

**Central America and the Caribbean:  
15 Years of Decentralisation?**

**Some Reflections on Development Cooperation**

Paper presented by

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**Decentralisation and social cohesion: lessons learnt**

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### PRELIMINARY NOTE:

This paper refers to Central America and the Caribbean as the Latin American regions most familiar to the author. Many of the author's reflection can be extrapolated to the rest of Latin America, with the possible exception of Brazil, which has a local authority system that is much more solid and structured.

### INTRODUCTION

#### ***Decentralisation or pro-activity?***

Decentralisation can be understood as the application of the principle of subsidiarity in the distribution of tasks between governmental bodies, with the maximum amount of power and responsibility transferred to governing bodies that are close to the people. Local government bodies, or municipalities, are the main beneficiaries of decentralisation in Central America. This has undoubtedly favoured human progress and, in turn, social cohesion.

In considering the classical model of the state and traditional methods for making public services available to the people, decentralisation implies a transfer of assets (infrastructures, etc.), human resources, financial resources, and political

responsibilities to the lowest possible level and in a way that does not affect efficacy and efficiency in the provision of a service. This model, nonetheless, although it may still be valid in certain fields, functions poorly in the world in which we live today, dominated as it is by interdependencies.

We operate, whether we like it or not, under the umbrella of governance, in which decisions that affect society in general cannot be taken unilaterally by a single player, for all that she/he is legitimised by votes. In this respect we are of the opinion that the term 'decentralisation' (not to mention associated concepts) is somewhat antiquated, loaded as it is with reminders of the bureaucratic state making an effort to adapt itself to a new model of public management. The term brings to mind the listing of powers that are exclusive and powers that are shared, debated, moreover, within a scenario of fairly predictable stability. What we are faced with, perhaps, is more than mere decentralisation, but rather a new culture for operating on the basis of networks that rely on the initiatives of the players - in short, pro-activity.

#### THE CENTRAL AMERICAN AND CARIBBEAN CASE

Much has been said in the last fifteen year in the CAC region and in the whole of Latin America in regard to the need for decentralisation and for designating the municipality as the main beneficiary of transferred powers. This need was first diagnosed by international cooperation bodies at the end of the 1980s, and has, since then, been advocated strongly. The notion, which seemed entirely rational, was generally and widely accepted. Another matter was reality. If we examine what has happened in recent years, we can conclude that decentralisation has advanced very little. There is a widespread perception that there has been much discussion on the subject, yet little actually done.

What follows are some reflections on how to account for this failure of decentralisation.

## **1.- There are no political incentives for decentralisation, and international cooperation, in fact, does not generally encourage such incentives**

Nobody denies that the Central American region includes some of the weakest nation states in Latin America. Similarly acknowledged is the fact that the governing elite has a strong authoritarian tradition, which goes hand in glove with a culture that is still very much governed by the servility that marks the practices of most of the political parties. Embarking on political initiatives in Central America is a risk that few are willing to assume.

If to this cultural and historical heritage we add the fact that globalisation is eroding the sovereignty and powers of these weak central governments, then it seems somewhat illusory to expect disinterested decentralisation in favour of municipalities that are held in low esteem and considered to be technically inept.

We have used the word 'disinterested' somewhat frivolously perhaps, but if we carefully analyse the reality, the fact is that there are few mayors or municipal associations that demand a true decentralisation of powers. The lack of a local government tradition and the low prestige in which the municipality is held in the CAC region mean that mayors who stand out politically soon aspire to being a deputy or minister. Consequently, their thinking processes rapidly adopt the positions of centralised power. The fact is that although mayors – like everyone – demand more resources, the demands for new powers and greater responsibility are few and far between.

Successful mayors are not the mayors who are better organisers, or who raise more taxes to implement measures in favour of the collectives they organise, but those who are successful in obtaining external resources for their municipality. This poor principle of action holds true - historically and for all the regions in question - despite the fact that as a principle it leads to dependency rather than local development. But it is also true that there are circumstances in which, in order to obtain external resources, some evidence has to be provided of having improved community organisation and developed tax collection capacities.

So, what is the background against which the Central American mayor operates today? Previously, when mayors had exhausted their possibilities of raising resources locally and needed to go beyond the municipality to obtain resources externally, they had only one option – the higher levels of government. They thus had to pay homage to central government, since in a poorly institutionalised state, there were no impartial mechanisms for the territorial sharing out of resources.

Nowadays, mayors have a new source for obtaining resources - international cooperation - whether in the form of official bilateral agreements between

countries or – for the smaller municipalities – of decentralised cooperation and NGOs. One of the best investments that mayors - or the increasing numbers of mayoresses - can make nowadays is to take a plane and do the rounds of Europe (or even the USA) to look for cooperation aid and/or solidarity agreements. I ask myself, however, whether we are not encouraging the ‘begging’ mayor; whether this is the way to move towards the decentralisation that has been advocated by international cooperation; whether this system of international relations is not in some way (even involuntarily) perverted.

We are undoubtedly living through a period of governance and of interdependence between players. And for the municipalities of Central America, a new player has emerged, who, as a consequence of its comparatively greater financial resources, is a crucially important player: international cooperation. Donors of development aid, local governments in the northern hemisphere, NGOs, etc. render account (often very little account) to their citizens or members, but assume no responsibility for the communities benefiting from their aid, and even less for the longer term impacts of this aid.

We are of the opinion that the donor culture needs to attain a degree of maturity and that a debate should be initiated in relation to the **local and political counterbalance** of cooperation. What of the Spanish local council which has undertaken to support its twin town in Nicaragua in proportion to the taxes it collects. Does this music sound sweet to the ears? Is this the road to development?

## **2.- The municipal financing model does not provide an incentive for local tax collection.**

It is widely acknowledged that a particular financing model greatly affects the life of an institution. In Central America and the Dominican Republic in general, municipalities unfortunately apply a structurally precarious financing model that fails to provide any incentives for local tax collection.

As a general rule, it can be said that municipal taxation systems in the CAC region are antiquated, with an excessive number of taxation types, a high tax collection cost, and relatively low returns. They are featured, moreover, by precarious tax administration systems (incomplete taxation registers and databases) and by an inadequate technical and legal capacity to enforce payment. But the major problem possibly lies in the fact that the most recently developed source of funds, i.e. the *situado municipal* (a specific proportion of taxes earmarked for municipalities), the programmes for combating poverty and the social investment funds, act as disincentives to local tax collection.

An important, fair, and necessary component of municipal financing is the transfer of funds from central to local government. In 1990, only Guatemala had a legally established *situado municipal* that obliges central government to transfer to the municipalities, on the basis of a clearly specified allocation formula, a percentage of national taxation revenues. The situation has greatly improved in recent years in that almost all the countries in the region have managed to negotiate important funds transfers from central to local government.<sup>1</sup> Pressures exercised by international cooperation bodies have played an important role in this positive turn of events.

Nonetheless, a perverse consequence of the *situado municipal* has been that this form of funding appears to have augmented, in the municipalities, what we could denominate 'fiscal laziness'. The evidence would indicate that the easier routes to raising finance are chosen; moreover, a substitution of revenue sources has occurred, with local tax collection showing a clear tendency to fall in the entire region.

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<sup>1</sup> Since 1987, Guatemala has allocated a *situado* of 8% of national tax revenues. Honduras, despite an objective of 5% since 1991, currently allocates around 3.5% to the *situado*. El Salvador has had a fixed annual amount allocated to municipalities, which since 1997 has gradually increased to around the current 6% level. The Dominican Republic also initiated a process in 1997 for gradually increased transfers, which currently represent 6% of national tax revenues. Since 2003, Nicaragua has had a *situado* of 4% and foresees an annual increase of 0.5% until the 10% *situado* that has been legislated for is achieved. Costa Rica has also approved legislation to gradually reach a *situado* level of 10%, although as yet, no steps have been taken to implement the law.

It would be a relatively easy matter to selectively stimulate local tax collection by means of an adjustment to the allocation formulae applied to central government funds transfers, e.g. for a municipality that had failed to raise a minimum sum in its own territory not to benefit from transfers in the same way as a municipality that had complied with minimum revenue raising criteria. The best formula is clearly one which would earmark a percentage of the central fund for municipalities on the basis of evidence of an annual increase in the collection of certain taxes, especially those related to property (widely accepted as the tax that is most genuinely municipal)<sup>2</sup>.

An even more perverse distortion occurs in relation to the poverty reduction programmes or social investment funds, when distributed on the basis of statistical indicators of poverty or need. The logical outcome is that the municipality that manages to improve these statistics is punished with lower funding in the subsequent financial period. Although it cannot be said that these indicators are interfered with, it is, nevertheless, widely acknowledged that statistical devices are used to ensure that they do not improve. Once again mayoral skills are stimulated - not in the sense of a better organisation of their territory and community, but in achieving official indicator levels that ensure more funds.

This trend towards minimising taxation responsibility implies a serious loss of municipal political responsibility and an important erosion of endogenous development capacities.

It is a poor precedent for democracy that a politician can present him/herself for election with a programme to be financed by another governmental body or by international cooperation aid and based on relatively little effort at the local level. This is a clear example of an affront against the political responsibility of elected representatives, and over the long term, an erosion of their authority. Fiscal responsibility is the framework for political responsibility and so should form the basis for the recovery of the prestige of mayors and of local politics.

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<sup>2</sup> *In comparison with the industrialised economies, Latin American and Caribbean countries rely more on consumption taxes than on income or property taxes to finance public spending. In the OECD countries, 75% of taxation revenues come from income and property taxes, whereas in Latin American and Caribbean countries, the equivalent proportion is 41%. Source: Construyendo la cohesión social en América Latina y el Caribe [Constructing social cohesión in Latin America and the Caribbean] by César P. Bouillon, Mayra Buvinic, and Carlos M. Jarque. Inter-American Development Bank, May 2004.*

## GENERAL REFLECTIONS

True decentralisation requires local government to be empowered, yet this endangers the position of members of the dominant central elite, a fact of which they are well aware. Take the Bolivian case, for example. Commencing in 1994, Bolivia has undergone a profound and genuine decentralisation process, resulting in a real empowerment of the people and an emancipation of many local authorities, with obvious benefits for the local populations. Nonetheless, the emergence of these new strategic players (mostly, although not exclusively indigenous peoples) in Bolivia's political arena is causing severe headaches for the ruling elites and the traditional parties, as has become evident since the last parliamentary elections. A similar analysis can be applied to El Salvador, which is the country in the CAC region that has undergone the greatest degree of decentralisation. Following its terrible civil war and commencing with the peace agreements, a new strategic player emerged onto the political stage, one that has carved out a political niche in the municipalities.

Faced with the prospect of having to share power with new players, the simplest reaction on the part of central governments is, under the seductive banner of decentralisation, to legislate powers to the municipalities. This is done, however, without making any provision for the allocation of human, material, or infrastructural resources to the municipalities. In colloquial language this is called 'passing the hot potato'. There is no need to dwell on the well-known fact of the confusion that is deliberately fostered when simple privatisation operations are classified as decentralisation. These operations, when carried through correctly may be extremely useful and valuable, but they have little to do with decentralisation. It is in this sense that we emphasise that there is an undoubted banalisation, even perversion of the notion of decentralisation, and ultimately, of associated concepts.

In conclusion, decentralisation is undoubtedly necessary in the CAC region and the current processes presently being debated should continue to receive support. That said, in the face of scenarios that are so lacking in promise, in the face of fifteen long years fostering the notion from multi-lateral platforms, and in the face of the degradation of the concept, it seems advisable not to use decentralisation as a banner for cooperation in strengthening institutions. On the contrary, we are of the opinion that it would be more useful to prioritise municipal projects and programmes that have as their basic aim local endogenous development (including employment generation), and fostered by pro-active attitudes on the part of municipalities converted into the leaders and representatives of their own network of local players. We believe that the best approach towards creating scenarios that are favourable to decentralisation is to sow the seeds of a culture of political initiative and risk among municipalities.

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**Central American and Caribbean spending in 2000**

Country	Population in 2000 (millions)	GDP/cap. in \$US	Central Govt. Expenditure (% GDP)	Municipal Expenditure (% GDP)	Central/Municipal Ratio	Municipal Expenditure /cap. ( \$US)
Guatemala	11.385	1,641	13.0	1.21	11/1	20
El Salvador	6.276	2,115	14.2	1.32	11/1	28
Honduras	6.485	914	23.9	1.53	16/1	14
Nicaragua	5.074	480	38.5	3.56 (*)	11/1	17
Costa Rica	4.023	4,062	15.9	1.01	16/1	41
Panama	2.856	3,396	-	0.69	N/A	23
Dominican Rep.	8.495	2,347	-	1.0	N/A	23
<b>CAC REGION</b>	<b>44.604</b>					

Note: We are of the opinion that the figures for Nicaragua may be distorted on account of international cooperation revenues.

Sources: Perazzo, A. Sistemas de Ingresos Municipales en Centroamérica. Una síntesis Comparativa [Municipal Revenue Systems in Central America. A Comparative Summary]. AECL, 2000

CELADE, Chile, 2000, Population Division, Demographic Bulletin No. 66, July 2000.

UN Statistics Division – National Accounts Main Aggregates (2000)