



DECENTRALISATION &
LOCAL GOVERNANCE



External Support for Decentralization Reforms & Local Governance Systems in the Asia Pacific: Better Performance, Higher Impact?

EQUALIZATION IN THE INTERGOVERNMENTAL TRANSFER SYSTEM

ROY BAHL

Regents Professor of Economics, Emeritus

Georgia State University

September, 2015

Manila

THE EQUALIZATION GOAL (IN THEORY)

- To guarantee every jurisdiction enough resource base to provide a minimum level of services.
- Central government will fill the gap between (a) the minimum level of public services and (b) the revenue the local government can raise at a “normal” level of effort.
- Minimum service levels are best measured on a sector by sector basis

EQUALIZATION FORMULA

- $ME = NR + IT$

Where

ME is the cost of minimum service level

NR is revenue potential at normal effort

IT is transfer needed to fill the gap

PER CAPITA GRANTS UNDER AN EQUALIZATION SYSTEM: SHORTCUTS

- More to places with greater expenditure needs
 - Population
 - Land area
 - Poverty
- More per capita grants to places with less revenue capacity
 - Per capita GDP
 - More urbanized
- What about management capacity, Infrastructure, etc.?

HOW TO DO EQUALIZATION

- The Guaranteed Service Level Approach (former Soviet states)
- The Formula Approach (Indonesia, Philippines, Pakistan)
- The Expert Judgement Approach (India)
- Assign Responsibility to Provinces (India, China)

HOW NOT TO DO EQUALIZATION

- Fund the year end fiscal deficit
- Allocate grants based on actual expenditures or revenues

EXPERIENCES IN ASIA

Country	Comment
CHINA	Derivation transfers give more to rich places; conditional and unconditional grants are equalizing
INDONESIA	Weak equalization based on formula and tax sharing system
PHILIPPINES	Little equalization based on the formula system
INDIA	Some components of the grant system are quite equalizing (the “schemes”), others are not
VIET NAM	Some degree of equalization
CAMBODIA	Provincial system gives more to places with less poverty; Commune and District systems are weakly equalizing

WHY EQUALIZATION SYSTEMS CAN FAIL

- Political Clout of Losers
- Poor Places have weak service delivery
- Goal of grant system is not equalization
- Central Government does not know how to do it
- Success in some sectors but not others
- Central Government does not monitor

POLICY ADVICE

- Develop an equalization strategy
- Define Targets for reduced disparities
- Develop tests and review annually

