beris and Berthet 2008).

Institutions of local accountability in developing countries are often weak, with the attendant risk of 'capture' of public resources by local elite (Bardhan 2002). For example, when local government revenues are largely coming from taxpayers outside the local jurisdiction through intergovernmental grants, as is often the case in developing countries with geographic concentration of national resources and low revenue potential, there is a greater risk of capture because local citizens might not be informed about what resources are available to their local representatives for the delivery of public services (Khemani 2006).

In their empirical work designed to identify major drivers of corruption, Gurgur and Shah (2002) find that lack of service orientation in the public sector, weak democratic institutions, economic isolation (closed economy), a colonial past, internal bureaucratic controls and centralized decision-making are major causes of local

[3] A detailed discussion of these tools and their application see Yilmaz, Beris and Serrano-Berthet (2008).

corruption. They argue that, when well designed, accountable decentralization enhances public sector performance and reduces corruption. Suffice it to note here that in order to advance this outcome, multiple mechanisms of organizational and institutional capacity building may need to take root in order for local government accountability to prove effective (Blair 2000).

5.1 Local Government Must Show Leadership

The challenge of opening the budget process to public oversight and scrutiny are political. Even in a democratizing, and decentralizing, context many government officials continue to resist the notion that budgets should be shared with the public. Strengthening of the demand side budgetary process can only be accomplished in localities where the head of the local government is willing to show leadership on this issue. Resistance at lower levels of the bureaucracy will only give way in the face of an environment that is supportive of these efforts.

Opening up the budgetary process to sharing and discussing information may be as simple as just training local government councils on legal requirements and establishing systems to monitor budget and service delivery performance. In countries with weak accountability and high levels of corruption, where actual budget expenditures are at risk of being spent on non-budget items, budget monitoring is at least as useful an area for public involvement as budget planning.

A major issue in many developing countries is the scrutiny of recurrent budgets. As Ahmad and Weiser (2006: 40) point out although "[t]he development portion of the budget is well contested, scrutinized for inter-constituency comparisons, and debated upon," the recurrent portion of the budget in many countries receives very little attention. This means that most of the budgetary outlay is not analyzed and nor subject to debate. In Pakistan, for example, "tehsil" councils' share of salaries and other operating costs represent a significant portion of local government operational budgets. In 2006, the provincial government increased salaries to government employees by 30-40%, while only increasing budget transfers to local governments by only 10%. As a result, local governments scrambled to rearrange their budgets to accommodate the higher wage levels. Consequently, the level of development funds was significantly reduced, and funds were reallocated to cover the higher wage bill.

5.2 Improving Local Public Sector Accountability

Improving local public sector accountability requires a complex approach that recognizes the diverse factors underlying the persistence of weak governance. What are the lessons that can be drawn from the international experience? Actions to improve local governance, public financial management and accountability need to be taken on numerous fronts.

The linkage between central and local government should not be overlooked since it can have significant positive (or adverse) effects on the accountability of local governments to their citizens. What is the appropriate role of central government to ensure accountability of local governments? The role of the central government in ensuring local government accountability is to ensure that: local governments are provided with services in accordance with the assignment of powers and functions to

local governments; and all local government resources (including the funds that are transferred to the local government by the central government) should be utilized efficiently and in the manner intended. The two dimensions describing central and local governments inherently create some tension between the various levels of government. For example, in a decentralized environment, central governments devolve many expenditure assignments to local governments. Often, local governments (correctly) argue that many of these devolved expenditures are not fully funded. As a result, this leads to a lack of accountability by the local government. From the local government's public expenditure point of view, it is essential that when the central government devolves expenditure responsibilities, that they be fully funded. This would enhance local government accountability to local residents.

Unless the public knows what goods and services are provided, how well they are provided, who the beneficiaries are, and how much they cost, it cannot demand (nor expect) effective government. To promote government accountability, government budgets and expenditure programs need to be disclosed to the public. Governments that do not yet have laws or regulations allowing for public consultation and monitoring of budgets should consider enacting such legislation. Governments that have already created such a framework should be encouraged to ensure that other parts of the budget rules are consistent with public participation and may wish to consider issuing general guidelines to local governments highlight best practice in implementing public consultation.

Perhaps due to the urgency of delivering services and ensuring that budgets are passed in a timely manner, consultative activity during the budget cycle almost exclusively focuses on budget preparation only and enactment. Mechanisms to monitor the use of funds or evaluate the impact of programs have proven to be generally weak or non-existent. The monitoring of local government budgets can take the form of legislative or community-based committees. In countries with weak accountability systems in place and where actual budget expenditures are at risk of being spent on non-budget activities, budget monitoring is at least as useful an areas for community based involvement as budget planning.

5.3 Consultation and Participation at the Local Level

Over the last two decades, there has been a substantial body of anecdotal evidence about the positive impact of consultative and participatory mechanisms in improving local service delivery. Most development practitioners and academics see participatory mechanisms as a process that allows citizens to be involved in debating, deliberating and influencing the distribution of public resources (Shah 2007, Wagle and Shah 2003). Participatory mechanisms encompass a range of initiatives where ordinary citizens and residents have the opportunity to prioritize spending decisions, influence resource allocation and monitor public spending. These participatory mechanisms are increasingly seen as an important tool to promote good governance by ensuring that social policies and public spending are more equitable, strengthening transparency and accountability, giving greater voice to citizens, especially marginalized residents and the poor, and enhancing deliberative democracy.

In this context, participatory budgeting is seen a powerful good governance tool in the context of the growing trend of decentralization across the world (Zamboni 2007,

Reames and Lynott 2006, United Nations 2005). Three key impacts of participatory budgeting are that they spur administrative reform, promote social justice and social inclusion objectives by involving socially excluded groups and altering spending priorities towards more equitable and sustainable objectives, and enhance democratic citizenship (Shah 2007, Reames and Lynott 2006). Furthermore, Ackerman (2003) claims that participatory budgeting structures reduce corrupt behavior and the political use of public funds thereby limiting opportunities for state capture.

There are four inter-related arguments that explain the rise of public participation in decision-making: citizen participation is a logical shift from insulated modes of governance to more open and transparent mechanisms in the post-modern age; disillusionment with bureaucracy; the search for democratic ideal; and the need for participation in developing countries (Shah 2007). In general, frustrated with the continuous failure of the state in addressing citizen's needs in an equal and fair manner and in recognition of the perceived challenges faced by an introverted public administration and the inadequacies in the functioning of representative democracies, a demand for a re-examination of the existing governance arrangements, particularly that of the policy-making processes became imminent (United Nations 2005, Shah 2007).

Participatory budgeting emerged as part of a larger effort in Brazil to extend and deepen existing democracy (Abers 1996; Wampler 2000, Santos 1998). Scholars attribute the Porto Alegre experience to a range of enabling political and social factors that were unique to Brazil. The 1988 constitutional reform in Brazil strengthened the scope of decentralization and gave mayors the opportunity to innovate especially in areas of participatory planning and management. The significant increase in local revenues following the 1988 reforms and the availability of resources that the municipality could allocate at its own discretion was a key factor in prompting demands for greater accountability and participation in decisions regarding the use of funds. The growing influence of social movements such as Movimento Dos Sem Terra and left leaning parties in a number of municipalities also helped to create a platform for popular participation in local decision-making (Wampler 2000, Fung and Wright 2001).

Participatory budgeting mechanisms and processes vary across countries and contexts and there is no agreement on what participatory budgeting means or how to go about it. The specific definitions and methodologies associated with participatory budgeting usually derive from Brazilian experiences, and especially that of Porto Alegre. These definitions tend to emphasize a process that combines direct and representative democracy, involves deliberation (and not merely consultation), is redistributive towards the poor, and is self-regulating, such that participants help define the rules governing the process, including the criteria by which resources are allocated (Goldfrank 2006).

In the Brazilian context, participatory budgeting practice is based on a complex set of rules and involves a year-long cycle of meetings which allows communities to decide on the allocation of resources for capital investments in the annual municipal budget. In a series of neighborhood, regional, and citywide assemblies, residents and elected budget delegates identify spending priorities and vote on which priorities to implement. An important part of the process is the formation of the Participatory Budget Council whose delegates are elected each year. In other countries, participatory budgeting encompasses a broader set of practices and includes mechanisms that make

information about public budgets clearer and more accessible; efforts to increase participation in all stages of budgeting and not just allocation, and efforts to strengthen participation and capacity among socially excluded and under-represented groups such as women to influence the local budgeting process (Reames and Lynott 2006, Shah 2007).

Unlike the Brazilian experience, often, civil society organizations can take the lead in facilitating participation at the local level. Such an approach is exemplified by the Institute for Democracy in South Africa (IDASA), an NGO that combines advocacy, training, and research. IDASA specializes in budget analysis, providing detailed policy analyses of proposed resource allocation choices. In 1995, IDASA began analyzing the budget from the perspective of women (the Women's Budget) and children (the Children's Budget). In India, a citizen-initiated public advocacy exercises were effective in bringing citizens' concerns about spending priorities to the attention of local officials, office holders and representatives. DISHA – an NGO with a broad membership of indigenous people – created a simple way to demystify and monitor budget allocations (Shah 2007). Wagle and Shah (2003) argue that the work of DISHA substantially enhanced the quality of debate on the budget, both inside the state assembly and outside, serving as an effective channel of feedback to the government. Participatory processes in Europe and North America also vary considerably from the Porto Alegre example. Participatory practices vary based on the extent and depth of participation as well as the extent of budget subject to consultation. In recent pilots in New Castle and Bradford UK, consultations were held with neighborhoods to decide on how to spend small sums of extra money. Participatory tools are also beginning to be used in Canada. Guelph, a local municipal government, in Ontario is using participatory mechanisms to allocate a small portion of the City's budget. Through the Guelph Neighborhood Support Coalition, neighborhood groups share and redistribute resources for local community projects, such as recreation programs, youth services, and physical improvements to community facilities (Lerner and Wagner 2006).

Participatory budgeting practices have achieved mixed results. A review of the effectiveness of participatory budgeting indicates that substantial local interactions are required to ensure that funds are not diverted from expressed local community objectives. Studies on the impact of participatory budgeting in Brazil have found a trend towards spending more in less favored neighborhoods, inhabited by lower income families and improvements in governance (Abers, 1996 & 1998; Baiocchi, 2001; Avritzer, 2002, Zamboni 2007). In other studies, Baiocchi, Heller, Chaudhuri, and Silva (2005) find that adoption of participatory budgeting increases opportunity for citizen engagement and empowerment and has significant impact on reducing poverty and improving access to basic services; Schnieder and Baquero (2006) argue that in Porto Alegre tax revenues have also expanded significantly following the adoption of participatory budgeting; and Fisman and Gatti (1998) provide evidence about the positive impact of consultative and participatory mechanisms in improving local service delivery.

While participatory budgeting represents a promising approach for strengthening the demand side of governance, institutionalizing participatory processes can be challenging. A combination of four factors makes it more likely that participatory budgeting programs will be adopted: enabling legislation and strong political support, a vibrant civil society willing and able to contribute to ongoing policy debates, a generally

supportive political environment that insulates participatory budgeting from legislators' attacks and financial resources to fund the projects selected by citizens. Critics argue that participatory budgeting creates a conflict of legitimacy by exposing tensions between participatory democracy and representative democracy as has been the case in Porto Alegre where the legislature has lost some powers (Utzig 2007). A primary weakness of participatory budgeting is that it principally focuses on specific public works only and does not really engage citizens around discussions on broader social policies and long-term planning.

Given the mixed country experiences and paucity of research on impacts of participatory budgeting, it is difficult to generalize on either success or failure of participatory budgeting initiatives. We provide that while the mechanics of the participatory budgeting exercise may be different in South Africa and Chile than Malawai and Cambodia, there is a need to advance the participatory process in all countries. While participatory budgeting can be a tool for better governance and can work in favor of the poor, three key factors underpin its success. i) normative, citizen participation has to be given a legal basis; (ii) regulative, an operational framework of participation with clear definition of roles and functions including the methodology of participation must be mutually agreed upon and put in place; and finally, (iii) regenerative, participation practice warrants several capacity building interventions involving both the civil society as well as the government organizations (United Nations 2005).

6 The Future of Budget Reform

Cynicism about the manner in which governments finance their operations has provided a stimulus for various budget reforms. Constantly disappointed by their efforts, budget reformers reach back and try again. However, focusing budget reform efforts exclusively on the budget document and process alone may be aiming at the wrong target. Citizens have an enormous stake in how local government funds are being spent, but are not normally admitted to the key decision making bodies that establish spending priorities and certainly not to auditing processes of the public budget.

One thing that is clear, citizens are demanding more direct and meaningful engagement in accountability systems. Voting at election time is no longer sufficient. The result of these pent-up demands has been widespread experimentation with novel techniques demanding answers and enforcement sanctions. When it comes to scrutinizing public spending, the near impossibility of obtaining certified (audited) government accounts implies that most citizen efforts can go no further than (participatory) budget formulation at the local level, or else budget analysis at high levels of aggregation, identifying the likely impact of proposed public spending on categories such as the poor.

Clarity of local government budgeting formats significantly impacts whether civil society can evaluate and monitor local government expenditures. Oftentimes, this is particularly true when monitoring the current (operational or administrative) expenditure portion of the budget, which receives almost no review by the public or local government legislative (council) branch. Efforts to introduce performance (program) budgeting are useful in allowing the general public to examine costs in detail and to connect expenditures to expected outcomes. However, local governments are often confronted

with human resource (ability) constraints in implementing this type of budgeting and the underlying accounting systems.

Efforts to strengthen budgetary process are most likely to meet with success in developing countries and in localities that have some underlying (effective) legal and regulatory framework that is supportive of public involvement in governance processes. National, and local, governments that do not have effective laws and regulations allowing for public consultation and monitoring of budgets should consider enacting such legislation. Governments that have already created such a framework should be further encouraged to ensure that other parts of the budget rules and consistent with public participation process. These governments may also wish to consider issuing rules and guidelines for ensuring more effective public consultation in the budgeting development, oversight and monitoring process.

Demand side measures for financial accountability include publicly accessible local government financial information (including budgets and end-of-year financial statements); public involvement in budgetary process through participatory budgeting practices; gender-sensitive planning, budgeting, and resource allocation, reinforced by gender audits; independent budget analysis and participatory public expenditure tracking programs that monitor budget execution and leakage of funds.

Only when citizens attain not only effective involvement in the budget formulation process but in the expenditure management side via more direct auditing, more direct expenditure analysis and control, of financial systems will full public sector budget accountability be achieved. Community (demand-side) participation is necessary, but not an adequate condition, for enabling greater local government accountability. Community based schemes for enhancing local government accountability generally need to combine legal, political, and administrative mechanisms (more effective budgeting, public oversight of local government expenditures, enforcement) with proactive community involvement.

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