THE IMPACT OF ELECTORAL DYNAMICS ON MUNICIPAL FISCAL MANAGEMENT IN NEPAL

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Declaration

I, Bibek Pokharel, hereby declare that this thesis entitled **THE IMPACT OF ELECTORAL DYNAMICS ON MUNICIPAL FISCAL MANAGEMENT IN NEPAL** submitted to the Central Department of Economics, Tribhuvan University, is my work prepared under the supervision of my supervisor, Dr. Resham Bahadur Thapa-Parajuli. I also certify that the thesis has been authored by me and helps that I have received in the research work and the preparation of this thesis have been acknowledged properly. Moreover, I attest that all information sources and literature used are indicated in the reference section and that no part of this thesis has either been submitted or accepted for any other degree at this or any other university or institution .

I will be solely responsible if any evidence is found against my declaration.

Bibek Pokharel
September 25, 2024

Letter of Recommendation

This thesis entitled **THE IMPACT OF ELECTORAL DYNAMICS ON MUNICIPAL FISCAL MANAGEMENT IN NEPAL** has been prepared by Mr. Bibek Pokharel under my supervision. I hereby recommend this thesis for examination by the Thesis Committee as a partial fulfillment of the requirements for the Degree of **Master of Arts** in **Economics**.

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Approval Sheet

We certify that the thesis entitled **THE IMPACT OF ELECTORAL DYNAMICS ON MUNICIPAL FISCAL MANAGEMENT IN NEPAL** submitted by **Mr.Bibek Pokharel** to the Central Department of Economics, Faculty of Humanities and Social Sciences, Tribhuvan University, Nepal in partial fulfillment of the requirements for the Degree of **MASTER OF ARTS** in **ECONOMICS** has been found satisfactory in scope and quality. Therefore, we accept this thesis as a part of the said degree.

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.

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Kathmandu, Nepal
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List of Abbreviations

AG	Auditor General
CBS	Central Bureau of Statistics
COVID-19	CoronaVirus Disease 2019
DiD	Difference-in-Differences
FGT	First Generation Theory
GDP	Gross Domestic Product
HHI	Herfindahl-Hirschman Index
LISA	Local Government Institutional Capacity Self-Assessment
NNRFC	National Natural Resources and Financial Commission
OECD	Organization for Economic Cooperation and Development
OLG	Overlapping Generation
OLS	Ordinary Least Square
SGT	Second Generation Theory
VDC	Village Development Committee
WB	The World Bank

Abstract

This study examines the relationship between the electoral behavior and the fiscal and economic discipline of the local governments of Nepal. The study has collected the electoral data from the local level election held in 2017 , the yearly data on fiscal and economic variables from 2017 to 2021, and the data on the performance of the local governments through LISA program. Descriptive and explanatory analyses are used to examine the state and relationship among the variables of interest. Pooled regressions has been carried out to investigate how the electoral dynamics affects the performance variables of the local governments, and panel regression later investigates how those performance variables translate to the fiscal management.

The findings reveal that electoral competition, as measured by HHI, has highly significant association with the performance scores of the local governments. Also, these performance scores of the local governments impacts the fiscal management, as measured through several key fiscal variables. The study concludes with the recommendations for strengthening electoral competition, increasing the education level, and proper monitoring and evaluations of the local level governments of Nepal.

Keywords: Local-level governments, fiscal federalism, elections, accountability

Chapter I: INTRODUCTION

1.1 Background of the Study

Representative governments, be in parliamentary or presidential system of representation, are accountable to the public welfare of the citizens. Autocratic and dictatorial regimes also heed the needs of people even though there is no direct accountability(Gilli & Yuan, 2014) through elections or other measures. The economic blueprint of a nation is largely shaped by the political and institutional factors, which are reflected in the fiscal performance at the national and subnational level(Rattsø, 1998; Dafflon, 2002). Subnational government could take various forms, some having only deconcentrated and delegated power while others possessing decentralized structure where powers, specifically economic, political, and fiscal powers are factually devolved to the subnational levels. It should be noted that decentralization, inherently, is neither good nor bad for efficiency, equity, or macroeconomic stability, rather its effects depends on institutional specific design and how building block of fiscal federalism namely, expenditure and revenue assignments, intergovernmental transfer, and subnational borrowing processes, are designed(Alt & Lowry, 1994).

Since subnational government play a crucial role in the overall economic development of nations, several studies have examined subnational government efficiency and its major determinants(De Borger, Kerstens, & Moesen, 1994; Worthington, 2000; Geys, 2006; Bruns & Himmler, 2008). Subnational government are designed to be closer to people and has the motive to increase public welfare, thus it is hard to develop a performance metrics to objectively measure and judge them(Gray & Jenkins, 2006). However, economic literature provides several methods through which it could be reasonably done and fiscal performance is one of such chief metrics. Different countries have different reasons to decentralize or devolve real powers, and procrustean model of power sharing, without regard to the reasons for the creation of federal structure, are destined to fail. Diversity in geography, economic status, language, and natural and human resources meant that different regions of Nepal had varying levels of needs and types of government services. The desire of people, the electorate, to better access and be involved in the governing mechanism, along with bevy of other factors, drove out the largely-autocratic and centralized rule of monarchial system and instituted Nepal as a Federal Republic.

The constitution of Nepal, formally promulgated in 2015, mandated Nepal to have a federal republic system of governance. Under this system, Nepal is administratively divided into 753 local levels, 7 provinces, and a unitary central government. The constitution also delineated the jurisdiction of each of these three levels of government, from the revenue and expenditure assignments of each levels to the inter-relationship among them. The vestige of old administrative system before the initiation of federalism still remains; explicitly in some cases, with the 77 district still holding considerable authority; or implicitly in other cases , with the new local level and province level boundary closely resembling the old Municipalities(or V.D.Cs.) and the development regions respectively. The installation of federalist structure, with considerable power devolved from the central to especially the local level governments could be thought of as another effort to development in the changed political and socio-economic context of Nepal. Federalism with a proper decentralization of power is assumed to be helpful not only for economic growth of the local levels(Iimi, 2005; Hadi, 2019; Carniti, Cerniglia, Longaretti, & Michelangeli, 2019), but could also aid in reducing inequality in development across federal regions(Baskaran, Feld, & Schnellenbach, 2016). Beyond economic growth, Federalism, with sufficient fiscal and economic authority decentralized with proper accountability mechanism, can help improve the democratic system of governance and can also assist in removing several impediments to development(Weingast, 2014).

However, federalism is not a universal panacea for economic growth and development. Federalism, as a doctrine of governance, does not have a standardized format and differs in the way it is implemented across countries and across time. Moreover, there are countries, like the USA, that were initially formed with a federal structure(Sargent, 2012), whereas others, such as Nepal, adopted federalism long after their formation. Additionally, federal system across nations were generally instituted more on the rational of political considerations rather than of economic welfare(Riker, 1964). Thus, Federalism should be considered from multiple perspectives with economics as a key aspect, but not the only one. Furthermore, federalism can be ill-suited when dealing with economic as well as other crises and long-run stability(Huberfeld, Gordon, & Jones, 2020). Peterson (1995) in his seminal work, *The Price of Federalism*, argues that for federalism to work, its functional and legislative perspective must be smooth and in tandem, and any discrepancies between these two perspectives would render federalism unsuitable as the governance mechanism.

Against such backdrop, Nepal instituted federalism through the constitution, with political, fiscal, economic, and other powers devolved and decentralized from the central unitary government to province and local-level governments[1]. While

[1] The brief overview on the number of federal structures is shown in Table 1

all local level governments wield considerable administrative power, not all local levels were created equal. These inequalities are reflected not only in demographic and geographic aspects, but also in the level of development as well as in the revenue and expenditure mobilization aspects of the local levels. In demographic aspect, Narpa Bhumi in Manang harbors the population of 538, while Kathmandu metropolitan city houses 862,400 people. Similarly, Bhaktapur municipality is the smallest local level with area of 6.56 sq.km. while Namkha rural-municipality in Humla district is largest with the area of 2419.64 sq.km..

Province	Numbers of Local Levels		
	Rural − Municipalities	*Municipalities*	*Sub − Metros&Metropolitans*
Koshi	88	46	3
Madhesh	59	73	4
Bagmati	74	41	4
Gandaki	58	26	1
Lumbini	73	32	4
Karnali	54	25	0
Sudurpaschim	54	33	1
Total	460	276	17

Table 1.1: Province-wise local levels classification

The advantages of federalism, namely, aiding in economic growth, reducing inequality, and strengthening democratic system of governance stem primarily because of the federal units having better understanding of and being more responsible to the demands of its denizens. Since 1980s, power devolved structure of governance, like federalism, has emerged as a valued political and economic goal in most developing countries, with advocates of such devolution justifying it on grounds of increased efficiency, more thoroughgoing equity, and for greater participation and responsiveness of government to citizens(Agrawal & Ribot, 2000). North (1981) explains how the state, an entity with comparative advantage in violence, realized its constraints as it grew in geography and population, and instituted the *bailiff* system, a historical precursor of the modern federal system. In the bailiff system, in which the sub-state units, by design were closer and more responsible to their denizens, a central ruler would install local rulers who were permitted to have their own bureaucracy, but still exerting stringent monitoring and controls over their actions.

The modern day federalism retains many characteristics of the bailiff system, although the desideratum motive in federalism is not the constraints on the central state's capacity but the democratic ideals of proper representations and responsibilities in governance. Devolving powers to subnational units creates the realm of decision making where those subnational units, or federal units, can exercise some autonomy while addressing the needs of the local populace. In democracy, voices of all denizens must be heard and sometimes it could result in ‘tyranny of majority’ where the voices and opinions of the minority group are not addressed properly. Federalist structure of governance addresses this issue as federal units, being smaller than the national government and being closer to the people, could represent the interest of people better. It is particularly useful when there exists uneven state of development within the nation, as federal units could tailor the policies to properly address the exact needs of the people. This view of federalist structure tailoring policies to better address the needs of the local region was succinctly summarized by Justice Brandeis, as :“It is one of the happy incidents of the federal system that a single courageous state may, if its citizen choose, serve as a laboratory, and try moral, social, and economic experiments without risk to rest of the country"(Rosen, 2016).

Federal units, being closer to the denizens and thus, more knowledgable to properly tailor policies for better addressing the local needs, benefit other units and nations as a whole as it would create stronger links of political accountability among local governments, the central government, the public sector, and the community(Eckardt, 2008). Agrawal and Ribot (2000) points out that along with representation, accountability is critical if devolved powers are to serve local needs efficiently and equitably. Thus, in federalism, the subnational units are important not just because they represent local people and their demands, but also because they are accountable to the local people. In Eckardt’s model of decentralization, there exists three distinct dimensions underlining all acts of decentralization, namely, actors. powers, and accountability. For federalism to attain its political and economic goals, there needs to be an understanding of the powers of various actors, the domains in which they exercise their powers, and to whom and how are the actors accountable. In democratic nations, such actors are mostly held downwardly accountable to local/federal constituencies, mainly through the electoral processes. Blair (2000) states how democratic local governance works primarily through participation and accountability. Participation, in this context, means giving meaningful role to citizens on decision that affects them, while accountability aspect is twin-fold, with bureaucrats accountable to elected officials and elected officials accountable to the local public. Such accountability is carried out through the working of four mediums, namely, elections, political parties, civil society, and media. Przeworski, Stokes, and Manin (1999) states that since the establishment of representative institutions, be it at national or subnational level, their basic structure has largely been;

i. Rulers who govern are selected through the electoral processes.

ii. Citizens, who vote and can urge rulers to follow a set of mandates but can't give legally binding instruction during the rulers' tenure.

iii. Rulers are held accountable through periodic elections where citizens vote.

Economic and public choice literatures assume that voters involvement, which can be measured through electoral participation enhance accountability and discourage rent seeking as well as shirking behavior, thereby increasing efficiency and other aspect of governance(Stigler, 1972; Barro, 1973).

Thus, election acts as the accountability mechanism that connects citizens with their representative. The primary motive through which election fulfills its role in making leaders accountable is through the anticipation of not being re-elected in the future leads the leaders not to shirk their obligations to voters in the present(Barro, 1973; Ferejohn, 1986; Manin, 1997). Fearon (1999) describes two principal mechanism by which elections might bring about public policies that voters desire - sanctioning and selection, Sanctioning mechanism works as elected officials are motivated to choose policies that most of the voters desire so as to get reelected, and selection mechanism work as voters usually have the options to select other opposition candidates who they could be better and less likely to shirk from their responsibilities.Besley and Burgess (2002) finds that in India, state governments are more responsible to local needs, especially in public service distribution during the time of emergencies, calamities, and disasters , where electoral accountability is greater.

Periodic election is the sin-qua-non feature of democracy. Elections provide mandates to the elected officials and give the people their say on organization of all aspect of the nation. One of the core feature of the modern day federalism is selections of federal legislatures and executives by the denizens of the federal units through periodic elections. As fiscal and economic power devolution are usually carried out, the elected leaders of the federal units are accountable to the public for the fiscal and economic health of the federal units. Through sanctioning and selecting mechanisms, the incumbent elected officials are motivated to improve the fiscal and economic indicators. Much of the research and literature on fiscal federalism reflects the traditional public finance approach to the issue(Galligan & Walsh, 1990), which was driven by the Musgravian principles of efficiency, equity , and stability(Musgrave, 1983). Even in the Musgravian approach to fiscal federalism, periodic elections for the rulers is the critical component of the well-designed power devolution system.

Accountability mechanism functions as a map from outcomes of actions of public officials to sanctions by citizens. Elections are a “Contingent renewal" of accountability mechanism, where sanctions are to extend or not to extend the governments' or incumbents' tenure(Przeworski et al., 1999). However, bridging accountability aspects of leaders towards fiscal and economic responsibilities with electoral motivations is not straightforward. One of the critical methodological roadblocks in conducting research of fiscal and economic performance is that no exact or well agreed performance metrics of public sector exists(Estrella López, 2003; Andrews & Shah, 2003; Uphoff, 2005). In private sectors, the economic roles and objectives are usually clearly outlined, making performance measurement and inference easier. Compounding the problem of accountability aspect is the informational aspects, especially as there exists informational asymmetry between elected officials and the voters. For example, elected officials might be more tempted by long run capital investment projects which are ultimately beneficial to the public but it incurs costs in the long run, thus, it creates a healthy fiscal result in the long run but public might be dismayed by the short term fiscal and economic costs. Additionally, when the incumbent expects that he or she will not be reelected, then it could result in the incumbent choosing not to be accountable and to extract high rents, breaking down the voters control completely(Ferejohn, 1986; Banks & Sundaram, 1998).

After the promulgation of the constitution, Nepal conducted its first election in a newly delineated local level in 2017 in three distinct phases. The differences in local levels was reflected in the voting turnout as well as in the electoral competition, as seen in Figure 1 and Figure 2 respectively. The initial differences in local level entities have other implications too, as more populated local level getting more funds from the central and provincial government as the population is one of the key factor in grants consideration[2]. Most importantly, after the promulgation of the constitution and two local-level election cycles concluded, some local levels have achieved considerable improvement in development while some have lagged behind[3]. The difference between fiscal performances of local levels could have several determinants, including, structural and political characteristics(De Borger et al., 1994), neighbor local government effects(Geys, 2006), and voters involvement(Geys, Heinemann, & Kalb, 2010). Nepal's foray in federal system with proper power devolution provides an excellent opportunity to investigate the prime determinants of fiscal and economic discipline of local level units. While there exists seven provinces, acting as the intermediate governance mechanism between local levels and the central government, local level

[2]NNFRC Fiscal Equalization Grant to local level criteria includes formula-based, minimum, and performance-based grants, all influenced by total and dependent population size.

[3]NNFRC annual reports as well as available provincial reports from Provincial Planning Commissions

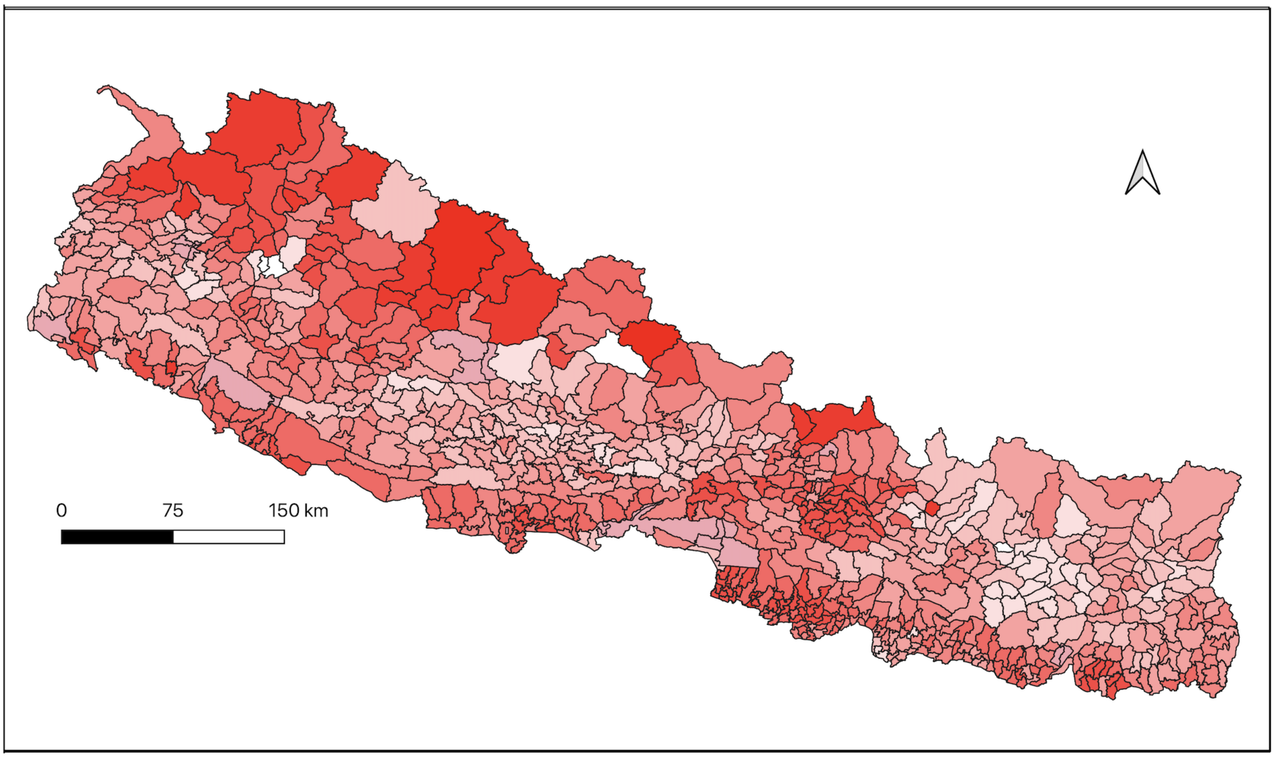

Figure 1: Heatmap of Voting Turnout at local levels

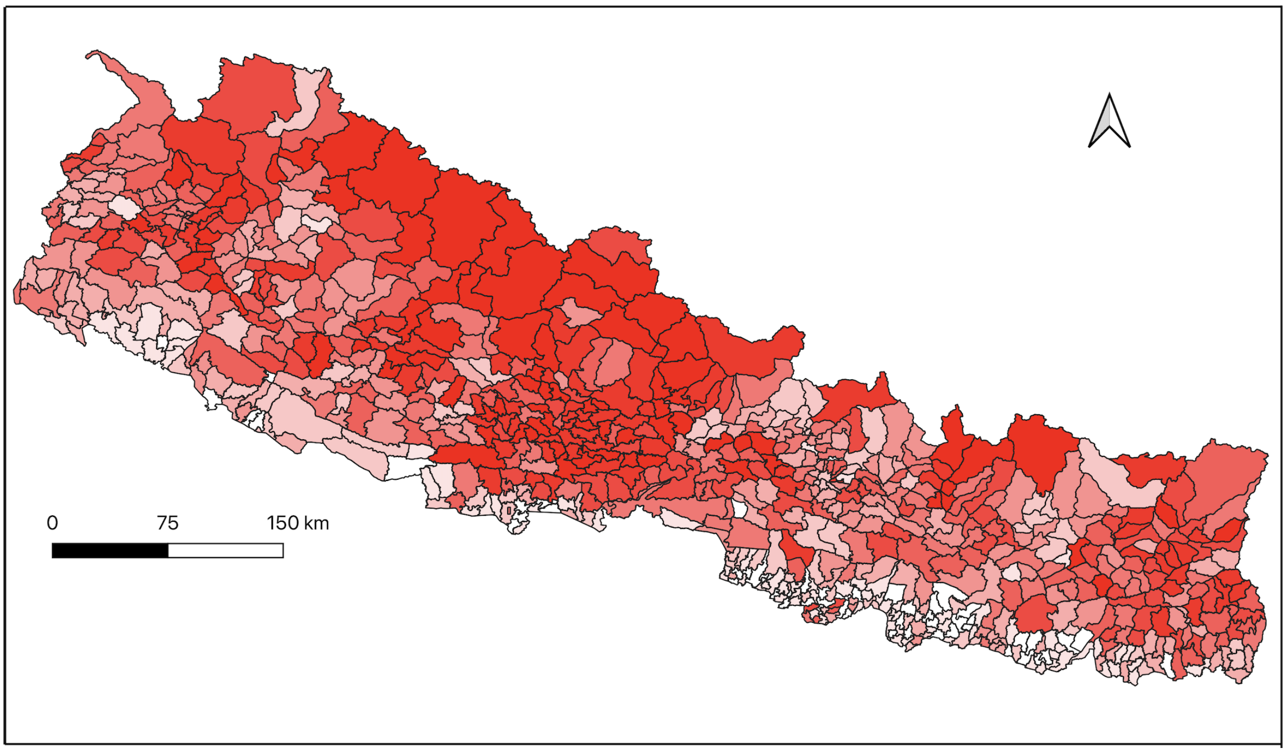

Figure 2: Heatmap of Herfindahl-Hirschman Index

governments are closer to people and provides a better avenue to compare the performances across nation. Thus, the fiscal and economic performances of local level jurisdictions are measured and their determinants are examined here instead of provincial level government.

1.2 Statement of the Problems

In federal structure, local level governments are designed to be the closest accessible government to the general public. With the considerable administrative power wielded by the local governments of Nepal, their role is paramount in increasing the living standards of the denizens of the local levels. However, some jurisdictions have been able to provide the required services and perform their duties so as to increase the living standards relative to other jurisdictions that have fell behind. Existing disparities as well as the workings of the local level governments that could worsen the economic equity in the future is detrimental to the general welfare of the denizens as well as for the practice of federalism. The trend of economic disparities among local level governments goes against the spirit of the federalism, constitution, as well as against the principles of equality. With the massive effort and cost of restructuring the nation already incurred, the inequality in development across local level governments, caused by the fiscal and economic management, raises serious questions towards the economic and the political system of the nation.

As the fiscal and economic performances vary among the local levels, it is important to investigate the chief determinants of such variation. As people's will and mandate was paramount in installing the federal system of governance, the impact of electoral influence, an extension of people's will, on fiscal and economic performance must be examined. As fiscal and economic powers are devolved from the central government and are utilized by the local level governments, it should be employed in an accountable manner so as to minimize rent-seeking and shirking behaviors. Elections, through sanctioning and selection mechanism, strives to limit such behaviors and it is of critical importance to judge the effect elections could have on such behaviors.

Election system in democracy offers the winner the authority to rule while simultaneously offering the loser the chance to run in the future(Przeworski et al., 1999). As elections are a medium to hold the elected officials accountable to the general public, electoral influence, through voting behaviors, influences the fiscal and economic working of the local level government of Nepal. Economic literatures are conflicting in the intensity and magnitude of effect electoral outcomes have on the fiscal and economic performances of the sub-national governments, thus, it is important to gauze what impact, on fiscal performance, did the first ever elected local government had in Nepal.

1.3 Research Questions

Based on the statement of the problem of this study, the research question are formulated. Thus, to properly analyze the differences in the electoral characteristics that led to differences in local level fiscal management, leading to some having a sound fiscal positions than others, the research question for this study could be stated as:

i. What are the differences in the electoral characteristics of local level units of Nepal?

ii. What are the differences in the fiscal performances of the local level governments of Nepal?

iii. How the differences in electoral characteristics translates to the differences in the fiscal performance of local level entities of Nepal?

These are the fundamental research questions that this study aims to investigate and answer. The primary focus would be on the third question, i.e., how are electoral characteristics and fiscal performance of the local level governments are related. As based on the statement of problem these research questions were formed, based on the premises of these research questions, the objectives of the study is defined.

1.4 Objectives of the Study

The chief aim of this study is to investigate the determinants and the differences in fiscal performances among the local level governments of Nepal, potentially leading to inequality in taking development initiatives as well as unequal outcome in living standards. The electoral composition and involvement of the local level entities are also analyzed, especially in relation to its effect on the fiscal management by the elected officials. Thus, the specific objectives could be stated as:
I. To analyze whether local electoral composition and behavior influence local government's performance in bevy of areas.
II. To gauge the impact of local government performance on economic and fiscal outcomes.
Additionally, apart from these two prime objectives, the accountability relationship that exists between the elected officials and the electorate is also the objective of this study.

1.5 Significance of the Study

The purpose of this study is to understand the inherent as well as overtime evolved fiscal and economic differences in the local level. Federal structure with powerful local entities are new facet through which the developmental activities desired by people could be efficiently and effectively achieved. Thus, it is imperative that the workings of the federal structure and the differences among and within local levels be properly investigated. Differences in fiscal management, resulting in unequal development leads to constricted economic opportunities for the less developed regions in the future, increase the political discontent, as well as severely impact social wellbeing factors(Saey, Kesteloot, & Vandermotten, 1998)

The findings of this study would be useful in understanding if the federal system is working as intended for most of the populace. It will equally be useful in contextualizing the factors that are making some local levels different than others, and the ways of mitigating those factors. Similarly, this study could be useful in understanding how the grants and other economic assistance programs from the central governments should be diverted or targeted towards for better effectiveness.

Chiefly, this study contextualizes how accountable are the local elected representatives of Nepal to their electorate. The accountability aspect would be measured through the fiscal performances and the differences in such performances would be analyzed through the differences in electoral compositions, behaviors, and outcomes. As the federal system of governance is a recent development in Nepal, it is of extreme importance to gauze how the elected officials of the local level governments are fulfilling their economic and fiscal accountabilities to the denizens of their local level.

1.6 Limitations of the Study

This study intends to use secondary data on economic activities of local levels to gauze their fiscal and economic differences. Those data in many cases were published by the local levels themselves or derived through the report of the AG office or through NNRFC. Similarly, the chief focus of this study is in economic sense, whereas the differences in local levels might be of non-economic in nature. Considering these factors, the chief limitations of this study can be summarized as:

i. The secondary data to be collected, published by the local levels themselves, sometimes are presented without the audit from the AG office or the third party. Thus, those data might have inconsistencies and presents problems for this study.

ii. The COVID-19 crises altered the financial and economic landscape of the local levels, with some suffering severely while other local levels were relatively unbothered.

iii. The first election for the local level governments in 2017 were held in three distinct stages, from May to September. The results of the previous stage might have influenced the subsequent electorate behavior. For simplicity, this study omits such influence.

iv. The LISA scores used in the analysis is a self-reported scores of the local governments, although there are several checks in the program to ensure the scores matches the performance.

v. This study omits the effect of potential gerrymandering of local level governments. Gerrymandering changes the dynamics of the effect that electorate have on elected officials and makes complex the analysis of electoral accountability, thus, this study assumes no gerrymandering was carried out.

1.7 Outline of the Study

This study contains the preliminary parts, the main body, bibliography, and annex. The preliminary parts, preceding the main body, consist of several pages, including the declaration sheet, approval sheet, acknowledgement, table of contents, list of tables, list of figures, list of abbreviations, and abstract. The bibliography section follows the main body, and at the end of this study annex is appended. Followings are the contents of the main body section of this study:
Chapter 1: Introduction: This first chapter basically explains what this study is about and how it is conducted. This chapter is further divided into the following sections:

i. Background of the study

ii. Statement of the problems

iii. Research Questions

iv. Objectives of the study

v. Significance of the study

vi. Limitation of the study

vii. Outline of the study

Chapter 2: Review of Literatures: This chapter is concerned with the existing body of work substantially related to the topic of this study. Thus, this chapter critically examines the books, journal articles, reports, and other concerned materials as they relate to the electoral accountability and fiscal performance. This chapter is sub-divided into theoretical and empirical review of existing literatures, with national context review sub-section added within the empirical section.

Chapter 3: Research Methodology: This chapter explains in detail the research design and the methods used to collect and analyze data. This sections further explains the nature of variables, the population and sample, and sources of data.

Chapter 4: Analysis and Discussion: This chapter details the nature and behavior of the data based on the framework of the preceding chapter.

Chapter 5: Summary and Conclusion This chapter summarizes the major findings of the research and presents the conclusion drawn, along with the suggested recommendations based on the results.

Chapter II: REVIEW OF LITERATURE

2.1 Introduction

This chapter examines several literatures related to the theme of elections, local governance, and their relationship as it pertains to fiscal and economic disciplines. As federalism is relatively a new practice for Nepal, and its' formal initiation was less than a decade ago, this field contains paucity of empirical research in the national context. However, there are plethora of literature on federalism both from the theoretical perspective as well as in the empirical and international context. Thus, this study first looks at the theoretical overview of differences in the local level fiscal and economic disciplines in the federalist system, followed by the empirical review of such differences. This section concentrates the international literature within the empirical review and finally presents the literature gap that this study further focuses upon.

2.2 Theoretical Review

The literatures in federalism and fiscal decentralization can be grouped into first generation model and the second generation theory. The FGT approach to the role of federalism and inequality among the federal units are characterized by the writings of chiefly, Musgrave, Oates, Tiebout, and Buchanan. The second generation models, characterized by using theories from microeconomics in federalism analysis, are chiefly influenced by the writings of Weingast, Seabright, Lockwood, and Coate. On balance, FGT theorists investigating fiscal federalism tended to focus on tax assignment among the subnational units and associate the process of fiscal decentralization with an enhancement in the overall degree of public sector responsiveness to a public demand and, ultimately, to an improvement in the economic efficiency of public economic activities by better linking resource allocation with public preferences. Whilst the SGT of fiscal federalism focuses on how political and institutional arrangements within subnational units interact and affects the economic and fiscal outcomes of the nation.

Tied with both FGT and SGT of fiscal federalism is the electoral accountability aspect. Downs (1957) is one of the early and seminal works examining how the electoral decisions are made and how the elected officials are held accountable. Inspired by the earlier work of Schumpeter, Downs developed the rational model which influences both, the voting turnout of the electorate, and the actions of incumbent and opposing candidates. Focusing on the available knowledge available, i.e., perfect or imperfect, and the cost of information, Downs' model posit that while voters decide their votes based on the rational utility assumptions, political parties and candidates formulate policies strictly as a means of gaining electoral victory. Thus, the elected officials are accountable to the electorate in increasing their utility through policy formulation and carrying out procedures, and apart from this social function, the incumbent also has the private motive, namely, to attain and maintain the income, power, and prestige of being in office. Thus, elections do affect the policy choice and formulation by the winners as they are accountable to increase the perceived general welfare level of the electorate.

Baron (1994) presents a model of electoral competition where electorate and candidates behaviors, influenced by ideologies, interest groups, campaign contributions, and information could manifest in an electoral equilibria. Investigating the interaction between the populace and candidates through various mediums, this model distinguishes the electorate as either informed or uninformed about the policy positions and ideologies presented by the political parties and the candidates. In this model, voters provides not just the votes in the election, but also makes up the interest groups, who, according to their ideological similarities, provide campaign contributions to the candidates and the political parties. The accountability of the elected officials are categorized through particularistic policies, which benefits only the selected group of the electorate, or collective policies, which benefits all electorate. Thus, in this model, the elected officials are accountable and it is within their realm of choices to fulfill their accountabilities, either to particularistic or collective electorate.

Grossman and Helpman (1996) investigates the dynamics between the competing parties as well as between candidates and electorate. This model examines the determinants of the policy positions, campaign contributions, vote counts, and policy compromise within an accountability framework. Ignoring the prospect of coalition formation, and limiting the analysis to a two-party system, this model assumes two types of voters, knowledgable voters who vote based on the ideologies of the candidates and are more prone to demand for accountability, and impressionable voters, with no set ideological preferences, who are susceptible to campaign advertisements and other forms of electioneering. Political equilibrium is achieved, either through influence motive or electoral motive or both, where candidate set their policy platforms maximizing their votes, and perspective voters set to be the recipient of maximal patronage that could be delivered to the party loyalists. Using a game theoretic approach to platform setting and voting decision, this paper develops six propositions, some of which achieves Nash equilibrium.

Alesina and Perotti (1996) tackle the crucial topic of fiscal consolidation and long-term fiscal balance in economic policy, which is a matter of great concern for emerging countries, transition economies, and members of the OECD. The two primary focuses are deficit reduction (particularly in high-debt-to-GDP nations) and the necessity of significant welfare and social security system reforms for long-term fiscal stability. The benefits of inflation targeting and central bank independence have been widely discussed in monetary policy discussions; however, there has been less theoretical and empirical research done on budget procedures and institutions.This study analyzes possible institutional adjustments and examines whether budget processes have an impact on budget balances and their composition. In order to centralize and streamline the budget process, it finds that budget processes do important and suggests strengthening the executive's role—specifically, that of the treasury minister—and improving transparency.Budget preparation, approval, and execution are governed by rules and regulations, as revealed by theoretical insights into budget institutions. This study makes a distinction between procedural requirements (like voting rules), numerical objectives (like balanced-budget regulations), and transparency rules. Although numerical objectives have the ability to promote fiscal discipline, they may also cause rigidity and less transparency, which might compromise their efficacy. There is a trade-off between hierarchical and collegial methods in the procedural norms that govern budget creation and approval.Collegial processes encourage checks and balances but may postpone budgetary adjustments, whereas hierarchical methods may improve fiscal discipline but may also benefit the majority. The influence of budget openness is also covered in the study, with an emphasis on how a lack of transparency can impede fiscal discipline by fostering innovative accounting procedures and raising doubts about the health of public finances.Research on nations in Europe, Latin America, and the United nations has shown empirical evidence that more fiscal restraint is linked to budgetary practices that are transparent and hierarchical. The hypothesis that more transparent and hierarchical processes promote financial discipline is supported by studies by previous literatures. Measuring transparency and comprehending how different budgetary procedures affect fiscal performance are still difficult tasks, though. Different budget rules and processes may have an impact on how quickly and efficiently governments respond to fiscal shocks. This paper concludes that efficient budgetary practices should avoid getting in the way of fiscally responsible governance, even if no organization can completely avert deficits once they are identified.

Smart and Sturm (2013) posit that periodic elections are the main medium through which the voters can hold elected officials and candidates accountable and the term limit imposition breaks such accountability by restricting voters' ability to reward politicians with reelection votes. Simultaneously, this study argues that term limits, which negates the accountability and disciplinary control of voters over the elected officials, can serve the interest of voters by increasing their welfare. This study formulates a model in which elected officials and opposing candidates have private information about the effectiveness of policies, which can be of two types, namely, public-spirited, in which payoffs coincides with those of the populace, and others, which have biased preferences. This study develops a political agency model where incumbent makes a binary policy decision on behalf of a representative voter. The model developed is a game between an infinitely loved representative voter and a sequence of elected politicians in an infinite period. This study compares single, two, and more term limit regulations effect, analyzes the implications of an endogenous pool of challengers, and examines asymmetric information between voters and incumbent while also analyzing the rents received and other utilities derived from implementing preferred policies by elected officials, and finally compares how the model developed compares with the existing empirical evidence. The study develops eight proposition, and argues that while accountability aspect is broken in case of term-limits, term-limits can decrease the rent-seeking and opportunistic behaviors of the elected officials.

Foucault, Seki, and Whitten (2017) explore the intricate relationship between political results, economic conditions, and tax laws. The authors focus on two main issues: whether voters hold incumbents responsible for bad economic performance regardless of the economic policies they implement, and if economic downturns make incumbents' election defeat inevitable. The authors offer a novel theoretical framework to investigate these issues, taking into account the combined effects of taxation policies, the definition of political authority, government ideology, and the state of the economy on election results. This theory suggests that taxation policies have an independent impact on election results, challenging the common notion that economic performance alone determines electoral success or failure.The study also makes use of a recently assembled dataset that contains data on economic indicators, elections, and government policies from both before and after the most recent financial crisis. The results show that a number of factors influence how taxation policies affect incumbent electoral success. In particular, these impacts differ according on the degree to which voters can clearly connect economic outcomes to the government in office, the government's ideological stance, and whether or not there was a recession in the year before an election.The study essentially emphasizes the complex link between voter behavior and economic management. It implies that people react not just to economic results but also to how fair and successful they believe the government's tax policy to be. Furthermore, the political environment, which includes the government's capacity to convey accountability for economic results and its ideological position on economic matters, moderates these impacts. This study adds to the body of knowledge on electoral accountability by providing a more in-depth analysis of the ways in which policy and economic issues interact to influence voter behavior. It emphasizes how crucial it is to take into account the larger political and economic backdrop when evaluating election results rather than depending just on economic metrics like GDP growth or unemployment rates.

The trade-offs between externalities and accountability, through governance and electoral uncertainty is examined by Aidt and Dutta (2017). The main emphasis is on the impact of fiscal decision-making centralization on political responsibility, especially when externalities—both positive and negative—are present. The study concludes that greater rent extraction by federal politicians results from centralization's weakening of political accountability, particularly when negative externalities are present. In situations when negative externalities are substantial, the article also implies that decentralization could be preferable to centralization.The research analyzes these dynamics using a standard agency model with uncertainty in the governance. In this model, elections are used by diverse voter groups (the principals) to hold a politician (the agent) responsible. The model presents the idea of governance uncertainty, which is the situation in which a politician is unsure of which voter group will play a key role in determining the election's outcome because of things like random variations in voter turnout. As demonstrated by actual cases such as how rain affects voter participation in different elections, this uncertainty can have a major impact on election results. In terms of how much rent a federal politician may take, the research shows an imbalance between positive and negative externalities. Despite regionalism's incapacity to absorb externalities, federal politicians may be able to collect more rents in the event of negative externalities than their regional counterparts. This might potentially render federalism less advantageous than regionalism. Federalism, on the other hand, is often more advantageous when there are positive externalities as it internalizes them without permitting further rent-seeking by federal politicians. By clearly quantifying the trade-offs between electoral accountability and internalization of externalities and by emphasizing how governance uncertainty affects these trade-offs, it provides great insights into how accountability works in the federal settings. The implications for fiscal integration and disintegration are also covered in the study, and it is suggested that in some situations, the existence of negative externalities may make decentralization more advantageous.The study comes to the conclusion that while choosing between centralization and decentralization, one should take into account the kind of externalities and how political accountability is affected by uncertainty in governance. Specifically, it implies that decentralization could be more Pareto optimal when negative externalities are substantial, as centralization might encourage federal politicians to take undue rent.

Examining the impact of decentralization and devolution on democratic governance and electoral responsibility, Charbonneau and Anderson (2021) contend that by bringing government closer to the people, decentralization might improve electoral accountability by strengthening voters' capacity to assign blame and hold local authorities accountable for their deeds. Their study also discuss some drawbacks, such as the adverse externalities that might result from decentralized systems without efficient supervision and coordination methods. They point out that decentralization can boost voter engagement and political participation by increasing the relevance and direct influence of local elections on the lives of individuals. Voters will be better equipped to make educated judgments on the performance of their representatives as a result of this close closeness to information. Their study also affirms voters becoming confused about which level of government is in charge of certain policies due to the complexity brought about by decentralization, which might weaken accountability. It talks about the double effects of decentralization: on the one hand, it gives local governments the flexibility to customize policies to meet the unique requirements of their communities, which promotes creativity and adaptability. However, it can also result in issues like unequal service delivery and capability gaps across local governments, which could compromise the efficacy of local governance.This work is consistent with previous empirical observations of the advantages and difficulties of decentralization, especially with regard to the ways in which local autonomy may improve democratic accountability and the standard of governance. It also supports the ideas of fiscal federalism covered by Oates (1999) in which the budgetary implications of decentralization play a critical role in determining its overall efficacy. In order to obtain the best governance outcomes, both texts stress the significance of striking a balance between autonomy and cooperation. In light of the current international discussions over the advantages of decentralization as a governance approach, the ideas from this chapter are very pertinent. Policymakers seeking to execute successful decentralization programs must grasp the trade-offs and dynamics outlined by by this study as nations and regions struggle with calls for increased local autonomy and better governance.To sum up, the study significantly enriches the decentralization literature by offering a nuanced perspective on how the devolution of power to local levels shapes local governance and electoral accountability. It emphasizes how crucial it is to create decentralized systems that support accountability, openness, and efficient service delivery—all of which are necessary for strong democratic institutions to function.

2.3 Empirical Review

There are about 27 countries with federal structure, albeit many of them do not have enough power decentralization or devolution from the central to the federal units. However, there have been multitudes of empirical studies on how the federal system of governance are accountable to the populace and to what extent does the behavior of electorate matters. Thus, this study presents the empirical review conducted in the international context analyzing federalism and the differences among the federal units.

Alt and Lowry (1994) examines previous literatures on the fiscal effects of split administration in different countries, and concentrates on the ways in which institutional restraints and political arrangements affect budgetary results, especially in the wake of economic shocks. The focus of the study is to comprehend the implications of institutional regulations like balanced budget requirements and deficit carryover legislation, as well as the influence of political power, whether it be united or split, on fiscal policy. To capture the complexity of fiscal decision-making, the study estimate simultaneous equations for income and expenditures using pooled time-series cross-sectional data from 48 states of the US between 1968 and 1987. Partisan control, institutional restraints, and economic shocks are just a few of the carefully chosen research variables that are used to examine how these elements combine to affect budgetary results. The results show that during economic downturns, divided governments—especially those with split legislatures—find it difficult to restore fiscal balance, which results in protracted deficits. States with strict deficit regulations, on the other hand, have united governments that are better equipped to handle sudden increases in revenue while preserving a steady fiscal balance. The study also reveals subtle party distinctions, demonstrating how Republicans and Democrats react to variations in revenue, which are impacted by economic cycles and government assistance, in different ways. The findings, which are based on extensive empirical testing and simulations, show how institutional design and political control combine to significantly influence state budgetary results.Overall, by highlighting the significance of institutional and political elements in managing state finances and providing insights into the dynamics of state budgeting procedures, the research adds to the body of knowledge on dynamics between fiscal policy and electoral accountability.

Besley and Case (1995) look at the economic impacts of governor term limits, with a specific emphasis on how they influence fiscal policies like taxes and state expenditure. This study's major goal is to determine if term limitations cause a fiscal cycle that results in large fluctuations in taxes and spending, particularly during periods when governors are ineligible for reelection (lame-duck periods) and thus do not have to be strictly accountable to their electorate. Using a data set from 1950 to 1986, the authors use panel data regression techniques to examine the association between governor term restrictions and budgetary results. Key variables in the analysis include state tax revenues, state expenditures, electoral cycle indicators (such as election proximity and the governor's ability to run for reelection), and disaster relief data from the Small Business Administration (SBA) as an exogenous factor that could influence fiscal decisions. The technique entails assessing the impact of term limits using indicator variables that correspond to different times in the electoral cycle, allowing the analysis to capture the subtle impacts of these cycles on budgetary behavior. For example, the study investigates whether taxes and expenditures vary between election years, election years preceding elections, and years when governors are lame ducks. Furthermore, the study examines the regional variance in the impact of term limits, distinguishing between Southern states and others, and further divides the analysis by party affiliation, with an emphasis on Democratic governors. The data indicate a separate fiscal cycle caused by term limitations. Governors who are ineligible for reelection tend to raise taxes and spend considerably in their final term, which is not found among governors who can still seek for office. This shows that lame-duck governors, free of the need to woo voters for future elections, are more inclined to pursue financially expanding policies. Furthermore, the study reveals that natural catastrophes, which necessitate an urgent and major governmental reaction, have a significant impact on budgetary behavior. Governors running for reelection tend to raise taxes and spend more aggressively in reaction to catastrophes, presumably to match voter expectations for disaster recovery, but lame-duck governors show no additional budgetary response beyond their usual practice. The paper also expands its analysis to include the broader economic ramifications of these fiscal cycles, with a particular emphasis on state income per capita. The findings show that states run by lame-duck Democratic governors had a considerable drop in per capita income, implying that the fiscal inefficiencies caused by term limits might have negative economic effects. The study closes by analyzing the possible inefficiencies induced by these fiscal cycles, namely the distortion in resource mobilization and public benefit provision that occurs when taxes and expenditures are drastically changed owing to political cycles rather than economic necessities. The research presents strong empirical evidence that governor term restrictions can result in inefficient budgetary measures, especially during lame-duck years. These findings highlight critical considerations regarding the trade-offs associated with term limits, which may minimize political entrenchment while creating budgetary distortions that might harm state economies.

Kalseth and Rattsø (1998) tackle the crucial topic of fiscal expenditure and long-term fiscal discpline, which is a matter of great concern for developing and developed nations alike.The study uses two main methodologies: (1) Data Envelopment Analysis (DEA) to establish a benchmark for the minimum required administrative spending, which serves as a reference point to measure overspending, and (2) a bargaining model integrated with political structures to understand the dynamics of administrative services. The study used a Tobit regression model to examine the influence of political variables on the discrepancy between the minimum needed spending and actual spending.The kind of political alliance (minority, majority, or one-party majority, for example), socialist presence in municipal councils, and additional economic and demographic characteristics are important determinants. The results show that while socialist-oriented councils often have higher spending because they prioritize administrative services, split political control frequently boosts bureaucratic influence and results in higher administrative expense. The study emphasizes how difficult it is for voters to limit administrative expenditures through elections alone because coalition dynamics and party agendas have a big impact on spending trends. The study's final conclusion is that political structures are a major factor in influencing administrative spending. The study focuses on the excessive administrative spendings of the Norwegian local governments and examines the impact of different ideologies of ruling government and the coalition form of the government. Their findings suggest that when there is a coalition type government, the bureaucrats influences on fiscal and economic decisions increases and accountability of elected officials towards the electorate suffers.

Besley and Burgess (2002) look at how political organizations and the media affect how responsive and accountable the state government of India is, especially when it comes to handling emergencies like natural disasters and food shortages. The main goal of this study is to assess how political and media developments affect government action and compare them to the contribution of economic development. While economic development is frequently regarded as essential, the study postulates that political and media elements may be more important in improving government reaction to crises.Panel data regression analysis is used in the technique, and year- and state-specific factors are controlled for using fixed effects models. The model investigates the link between several explanatory variables, such as economic, media, and political factors, and government actions, such as public food distribution and catastrophe relief spending. In order to evaluate the influence of shock factors on government actions, the analysis incorporates interaction terms between media or political variables and shock variables (such as shifts in food production and flood damage).The data covers the years 1958 to 1992 and includes information on several Indian states. Economic parameters include population density, urbanization, state income per capita, and federal government revenue. Political factors include election timing, political competitiveness, and voter turnout, while media variables include total newspaper circulation and its breakdown by language. To mitigate potential endogeniety issues, media ownership is used as an instrument for newspaper circulation through the use of instrumental variable approaches.The results show a positive correlation between increased newspaper readership and improved government reaction to flood damage and drops in food output. Since regional language newspapers are better at reaching disadvantaged communities and addressing local concerns, this effect is especially pronounced for them. Political variables also have a big impact: more political competition and more voter turnout are linked to more government engagement, especially when it comes to public food distribution. Comparatively speaking, media and political variables have a greater influence on government responsiveness than economic growth factors like state income and federal revenue.The findings indicate that political institutions and media development are critical for enhancing government responsiveness, and they may even have a greater impact than economic development. Because of its local emphasis, regional media and strong political institutions improve government response and accountability. The study emphasizes the significance of a strong political environment and a well-developed media in guaranteeing efficient administration and proposes that future research should examine the ways in which media development affects local government accountability and other policy domains in emerging nations.

Martinussen (2004) investigates the factors that determine electoral performance of candidates and parties in local Norwegian elections, focusing on both political and economic drivers. The prime objective of this study is to examine how different political characteristics and economic situations influence election support for incumbent parties. To do this, this study uses OLS regression and stepwise regression methods. The political variables examined include the form of government (one-party or coalition), the government's minority status, and the amount of support from national parties. Unemployment rates, changes in municipal fees and levies, and the scope and quality of local services are among the economic considerations made.The study concludes that political qualities have a significant influence on election performance. Specifically, one-party regimes suffer higher election losses than coalition administrations. This is because one-party administrations provide more transparent accountability, making it simpler for citizens to express unhappiness. Minority administrations, on the other hand, gain from electoral support because they may transfer blame for policy errors, making them less open to criticism. National party support is also important, as more national support translates into increased support for local chapters. Furthermore, the ideological alignment of the mayor and deputy mayor is important, with governments made up of ideologically similar parties being more likely to face negative voter assessment.In terms of economic drivers, the study finds that rises in unemployment and municipal taxes or levies reduce support for the incumbent mayor's party. For example, a one-percentage-point rise in unemployment results in a 1.12-point drop in incumbent support. Conversely, high levels of service coverage are positively related with electoral support, implying that voters favor improved access to services over cost savings.The study also presents a Change and Level Version Model, which investigates whether voters evaluate both changes in economic indicators and their relative levels when rating incumbents. This method emphasizes how voters compare local incumbents to other towns or national averages, which influences their decision-making. The study concludes that, while economic changes have a direct influence on election performance, the level of economic indicators in comparison to others is equally important.

Cutler (2008) examines the role of voters accountability demand and the complexities they face when trying to attribute responsibility for policy outcomes across multiple levels of government, in context of Canadian Federalism. The study underscores the challenges posed by Canada's decentralized federal structure, where overlapping responsibilities can lead to confusion and hinder voters' ability to discern which government is accountable for specific outcomes. This study criticizes the extant literature for their simplistic measurement of voters responsibilities and the neglect of the certainty with which voters make those responsibilities attributions. Using the data from the original survey research conducted during the provincial elections in Ontario and Saskatchewan in 2003, followed by a federal election in 2004, the study indicates that voters struggle to differentiate the roles of different levels of government and further indicates that attentiveness to politics only slightly improves the accuracy of attributions.This study, thus, highlights difficulties in holding incumbents accountable in a federal system of governance where policy formulation and execution takes place in a complicated manner.

Eckardt (2008) examines how political responsibility affects local governments' performance in the context of Indonesia, with a particular emphasis on the ways in which different local government circumstances influence the provision of public services. The study's main goal is to investigate how political structures and procedures affect local governments' capacity to better serve the needs of the community and provide public services. The accountability framework, on which the research is based, asserts that efficient political accountability frameworks increase local governments' responsiveness and boost service quality.The study uses a variety of approaches, including OLS regression analysis, to investigates the accountability aspects of the local governments. Based on a sample of 177 districts, this study gathers information on a range of political, budgetary, and socioeconomic factors. The study looks at the relationship between perceived improvements in public services and political accountability indices such political fragmentation, corruption in accountability reports, community involvement, and information access.Every variable is measured in depth in the paper, the likelihood that two randomly chosen council members would belong to separate parties is used to measure political fragmentation variable, with larger values denoting more fragmentation.The percentage of households reporting instances of corruption in local executives' yearly reports is taken as in Corruption in Accountability Reports. Higher values indicate more community participation. Access to information is determined by the proportion of residents attending health planning meetings and following local elections. Per capita expenditures, the percentage of wage bills in local budgets, and the share of development expenditures on health and education are used to evaluate the state of the fiscal system. In addition, to measure the effect of fiscal transfers on service performance, the proportion of the general allocation grant in total revenues (SHDAU) is examined.The study's conclusions show that there are a number of important connections between service delivery and political accountability metrics. Perceived advances in public services are positively correlated with more community engagement and less political corruption; conversely, higher political fragmentation is correlated with poorer service satisfaction. The study also reveals that while the influence of fiscal variables like wage bills and income sources exhibits complicated and even conflicting outcomes, larger per capita expenditures typically increase service quality. The article concludes that the efficacy of political accountability systems has a notable impact on the performance of local governments. Better services are typically provided by governments that are less corrupt, less divided, and more receptive to citizen involvement. The study does point out that while though these connections offer insightful information, causality cannot be conclusively proven, and the outcomes might be impacted by other unobserved variables. In order to validate these results and investigate the long-term impacts of decentralization on local government performance, the report highlights the necessity for more research.

Gervasoni (2010) explores the concept of rentier states at a subnational level of Argentina, proposing that regions heavily reliant on external rents, such as natural resources or federal transfers, tend to develop unique political and governance characteristics. The theory presented suggests that these regions are less accountable and more autocratic due to their economic structure, which minimizes the need for taxation and thus, reduces citizen engagement, subsequently decreasing the accountability of the elected officials. This study extends the concept of rentier to the subnational level, arguing that similar dynamics can be observed within regions or states. The background sets the stage for understanding how economic dependencies, especially those based on external rents, influence political institutions and governance behaviors at the subnational level.The core of the paper revolves around developing a theory that regions reliant on external rents exhibit distinct governance structures. The theory posits that when a region's economy is heavily supported by income from outside sources, such as natural resource extraction or federal government transfers, it reduces the region's need to tax its citizens. This lack of taxation diminishes the social contract between the state and its citizens, leading to less democratic engagement and greater potential for autocratic governance. The theory draws parallels with national-level rentier states, where governments are similarly less accountable due to their financial independence from the populace. The methodology section outlines the research approach used to investigate the theory. The paper employs a mixed-methods approach, combining both qualitative and quantitative analyses to explore the relationship between external rents and governance characteristics at the subnational level. The study uses statistical models to analyze data from various subnational regions, looking for correlations between the level of reliance on external rents and indicators of governance, such as democratic engagement, accountability, and transparency. In addition to the quantitative analysis, the paper includes case studies of specific subnational regions that are heavily dependent on external rents. These case studies provide a detailed examination of how economic dependency shapes political institutions and governance behaviors in practice. They explore real-world examples of regions that exhibit less democratic engagement and more centralized, non-transparent governance due to their economic reliance on external income. The mixed-methods approach allows the paper to present a comprehensive view of the issue, combining broad statistical trends with in-depth qualitative insights.The findings of the study support the proposed theory, demonstrating a clear link between external rent reliance and specific governance traits at the subnational level. Regions that depend heavily on external rents tend to exhibit less accountability, reduced democratic engagement, and a greater tendency towards centralized, autocratic governance. The analysis reveals that these regions often lack robust institutional frameworks for ensuring transparency and citizen participation, which are more commonly found in regions with diverse economic bases, conclusively emphasizing the importance of understanding economic foundations in shaping political institutions and behavior at the subnational level. It argues that recognizing the impact of external rents on governance can help policymakers design better frameworks for accountability and democratic practices in rentier regions. The paper also suggests that future research should continue to explore these dynamics, particularly in regions where economic dependencies are likely to influence political outcomes significantly.

Skoufias, Narayan, Dasgupta, and Kaiser (2011) investigate the impact of electoral reforms on local government performance in Indonesia, with a particular focus on the implementation of direct elections for district heads. The study's primary objectives are to assess how these reforms have influenced district-level expenditures and income, to evaluate whether spending patterns align with district needs, and to explore the variations in impact across different regions and leadership situations. By doing so, Bibek aims to understand how electoral accountability shapes fiscal behavior and whether direct elections lead to more responsible and responsive governance at the local level.To address these questions, the study employs a quasi-experimental methodology, comparing districts that transitioned to direct elections with those where elections were postponed. This approach allows for a natural comparison, offering insights into the causal effects of electoral reform. The data are drawn from several sources, including the Village Potential Series, the National Socio-Economic Survey, and district-level budgetary records. These sources provide a comprehensive view of how expenditures, revenues, and budget surpluses evolved before and after the introduction of direct elections.Key variables considered in the analysis include the initial levels of public goods and services, service coverage rates, the economic circumstances of districts, and various political factors that could influence local governance outcomes. By controlling for these variables, the study isolates the specific effects of electoral reforms on fiscal performance.

Their results show that the introduction of direct elections led to significant increases in both spending and income at the district level. One of the key findings is that revenue generation from internal sources—such as local taxes and fees—saw substantial growth, suggesting that electoral accountability encouraged district leaders to put greater effort into generating revenue. As a result, districts experienced larger budget surpluses, with revenue growth outpacing the increase in spending. This finding supports the idea that direct elections can promote greater fiscal responsibility, as elected officials are incentivized to manage local budgets more effectively.However, the study also uncovers important regional differences in the effects of electoral reform. The positive impact of direct elections on spending was more pronounced in districts outside of Java and Bali, indicating that these reforms had a stronger influence on fiscal performance in less developed regions. Additionally, the election of new leaders was associated with greater fiscal improvements, while the re-election of incumbents had a less significant impact.

This suggests that the introduction of direct elections may have helped bring fresh perspectives and accountability to local governance, particularly in areas where leadership turnover occurred.Despite the overall improvements in fiscal performance, the study finds only a modest alignment between expenditures and district needs. This indicates that while electoral reforms have led to increased spending, the additional funds were not necessarily directed toward addressing specific local challenges. In fact, the reforms may have exacerbated existing imbalances, with some regions benefiting more than others, rather than ensuring that spending was targeted to the areas of greatest need. One notable example is the health sector, which did not see significant increases in expenditures despite the overall growth in spending. This raises concerns about whether certain sectors are being neglected under the new electoral system and suggests the need for further investigation into the allocation of resources.In summary, this study concludes that while electoral reforms in Indonesia have improved fiscal performance and helped increase budget surpluses, they have not fully addressed the issue of regional imbalances or led to significant improvements in service delivery, particularly in the health sector. The study highlights the need for further research into the long-term effects of electoral changes, their impact on specific sectors, and the optimal timing of such reforms to ensure that local governments are both accountable and responsive to the needs of their constituents. These findings underscore the complexity of implementing electoral reforms and the importance of carefully designing policies to maximize their potential benefits.

Ferraz and Finan (2011) investigate the link between reelection incentives and corruption among municipal politicians of Brazil. The major goal is to determine if the prospect of reelection successfully punishes incumbent politicians and minimizes their involvement in corrupt activities. To address this, the research employs a unique dataset of corruption practices revealed by local politicians and takes use of the variance in electoral incentives caused by term limitations. It specifically compares first-term mayors, who are eligible for reelection, to second-term mayors, who are subject to a term restriction and hence termed "lame ducks." The data show that first-term mayors are much less corrupt than their second-term counterparts, with 27% less rent-seeking activity. This difference is consistent across model configurations and compensates for possible confounding variables such as unobserved variations in municipal features, political aptitude, or experience. The paper interprets these findings using a political agency model, implying that first-term mayors are prevented from corrupt acts owing to fear of electoral repercussions. Methodologically, the article employs a variety of factors to examine the consequences of electoral accountability. Key determinants include the existence of local media (radio stations and newspapers) and local prosecutors, who act as proxy for information availability and the perceived cost of corruption. The research also includes indicators of political competitiveness, such as the proportion of local council members from the mayor's party and a political Herfindahl index, to investigate how election dynamics affect corruption levels. Regression studies are performed to compare the effects of these factors on corruption between first- and second-term mayors. To overcome such biases, the study investigates whether first-term mayors are more likely to bribe auditors, or if auditors are swayed by election timing or party connections. The findings show no significant changes in impacts based on audit timing, auditor affiliations, or the value of examined projects, implying that the observed variances in corruption are not due to auditor prejudice. Furthermore, the research investigates the concept that second-term mayors are less motivated to conceal corruption due to their lame-duck position, but concludes that this explanation does not adequately explain for the observed results. This study concludes that electoral accountability, as supported by reelection incentives, has an important role in reducing corruption among municipal officials. The findings lend credence to the idea that measures assuring political accountability may considerably restrain rent-seeking behaviors, especially in environments where corruption is endemic and political elites dominate. However, the report emphasizes the need for more research to establish the best design of term limits and to assess their broader influence on governance, policymaking, and overall voter welfare. The study emphasizes the significance of boosting openness and information availability, as well as political rivalry, in order to increase the effectiveness of electoral accountability in eliminating and reducing corruption.

Jones, Meloni, and Tommasi (2012) examine into the intricate connection between public expenditure and election results, with a focus on federal systems of Argentina. Voters often punish governments that run deficits or raise expenditure, as previous literatures have demonstrated. It has been observed that voters in the United States and other similar nations generally react unfavorably to budgetary growth. This is a commonly held belief in the literature, especially in industrialized countries where voters are thought to place a higher priority on budgetary discipline. This prevalent knowledge, particularly in emerging nations with federal systems, does not always hold true as voters may actually favor fiscal growth at the subnational level. According to previous research, voters in the United States, Israel, and Colombia, for instance, typically penalize municipal governments for having lax budgetary policies. However, in Brazil, Russia, and Argentina, more regional or local government spending is frequently linked to better election results for incumbents, indicating a distinct dynamic at work.The study makes the case that these disparate outcomes are due to the way fiscal federalism is set up in these nations. Voters frequently believe that more public expenditure is funded by the federal government rather than by their own taxes under federal systems like Argentina's. The people are more inclined to reward politicians who participate in fiscal expansion as a result of this impression, which lowers their perception of the actual cost of such expenditure. This conduct resembles the dynamics seen in American pork-barrel politics, in which local legislators get compensation for obtaining federal funding for their districts without raising local taxes in the process. The authors offer a simplified model that compares various budgetary arrangements and how voter behavior is affected in order to explain these events. Voters are more inclined to penalize excessive expenditure in systems with strict budgetary limitations, like the US, since they face the actual expense of the increases. On the other hand, people could be more likely to back politicians who raise expenditure under systems with loose budget restrictions, like Argentina's, where the cost is shared by the entire country.These findings have important policy and governance ramifications. This study, using the result of six gubernatorial elections from 1987-2007 in 24 provinces of Argentina, contends that voter behavior and political incentives to support fiscal expansion can be significantly impacted by the structure of fiscal federalism. This knowledge is essential for developing policies that promote financial restraint while upholding political accountability. Thus, by highlighting the significance of fiscal federalism in influencing voter incentives and election outcomes—particularly in developing nations with decentralized governance structures—the article contributes to the growing body of research on the political economy of fiscal policy.

Gemmell, Kneller, and Sanz (2013) explore the impact of fiscal decentralization on economic growth, with a particular focus on how the devolution of spending and revenue responsibilities influences this relationship. The study revisits Oates' (1972) premise, which argues that economic efficiency improves when there is a close alignment between revenue discretion and expenditure obligations at the subnational level. This study aims to provide a more nuanced understanding of this relationship by analyzing how different aspects of fiscal decentralization interact to affect growth.To conduct this analysis, this paper employs panel data regressions and the Pooled Mean Group estimator, enabling the study to account for both long-term and short-term dynamics across countries. By incorporating instrumental variables, such as lagged values of fiscal decentralization and investment, the study addresses potential issues of endogeneity—where variables might be mutually influencing each other. Extensive diagnostic tests confirm the robustness of the results, adding credibility to the conclusions.The study is based on panel data from 23 OECD countries over the period 1972–2005, offering a broad view of how fiscal decentralization has influenced growth in developed economies. It explores various dimensions of decentralization, including government revenue composition and the distinction between direct expenditure controlled by local entities versus self-financed revenue streams. The findings indicate that while expenditure decentralization—particularly when local entities have control over spending without equivalent control over revenues—tends to have a negative influence on economic growth, revenue decentralization has the opposite effect, promoting growth.Specifically, the study supports Oates' hypothesis by demonstrating that when revenue discretion is closely aligned with expenditure obligations at the local level, it leads to more efficient and effective governance, which in turn fosters economic growth. The results are consistent across different datasets and methodologies, reinforcing the conclusion that both spending and revenue decentralization should be considered together to fully understand their effects on growth.One of the key policy implications of the study is that to maximize economic growth, governments should focus on reducing expenditure decentralization—particularly in cases where local entities have significant spending responsibilities without sufficient revenue control—while simultaneously increasing the portion of local expenditures that are self-financed through local revenues. This alignment ensures that local governments are held accountable for their spending and are motivated to use resources efficiently, ultimately contributing to stronger economic performance. The findings highlight the importance of fiscal balance at the subnational level and suggest that a well-designed fiscal framework that ties revenue collection to expenditure obligations can be a powerful driver of economic growth.

Gélineau (2013) investigates how electoral representatives are accountable to their electorate in developing countries. Not satisfied with the extant literatures which focus heavily in the industrialized nations, this study examines the accountability aspects and electoral incentives in the developing nations. Using a large-n approach with the survey data, this analysis develops a series of incumbent support model to measure the impact of economic assessment in developing countries. This study separates the motives of electorate, and focuses on the economic vote, the voters who actually vote primarily based on the economic aspects. This study uses the public opinion data from various developing nations, estimates incumbent support from it, and estimate average effect using Monte Carlo simulation. The variables investigated include 'economy', which captures individuals' assessments of past and future economic performance; 'ses' (socioeconomic status), which includes variables like age, education, and gender; 'ideology', which reflects political attachment or ideological stance; and 'controls', which include region-specific factors such as corruption, crime, and support for democracy. The dependent variables utilized are 'vote' (voting intentions) and 'approv' (approval of the president or administration). The findings show that economic assessments regularly influence incumbent support, with negative evaluations leading to disapproval and favorable evaluations to support. This impact is typically significant across both the ‘vote’ and ‘approv’ models, although the ‘approv’ model has a greater rate of significance, most likely due to the difficulties in estimating vote intentions outside of electoral seasonsThis study finds that economic aspects are important factor in holding the elected officials accountable to people, as people heavily base their voting decisions on it. Thus, this study, encompassing 51 countries of the developing world over the 1995-2009 period, concludes that while voters do strongly hold the incumbents accountable for economic aspects, they also sometimes vote on prospective assessments rather than strictly retrospective economic assessments.

Porcelli (2014) evaluates the efficiency of local governments of Italy and how it relates to the electoral accountability. Previous literatures posit that electoral systems can significantly influence the performance of government by incentivizing politicians to act in the best interest of voters. These models suggest that when voters can directly hold their elected officials accountable, particularly in majoritarian electoral systems, there is a greater likelihood of reducing rent-seeking behaviors and enhancing public service delivery.However, these studies have frequently encountered difficulties in accounting for the complexities and variations in institutional settings, leading to inconclusive or context-specific findings. The need for more robust empirical approaches that can address these challenges is a recurring theme in this study of Italian local governments. Comprehensively examining the reforms of Italian regional governments in health care sector, this study evaluates the impact of the electoral reform in a quasi-experimental setting.Thus, this study builds on this methodological tradition by integrating DiD with stochastic frontier analysis (SFA) and data envelopment analysis (DEA). This combination allows for a more nuanced examination of the efficiency effects of electoral and fiscal reforms, specifically within the context of the Italian health care sector. The study concludes by agreeing with recent theoretical literatures showing a positive association between local government efficiency and the electoral accountability, which are further influenced by the institutional factors such as electoral rules and fiscal decentralization.

Fosssati (2018) analyzes the early theories of electoral accountability which were largely developed in established democracies, where voters are expected to evaluate incumbents based on their performance in office. These theories suggest that democratic accountability is a key mechanism through which citizens can hold elected officials responsible, thus ensuring good governance. However, the application of these theories to developing democracies has been met with mixed results, often due to varying levels of democratic consolidation, political competition, and the presence of clientelism.In Southeast Asia, and Indonesia in particular, the scholarship has been divided on whether electoral accountability functions effectively. Some scholars argue that clientelism and patronage politics dominate the electoral process in Indonesia, undermining the accountability mechanism. These studies emphasize the persistence of money politics, vote-buying, and the influence of local elites in determining electoral outcomes. As a result, voters are often seen as passive recipients of patronage, rather than active agents in holding their leaders accountable.However, other scholars have highlighted the gradual emergence of performance-based voting in Indonesia, particularly in urban areas with higher levels of education and political awareness. These studies suggest that as democracy deepens, voters begin to assess incumbents more critically, taking into account their policy performance and governance outcomes This shift is seen as part of a broader trend towards democratic consolidation, where electoral accountability becomes more effective over time.This study builds on this body of literature by examining electoral accountability in three Indonesian cities: Medan, Samarinda, and Surabaya. The choice of Medan, Samarinda, and Surabaya as case studies is deliberate, as these cities represent different political and socio-economic environments. Medan is characterized by intense political competition and a history of clientelism, while Samarinda presents a middle ground with moderate political contestation. Surabaya, on the other hand, is noted for its relatively high levels of civic engagement and government performance. It contributes to the ongoing debate by providing empirical evidence that while clientelism remains prevalent, there is also significant evidence of performance-based voting. The core of the study's quantitative analysis involves a survey conducted among voters in these three cities. The survey was designed to capture voters' evaluations of local government performance and their voting behavior in recent elections. Respondents were asked about their satisfaction with local services, perceptions of corruption, and their likelihood of supporting the incumbent mayor or governor. To complement the quantitative findings, the study also incorporates qualitative interviews with key informants, including local politicians, campaign managers, and political analysts. These interviews provide context to the survey data by exploring the dynamics of local politics, the role of clientelism, and the strategies used by incumbents to secure votes. The study's findings suggest that Indonesian voters are increasingly using their electoral power to hold local politicians accountable, indicating a more nuanced understanding of how democracy is functioning at the local level in Indonesia. This research thus aligns with the emerging view that electoral accountability is possible in developing democracies, but its effectiveness varies depending on local contexts and the level of democratic maturity.

Veiga and Veiga (2019) investigate how accountability, driven by electoral incentives, shapes fiscal policies in Portugal's local governments, particularly through the imposition of mayoral term limits. The study aims to address conflicting findings in the literature regarding how accountability is impacted when term limits are introduced. By focusing on 308 municipalities over five election cycles (1998–2013) and using a difference-in-differences approach, the study examines how term limits affect fiscal outcomes such as revenues and expenditures.The findings reveal that when mayors are term-limited and unable to run for reelection, accountability diminishes. These mayors tend to reduce efforts to collect revenues or sustain spending, leading to a decline in both. Without the electoral pressure to appeal to voters, their incentives to engage in proactive fiscal management weaken, resulting in a notable decrease in government performance.Conversely, mayors who are eligible for reelection are found to be more accountable, as they are motivated by electoral incentives to secure voter approval. These mayors focus on new investments and actively pursue conditional grants from the central government, which can directly impact their chances of reelection.The study concludes that elections play a key role in holding officials accountable for their fiscal policies. However, the introduction of term limits can undermine this accountability, as the lack of reelection prospects reduces the motivation for mayors to maintain fiscal discipline. In this way, while term limits are intended to prevent political entrenchment, they can inadvertently weaken the fiscal responsibility of local leaders.

Marín, Goda, and Tabares-Pozos (2021) investigate the link between electoral participation, political competitiveness, and fiscal success in Colombian municipalities between 2000 and 2015. The research uses an unbalanced panel data fixed effects model to compensate for unobserved time-invariant local institutional structures, ensuring that the analysis takes into account each municipality's distinctive characteristics.Municipal fiscal performance, as measured by the composite Fiscal Performance Index (FPI), is the dependent variable, with political competitiveness and election participation serving as the key independent factors. The FPI is calculated using Principal Components Analysis (PCA) and takes into account six essential areas of local public finances: operational costs, debt service, transfer revenue, internal resource creation, investment spending, and saves capacity. Political competitiveness is evaluated by the Herfindahl-Hirschman Index (HHI) and the mayor's party's percentage of council seats, whilst voter turnout rates show electoral involvement. Control factors such as political affiliation with higher levels of government, education quality, violence occurrence, income, and population density are included to offer a more complete study. The findings show that more political competition, as measured by a lower HHI, and increased voter turnout have a favorable impact on local budgetary performance. Specifically, greater distributed political power within the council and active voter engagement result in better budgetary outcomes, which is consistent with political accountability theories that believe higher competition and scrutiny encourage better governance. Furthermore, the examination of FPI subcomponents reveals that political competition improves own resource production, investment, and savings capacity while decreasing operational expenditures and debt servicing costs.The study recognizes a constraint in completely capturing political competitiveness in Colombia due to the fluid nature of party memberships, where politicians regularly switch parties, confounding the examination of formal electoral statistics. Despite this, the study concludes that the decline of traditional political party dominance and the rise of new parties over the last two decades has benefited Colombia's local fiscal performance, emphasizing the importance of political diversity and active citizen participation in improving governance outcomes.

Mendoza, Hankla, and Martinez-Vazquez (2021) examine the impact of government performance and expenditure patterns on the likelihood of mayors being recalled or reelected in Peruvian municipalities from 2011 to 2014. The study seeks to comprehend how various performance measures and spending patterns influence local political results. To do this, a cross-sectional study was carried out on a sample of 1,632 district municipalities, using ordered logit models to investigate recall probability and probit binary models to estimate reelection prospects. The recall dependent variable is an ordinal variable that indicates if a Mayor is not part of a recall process, is part of the recall process but not revoked, or has been revoked. The reelection model employs a binary dummy variable that indicates whether a Mayor was reelected or not. The research takes into account performance characteristics such as garbage collection frequency and primary school dropout rates, both of which are important in determining the efficacy of municipal services. Several models are used to examine spending variables, including total expenditure per capita, transfer-financed expenditure, and the distinction between capital and current expenditures. The data show that improved waste management and decreased dropout rates have a major impact on both recall and reelection. improved overall expenditure per capita is linked to lower recall hazards and improved reelection prospects. However, the analysis reveals an unexpected finding: more dependence on vertical transfers, rather than improving reelection prospects, is associated with a higher probability of remembering. This shows that voters may see local governments' reliance on transfers as evidence of poor performance. The data also reveals that political alignment with higher levels of government and the number of candidates in elections increase recall probability, while biases such as gender discrimination against female mayors and geographical accessibility issues influence outcomes even more. The study suggests that, while municipal accountability systems in Peru are relatively efficient in holding mayors accountable based on performance criteria, flaws exist, including the possibility of political misuse and prejudice.

2.4 Literature Gap

As Nepal is a relatively new federal state, paucity of research have been carried out in the national context examining the role of electorate in shaping the fiscal discipline of their local government. Neither have there been literatures analyzing the similarities and disparities that exist among local level of Nepal. Existing theoretical and empirical literature suggests that electorate influence the behavior of the elected officials in regard to the formulation and execution of fiscal and economic policies. However, such conclusions are not always valid as other literature contends that electoral accountability of officials depends on the institutional and other factors and that the officials might have little to no accountability to the electorate.

Further, federalism, with different level of governments, complicates the accountability process as voters might not have enough information to adjudge the policy formulation and implementation jurisdictions of different level of governments. In Nepali context, local level governments are the closest level of government and its officials are elected by the citizens of that local level. With the clear link in existing literature between fiscal and economic discipline with the economic growth, it is paramount to analyze the extent to which the electorate affects the fiscal and economic decision making of the local level entities of Nepal.

Chapter III: RESEARCH METHODOLOGY

3.1 Introduction

The basic structure for this research work is presented in this section. This section presents the research design, along with conceptual framework, detailing how the research work has been conducted to achieve the research objectives. Thus, this section contains the details of the research design, conceptual framework, sources of data, tools of analysis, along with operational definition of the variables used in this research.

3.2 Research Design

To achieve the objectives of this thesis, the research will employ descriptive and explanatory research design.Firstly, analysis of how local levels of Nepal differ in fiscal, economic, and electoral sense will be conducted through descriptive design. Then for the first objective, to gauge the impact of electorate on performance indicators of LISA, a pooled cross sectional regression will be conducted. This regression will use the data collected from the first local level election in 2017 and the performance scores across variety of local governance behavior, as recorded in LISA database. For the second objective, to gauge the impact of performance scores on the fiscal outcomes, panel regression will be carried out. This regression will use data collected from the LISA database and the fiscal data of each local level as provided by the AG annual reports.

3.3 Conceptual Framework

In empirical research, a conceptual framework serves as a critical blueprint that outlines the key variables and their interrelationships. It provides a structured approach to understanding how different factors influence the phenomenon under investigation. The following diagram shows how electoral competition, through electoral accountability, influences the governance scores of the local level of Nepal. The conceptual framework, as shown in the figure 3, shows the first step of our research design.

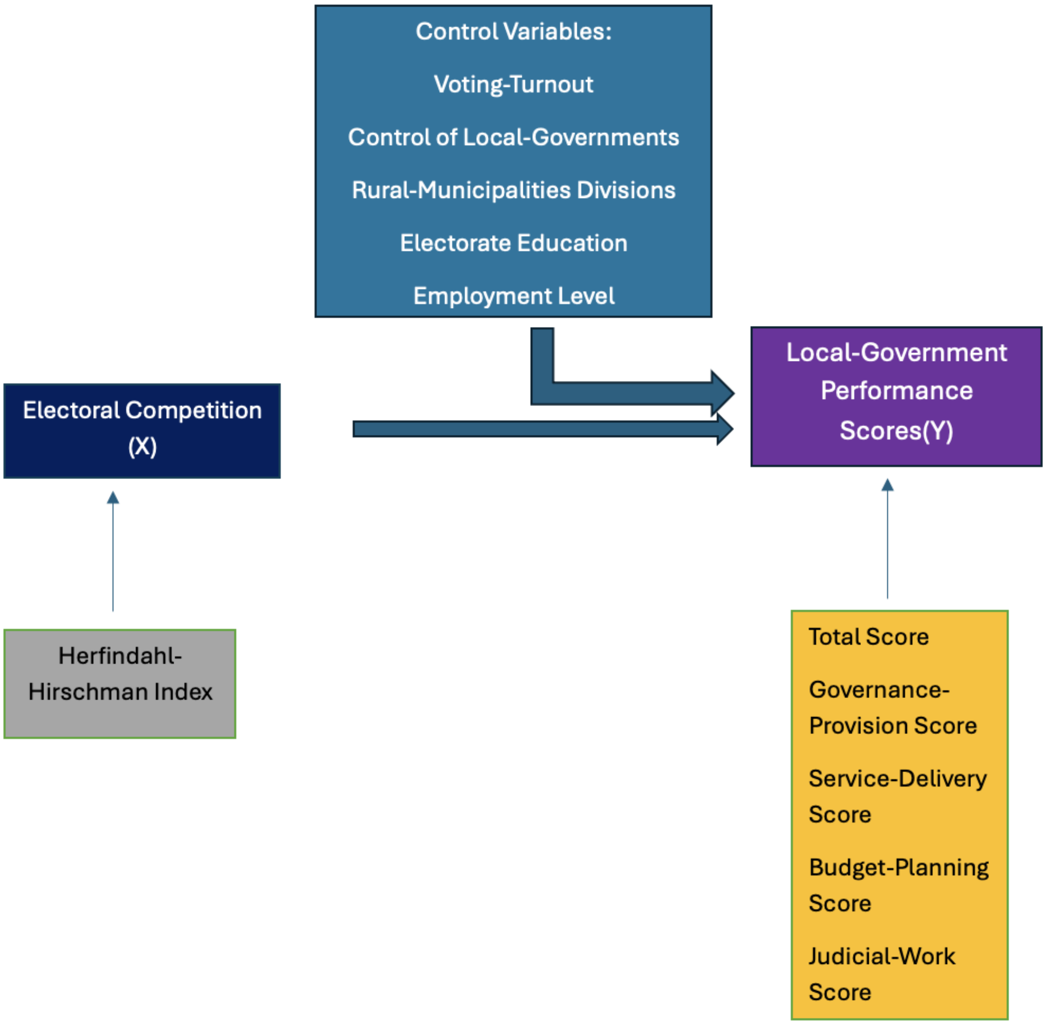

Figure 3: Conceptual Framework of the study-first step

The following figure presents the second step of the conceptual framework, which shows how the governance scores of the local governments translates to the fiscal management. Here, as seen in the figure, the dependent variable of the first step is the independent variables, thus, allowing the study to link up the electoral dynamics with the fiscal management through the governance mechanism.

3.4 Sources of data

Data have been collected from bevy of sources for this empirical study. The data related to election which are used to construct Herfindahl-Hirschman index and Voting-Turnout variables, were collected from the Election Commission of Nepal website[4] and the official publications of the Election Commission. The data on the

[4]election.gov.np

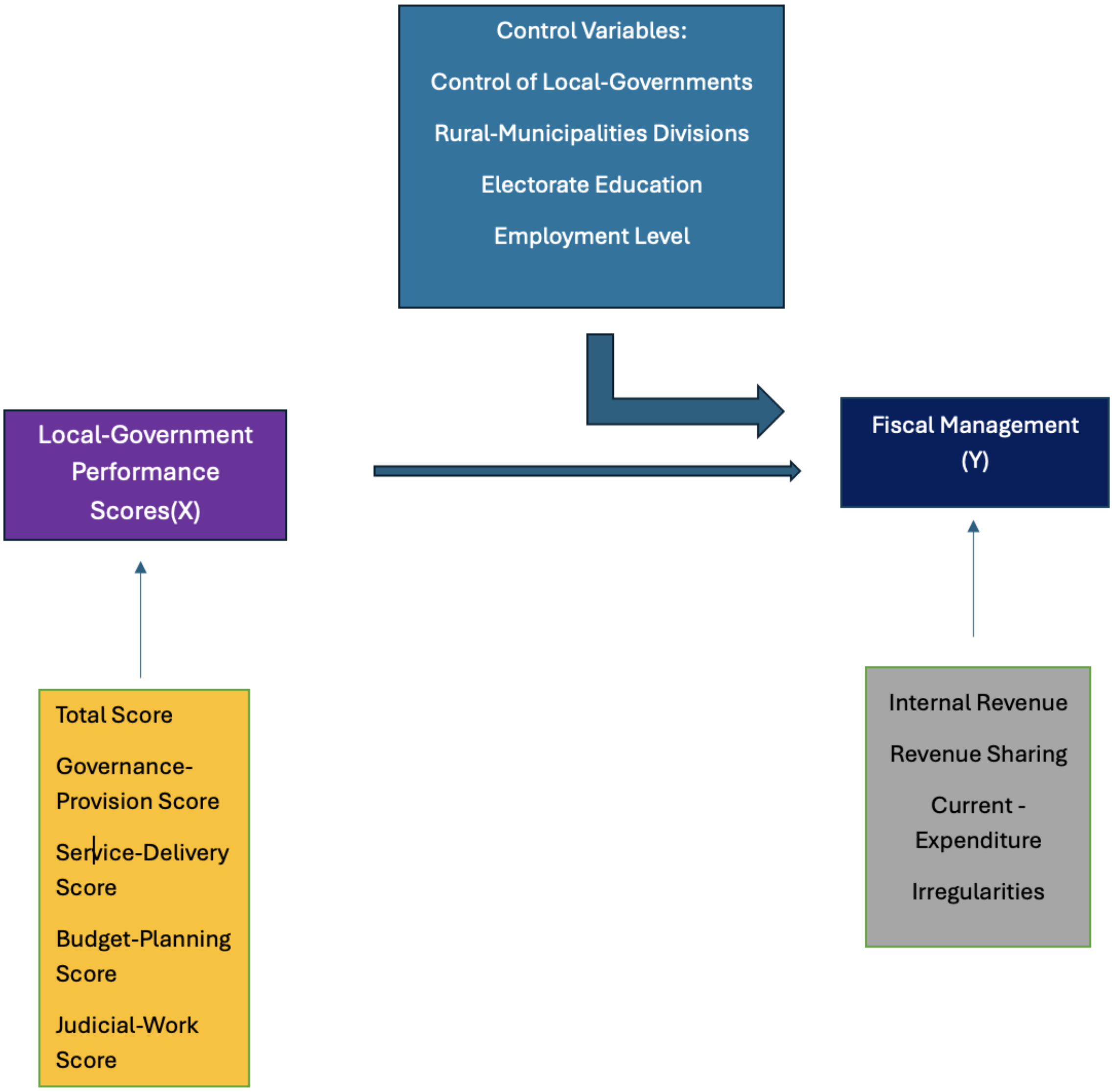

Figure 4: Conceptual Framework of the study-second step

status of local levels were collected from the Ministry of Federal Affairs and General Administration[5]. The data on the performance scores of the local governments were taken from the LISA page of the MoFAGA website[6]

The data on composition of the local governments were taken from the respective local government websites as well as from the Election Commission, whereas the data on the education status of the local level were taken from the census result of 2021 provided by the CBS. For the fiscal and economic characteristics, including, data on internal revenue each year, income from revenue sharing, current expenditure, and irregularities/Beruju, the data were taken from the annual

[5]mofaga.gov.np
[6]lisa.mofaga.gov.np

published report of AG and cross verified through matching it with the respective local levels.

3.5 Operational Definitions of Variables

The study uses the following variables in the descriptive and explanatory analysis. The Acronym provided here will be used while specifying the model too.
Herfindahl-Hirschman Index: HHI is a measure of electoral competition and concentration. It quantifies the level of concentration among mayoral candidates in the 2017 election of Nepal, indicating how evenly or unevenly votes were distributed among them. The score theoretically ranges from 0 to 1, where score closer to 0 indicates the more competitive election while the score closer to 1 indicates more uncompetitive election, where a few candidates dominate the vote share. To make the calculation simple, we only take top four vote receivers, and sum others into another group, where applicable as most constituency did not have more than five candidates.The HHI in our study has been calculated following these steps:

i. Obtaining the share of vote of each candidates in the election, thus, dividing the vote received by each candidates by the total vote.

ii. The next step is squaring the vote share of each candidates.

iii. The final step is to sum the squared share of all the candidates of the election. Thus, it could be written as the following formula:

$$HHI = \sum_{i-1}^{n} (s_i)^2$$

where s_i is the vote share of the mayoral candidate i, and n is the total number of candidates.
Voting-Turnout: VoteTurnout is, as the name implies, the percentage of total electorate that voted in the election. Thus, the percentage theoretically ranges between 0 to 100, but seldom is 0.
Control of Local-Governments: DividedControl, is a dummy variable which indicates if the mayors and deputy mayors are of the same party with the majority of ward members. Thus, it takes a value of 0 if the mayor and deputy mayor are of the same party with the majority of ward members, thus no divided control, and 1 when mayor and deputy mayor are not of the same party, or when they are of the same party but they do not have the majority of ward members of the same party.

Rural-Municipalities category: DummyRM, is a dummy variable which indicates if the local jurisdiction is a Rural-Municipality. If the local government is a Rural-Municipality, it is 1 and if it is not, the value is 0.
Employment percentage: Employ, is a variable that measures the percentage of people who are employed as per the characterization by CBS. This data is a courtesy of CBS and it is taken as having time-invariant characteristics as the yearly employment data are not available at local levels.
Electorate Education: Highedu, is a variable that measures the percentage of people of the local area who have completed intermediate level or more. The data is also a courtesy of CBS, which is based on the 2021 census. Since the education data does not change fast, this study takes the data of 2021 to be applicable to years from 2019 to 2022.
Total Governance Score: TotScore, the score as provided by the LISA program for most of the local levels yearly. It is made up of 10 different other scores related to the performance of the government.
Governance Provision Score: GovtProv, this score is one of the component of the Total Governance Score as published in the LISA database. This score is normalized to interpret the result better. It shows how the internal local governance structure is organized.
Service Delivery Score: ServDeliv, similar to the governance provision score, it is one of the component of the total score and is normalized for better analysis. It shows how the service is rendered by the local governance and is scored as mandated by the LISA operational procedure.
Budget Planning Score: BudgPlan, similar to the governance and service delivery score, it is one of the component of the total score and is normalized for analysis. It shows how the annual budget and project planning is carried out by the local governments.
Judicial Work Score: PhyInfra, one of the component of total score, it is normalized for analysis.It shows how the physical infrastructure promotion work of the local governments is carried out during the year.
Internal-Revenue: Intrevtot, is a variable that measures the internal income generated by the local level divided by the total revenue of that local level. Thus, this variable gives us what percentage of total revenue of that local level was generated internally by the concerned local level. The study expects that independent variables, governance performance scores, to have a positive association with this variable as when performance value increases, the local level is more willing and able to increase its internal source of income and thus, corresponding rise in the share of internal revenue to total revenue.
Revenue-Sharing: Revshrtot, is a variable that calculates the income earned

by the local levels as a fraction of their total revenue, from sharing the revenue with the provincial and central government. The study expects positive association with governance performance scores for the same reason as mentioned in Internal-Revenue variable section.

Current Expenditure: Curexptot variable is the fraction of the current expenditure of the local level to its total expenditure. The study expects positive association with governance performance scores as increase in HHI means decrease in electoral competition, which could weaken accountability and motivate the elected officials to spend more on current expenditures.

Irregularities-Beruju: Berujutot variable measures the 'Beruju' of each local level as a percentage of the total expenditure of that local level. Raw comparison of it would not be wise as there are local levels with different stratum of expenditures, thus, per capita technique is applied.

3.6 Tools of analysis

3.6.1 Descriptive Analysis

This study performs the descriptive analysis of the variable used in the model using statistical tools such as mean, median, and standard deviation to give context to the variables. Thus, in the next section, this study would provide the descriptive statistics of variables like HerfindahI-Hirschman Index, Vote-Turnout, Education level, Internal income of local governments among other variables.

3.6.2 Explanatory Analysis

The examination of relationship between electoral competition, as given by HHI, with the variables of fiscal and economic discipline will be carried out. For the first relationship between electoral dynamics and governance performance scores, the independent variable and control variables are all time-invariant, while the dependent variables of governance performance scores are all time variant, Wooldridge (2009) and Wooldridge (2010) states that neither fixed effect regression model nor random effect model could be used as key regressors are time-invariant. While panel structure would have allowed for the analysis of effects across multiple years, this study intends to capture broad, long-term effect and using pooled regression is valid for it.

For the second relationship, unbalanced panel regression would be used for analysis as the data are suited for it. Tests would be carried out to see whether fixed or random effect model would better present the relationship between the dependent variables and the independent variables, along with other tests to account for proper model specifications.

3.6.3 Model Specification

For the first relationship, this study will be using pooled cross sectional regression to investigate the relationship between the independent and dependent variables. Since the cross sectional regression merges the panel observations, without taking account of time variation, and would not account for autocorrelations in the residuals, this study runs a pooled regression with the following equation:

$$\begin{aligned} Y_{it} = \alpha + \beta_1 \mathrm{HHI}_i + \beta_2 \mathrm{VoterTurnout}_i + \beta_3 \mathrm{HighEdu}_i \\ + \beta_4 \mathrm{DumRM}_i + \beta_5 \mathrm{DivControl}_i + \beta_6 \mathrm{Employ} + \beta_\gamma D_t + \epsilon_{it} \end{aligned} \tag{1}$$

Where:
- Y_{it} - Dependent variables(Governance performance scores, including TotScore, GovtProv, ServDeliv, BudgPlan, and PhyInfra, of local level i at time t.)
- HHI (Herfindahl-Hirschman Index) measures political concentration at mayoral level.
- $VoterTurnout$ represents the voting percentage.
- *Divcontrol* is a dummy variable indicating whether the control of the jurisdiction is divided or not.
- *highedu* refers to the percentage of highly educated(intermediate or more) individuals.
- *DumRM* is a dummy variable indicating rural or municipal areas.
-*Employ* is an employment variable, that is provided by the census of 2078.
-D_t - Dummy variables for the years 2077, 2078, and 2079 (to control for time effects).
-β_γ -Coefficients for the time dummies.
- α is the intercept.
- ϵ is the error term.
Each coefficient $\beta_1, \beta_2, \beta_3, \beta_4, \beta_5, \beta_6$ will represent the estimated effect of the corresponding independent variable on the variables of governance performance score.

For the second relationship, unbalanced panel regression would be used with the following specification:

$$\begin{aligned} Y_{it} = \alpha + \beta_1 \mathrm{Governance\_Score}_{it} + \beta_2 \mathrm{Highedu}_i + \beta_3 \mathrm{DivControl}_i \\ + \beta_4 \mathrm{DumRM}_i + \beta_5 \mathrm{Employ}_i + u_i + \epsilon_{it} \end{aligned} \tag{2}$$

Where:
- Y_{it} - Dependent variables showing the fiscal conditions of the local level i at time

t, including Intrevtot, Revshrtot, Curexptot, and Berujutot.

-$Governance\_Score_{it}$ - The chief independent variable is the total governance score of local government i at time t, as provided by the LISA database.

-Other control variables are as explained in equation (1).

-u_i represents the unit-specific error term or unobserved heterogeneity. It captures the effects that are specific to each local level but do not vary over time. These could be characteristics that are unique to each local level but are not directly observed or included in the model. It captures unit-specific characteristics that are constant over time(fixed or random effect depending on the model that would be used).

-ϵ_{it} represents the idiosyncratic error term that captures the time-varying shocks or random errors for each local level at time t. Thus, it contains random shocks or error that are not explained by the independent variables and change over time.

Chapter IV: ANALYSIS AND DISCUSSION

In this section, descriptive and explanatory analysis will be conducted on the variables of interest. Descriptive analysis details the measure of central tendency as well as the measure of dispersion of the independent, control, and dependent variables. The results of the p regression will be presented and the relationship among the variables will be analyzed in the explanatory subsection.

4.1 Descriptive Analysis

The Mean, Standard deviation, minimum, and maximum value of the variables will be presented in Table 2 These statistics help to understand how the overall data is distributed, which will be further analyzed in the explanatory analysis.

Variables	Summary Statistics			
	Mean	*Std.Dev.*	*Min*	*Max*
HHI	35.058	10.084	20.091	100
VoterTurnout	74.475	5.818	41.5	100
HighEdu	14.691	5.839	3.161	49.091
Employ	22.393	13.103	5.099	67.257
IntRevtot	3.504	5.677	0	71.135
RevShrtot	13.547	5.216	0	56.451
CurExp	51.209	13.162	0	90.627
Beruju	9.441	12.442	0	4.172
TotScore	58.930	15.601	5.25	97.5
GovtProv	80.030	14.871	0	100
BudgPlan	61.157	18.046	0	100
ServDeliv	63.995	18.919	0	100
PhyInfra	43.749	21.219	0	100

Table 2: Descriptive Satistics of Variables

The descriptive statistics gives context to the variables of interest. Firstly, two dummy variables, namely DumRM, which represents whether the local level is a Rural-Municipality or not , and Divcontrol, which indicates if the local area government is controlled by the single party or not, is not indicated in the table above. There are 460 Rural-Municipalities in Nepal, and the rest are either municipalities, sub-metropolitan, or metropolitan city, thus, DumRM has 460 dummy as 1, and rest as 0. Similarly, there are 183 local level governments with divided political control at local level governments based on the election of 2017.

As seen from the table, the HHI average value is 35.058, meaning that overall the electoral competition was fairly competitive at the mayoral level of Nepal. The minimum value of HHI, indicating more competitive election was 0.201, which in a five party framework denotes extreme competition. The maximum value of 1, which indicates no competition, was due to the fact that in three of the local jurisdiction has unopposed mayors, indicating no competition. For voter turnout variable, the average is 74.475, with the standard deviation of 5.818. The maximum value of 100 is generated because of the unopposed mayoral candidates in the election. For higher education variable, it shows how uneven the educational attainment is among the local levels, as in some local levels, only about 3 % of people have intermediate degree of more, whereas the maximum value is nearly of majority having such degree.

The variables of fiscal discipline also show interesting dynamics. These variables were generated though the performance of the local levels in fiscal years of 2076/77,2077/78, and 2078/79 B.S., so that pooled regression could be performed, while losing the panel dimension for the first regression. The variable IntRevtot, which shows the revenue generated internally to the total revenue has the value of 3.504, meaning on average only about three and half percent of total revenue are generated internally, while in some local-levels for some years, more than 71% of the total revenue was generated internally. Similar is the case of revenue sharing to total revenue variable and current expenditure variable. In CurExp, the local levels spend more than half of their total expenditure as current expenditure, which is concerning. Irregularity variable, Beruju, shows how some local-levels have done well to control such expenditures while others have more to do, and how spread out the distribution is. Similarly, the variables of the government performance scores on different aspects of local governments, also shows interesting dynamics, The total scores of the local governments in the three year periods ranges from 5.25 to 97.5, with a mean score of 58.930. Other components of the total scores are normalized and shows how they differ across the local governments in Nepal.

4.2 Electoral influences on governance performance of local levels

4.2.1 Correlation Analysis

In this section, the correlation among the regressor variables, for the pooled regressions, are analyzed to ensure that there is no multicollinearity among the regressor. Since our regressors are HHI, VoterTurnout, Highedu, Divcontrol, Employ, and DumRM, for the first regression, the correlation Analysis will look at the correlation among them, as shown is the Table 3.

From Table, there seems to be no high correlation among variables for the problem of multi-collinearity to arise. At the higher end of spectrum of correlation is

	HHI	VoteTurnout	Highedu	DumRM	Divcontrol	Employ
HHI	1.000					
VoteTurnout	-0.1195	1.000				
Highedu	0.087	0.084	1.000			
DumRM	0.1291	-0.097	-0.372	1.000		
Divcontrol	0.095	0.047	0.042	-0.049	1.000	
Employ	-0.380	0.328	0.434	-0.397	0.001	1.000

Table 3: Correlation Matrix

the correlation between the employment and higher education variable of 0.434, indicating that higher education value is moderately influenced by the employment variable value. As the above correlation values shows the mild correlation of Employ with other variables, this study also checks for VIF.

The following table checks for the multicollinearity using the VIF. As tables

Variables	VIF	1/VIF
HHI	1.28	0.781
VoteTurnout	1.15	0.991
Employ	1.88	0.531
Highedu	1.52	0.658
DumRM	1.28	0.781
Divcontrol	1.01	0.990
Year.2077	1.47	0.681
Year.2078	1.47	0.681
Mean VIF	1.38	

Table 4: VIF- Multicolinearity Test

3 and 4 show, this study would not have concern with implementing pooled regression model as the variables are not correlated to each other, allowing for a more reliable coefficient estimates.

4.2.2 Results from Pooled Regression Analysis

Using equation(1) from the model specification subsection of Research Methodology section, this study carried out pooled regression to explore the relationship between independent and dependent variables. The dependent variable(Y) are the scores of the local government performance, including TotScore, GovtProv, ServDeliv, BudgPlan, and PhyInfra, while independent variables(X) are HHI, VoteTurnout, Highedu, DumRM, Employ and Divcontrol. The result of the regressions are given in the table(5).

Table 5 shows the regression output and thus, the relationship among variables. HHI, the index of electoral competition, is highly significant across all the depen-

Variables	TotScore	GovtProv	ServDeliv	BudgPlan	PhyInfra
HHI	0.147***	0.175***	0.158***	0.227***	0.188***
	(0.048)	(0.045)	(0.060)	(0.053)	(0.066)
VoteTurnout	-0.226***	-0.114*	-0.312***	-0.275***	-0.235**
	(0.076)	(0.067)	(0.087)	(0.085)	(0.111)
Highedu	0.617***	0.438***	0.574***	0.434***	0.655***
	(0.094)	(0.086)	(0.109)	(0.105)	(0.130)
DumRM	-3.293***	-2.210**	-2.517***	-0.969	-7.724***
	(0.999)	(0.931)	(1.121)	(0.1.162)	(1.412)
Employ	-0.095*	-0.095*	-0.053	-0.103*	-0.060
	(0.048)	(0.046)	(0.056)	(0.056)	(0.060)
Dividedcontrol	-0.796	-0.692	-0.060	-0.150	-1.524
	(0.972)	(0.917)	(1.160)	(1.121)	(1.345)
2077.Year	7.41***	6.40***	10.53***	7.16***	6.59***
	(0.59)	(0.69)	(0.80)	(0.8)	(0.82)
2078.Year	12.72***	9.86***	17.32***	11.99***	11.16***
	(0.65)	(0.74)	(0.85)	(0.82)	(0.92)
Constant	58.35***	73.5***	65.63***	71.56***	44.78***
	(5.863)	(5.269)	(6.715)	(6.63)	(8.66)
Observations	1998	1998	1998	1998	1998
R-squared	0.1838	0.1219	0.1816	0.1172	0.1288
Clustered Standard	errors	in parentheses	, ***p<0.01,	**p<0.05, *p<0.1	

Table 5: Pooled Regression results with coefficients and standard errors

dent variables, and the direction is as the study expected in the earlier sections. Our regression table agrees with the realm of literature which concede that high electoral competition produces winners who are not guaranteed to win the next election, thus, they aim to maximize their own rent seeking and profiteering behavior while in office. Thus, as HHI increases, the electoral competition decreases, and it would cause the increase in the total score and other scores of the governance performance of local levels as less competitive jurisdiction mayors perceive more chances of winning and are motivated to govern in an accountable and responsible fashion. Voting Turnout also plays the similar role as it shows significant and negative association with the scores of governance performance. As Voting turnout increases, more people are directly involved in the selection of the candidates, the winning candidates might infer that it would be difficult to win the next election, and thus involve themselves with maximizing the rent seeking behavior. Jurisdiction where turnout is low, seems to encourage mayors to perform better with the hope of being reelected in the next election.

The presence of highly educated people also affects the scores of governance performance in a positive and significant manners. More presence of educated people would better use their 'sanction and selection' power, thus, encouraging the mayors to improve performance metrics as well as encouraging the losing candidates to better analyze the decisions of the mayors and to prepare well for the next election. The dummy variable for the rural and municipal jurisdiction significantly affects the performance scores of the government. As the table shows, being a rural-municipality would lower the total score and the scores across other performance variables of the local governments, more so than other variables of the regression model.

There is a significant and positive effect of years in the scores of the governance performance measures in this model. It could be because of bevy of factors but it could chiefly be because of the fact that the data keeping and entry methods were improved in subsequent years, and that the impact of COVID-19 were extreme on the beginning of the time frame of data collection of governmental scores. The R-Squared measure of different equations are provided at the end of the table. The R squared values are relative low, as there could be other variables that are missing from this model. It should be noted that in economics, like in other social science disciplines, the behaviors of people are complex and the explanatory power of model of human behaviors are usually at the lower end of the spectrum.

4.3 Governance performance influence on fiscal discipline - using panel regression result here:show , with Hausman test, BP LM tests, stationary test and other tests here.

This section performs the panel regression to investigate the relationship between the score of the governance performance and the variables of fiscal management and discipline. First, correlation and VIF analysis will be conducted to test for multicollinearity among the regressor, then Breusch-Pagan Lagrange Multiplier test would be carried out for for determining between pooled OLS regression and panel regression, followed by Hausman test to determine whether random effect or fixed effect panel regression should be used. Also, Heteroskedasticity and serial autocorrelation will be tested along with cross-sectional dependance and unit root tests.

4.3.1 Correlation Analysis

In this section, the correlation among the regressor variables are checked to ensure that there is no excessive multicollinearity among them. Since our regressors are Total Score, Employment, DumRM, Highedu, and Divcontrol, the correlation

Analysis will look at the correlation among them, as shown is the Table 6.

	Total_Score	Employ	DumRM	Highedu	Divcontrol
Total_Score	1.000				
Employ	0.017	1.000			
DumRM	- 0.141	-0.407	1.000		
Highedu	0.221	0.471	-0.389	1.000	
Divcontrol	0.000	-0.006	-0.041	0.035	1.000

Table 6: Correlation Matrix for Panel variables

From Table 6, there seems to be no high correlation among variables for the problem of multi-collinearity to arise, as the variables are similar to those used in correlation analysis of Table 3. Explanations for the relatively high correlation between selected variables are already given previous sections and thus, this study now checks for VIF. Panel regressions account for variability across both cross-sectional units and time, which complicates the calculation and interpretation of the VIF. Thus, this study calculates VIF based on the pooled regression approach as it provides a good approximation for the multicollinearity among variables while conducting panel regression.

Variables	VIF	1/VIF
Highedu	1.43	0.697
Employ	1.41	0.707
DumRM	1.29	0.776
Total_Score	1.07	0.933
Divcontrol	1.00	0.996
Mean VIF	1.24	

Table 7: VIF- Multicolinearity Test for panel regression

As Tables 6 and 7 show, there is no considerable degree of multi-correlation among the variables to be used as the regressors. Thus, we can safely proceed towards checking if the pooled regression would be sufficient or the panel regression would be needed in the next sub-section.

4.3.2 Breusch-Pagan LM Test

Breusch-Pagan LM test would check whether the data demands the panel regression or the pooled regression would suffice. This test checks if the cross-sectional units in the panel has the same intercept or a different intercept. Thus, we run both, pooled and random effect panel regression and determine this test statistic to determine which regression model is better suited for our analysis. This test yields the following result:

Variables	Chibar2(01)	$prob > chibar2$
Intrevtot	332	0.000
Revshrtot	203.25	0.000
Curexp	33.71	0.000
Beruju	109.2	0.000

Table 8: Breusch-Pagan LM Test

As the result indicate that p-value = 0.000, for all the dependent variables , we conclude that the Pooled OLS model is not efficient estimator for our analysis. Thus, this study would be using panel regression model to explain the relationship between the governance scores of the local levels and the fiscal performance.

4.3.3 Hausman Test

Breusch-Pagan LM test suggests that the data is not pool-able and panel regression must be conducted. We administer Hausman test to further determine which type of panel regression, fixed effect or random effect, is more suited for the analysis. Since our independent variables contain both time variant and time invariant characteristics, it is essential that we test which model, random or fixed effect would be more appropriate for the analysis.

Hausman test helps decide between fixed and random effect model by testing if the unobserved heterogeneity are correlated with the regressors. In the fixed effect model, it is assumed that individual specific effects are correlated with the independent variables, thus, it drops time-invariant regressors, while random effect model assumes that individual specific effects are uncorrelated with the independent variables, thus, it doesn't drop the time-invariant variables, and include those individual effects as a part of error term. Thus, we first run the fixed effect regression, store its estimates, then run the random effect regression and store its estimates, then perform the Hausman test on the stored estimates to determine which regression model is more appropriate. In this test, lower p-value, usually less than 0.05, indicates that fixed effect model is more appropriate, while higher p-value indicates that random effect regression is better suited. The result of the Hausman test is as follows:

Variables	Chi2(1)	$prob > chi$
Intrevtot	0.2	0.6581
Revshrtot	2.84	0.092
Curexp	33.71	0.000
Beruju	109.2	0.000

Table 9: Hausman Test

4.4 Discussion

Chapter V: SUMMARY AND CONCLUSION

5.1 Introduction

This section presents a comprehensive summary of the major findings of this research, draws conclusions, and offers recommendations based on the analysis of the study. As outlined in the earlier sections, the primary objective of this study is to examine how electoral characteristics influence the fiscal and economic decision-making processes of local governments in Nepal. To achieve this objective, data was collected on the electoral characteristics of local levels based on the 2017 local level elections. Additionally, fiscal and economic data was gathered for all 753 local governments in Nepal spanning the years 2017 to 2021. However, due to the lack of standardization in the 2017 and 2018 data provided by the government, these years' data were excluded from the analysis. Instead, the study utilized data from the years 2018 to 2021, leading up to the subsequent local level election, for a more accurate analysis.

5.2 Summary and Conclusion

The role of elections in democratic systems is well-documented in economic and political science literature, particularly regarding their influence on the behavior of elected officials. Elections serve as a crucial mechanism for ensuring fiscal and economic discipline among elected officials through processes of accountability, which include both sanctions and selection. This study has found that the local governments in Nepal exhibit fiscal accountability as a result of their electoral characteristics. According to the regression analysis presented in the earlier sections, the Herfindahl-Hirschman Index (HHI) of electoral competition at the mayoral level significantly impacts various aspects of fiscal and economic discipline.

Specifically, as the level of electoral competition increases, the HHI index decreases. This relationship was anticipated to result in a negative correlation with revenue variables and a positive correlation with expenditure variables. The regression results confirmed these predictions, establishing that local governments in Nepal are indeed influenced by the level of electoral competition. Moreover, the findings of this study highlight the importance of education in relation to fiscal and economic discipline. Higher levels of education within a local government are associated with positive and significant effects on revenue variables and negative and significant effects on expenditure variables. In other words, as the educational level of the local population increases, the fiscal and economic indicators also improve.

Our finding also reveals that having divided control of the local government do not significantly effect the income variables, and only weakly effect the expenditure variables. It suggests that power sharing is not inherently good or bad in context of Nepals federalism. Furthermore, the difference of fiscal and economic performance between rural municipalities and municipalities is significant, as our finding shows that rural municipalities significantly collect less internal revenue and spends more on current expenditures compared to municipalities.

We can conclude that ....Based on the findings of this study, several recommendations can be made to enhance the fiscal and economic performance of local governments in Nepal. These recommendations are aimed at improving electoral processes, leveraging educational advancements, and addressing the disparities between different types of municipalities.

i. **Strengthen electoral competition:**This study highlights the significant impact of electoral competition on fiscal and economic discipline. To foster a more competitive electoral environment, it is recommended that reforms be introduced to enhance transparency and fairness in elections. This could involve improving electoral processes, ensuring that candidates have equal opportunities, and implementing measures to prevent electoral fraud. Increasing the level of competition can help ensure that elected officials remain accountable to their constituents and are motivated to manage fiscal resources more effectively.

ii. **Promote educational attainment:** The positive correlation between higher education levels and improved fiscal and economic indicators suggests that investing in education can yield substantial benefits for local governments. Policies aimed at enhancing educational opportunities and increasing the educational attainment of the local population should be prioritized. This could include expanding access to quality education, providing vocational training programs, and supporting adult education initiatives. By improving the overall educational level, local governments can benefit from a more informed electorate and better governance outcomes.

iii. **Further research on power sharing:** This study found that divided control of local governments does not significantly affect income variables and only weakly affects expenditure variables. This suggests that power-sharing arrangements may not have a clear-cut impact on fiscal performance. It is recommended that further research be conducted to explore the nuances of power-sharing arrangements and their effects on governance. In the meantime, policymakers should consider the specific context of each local government when designing power-sharing structures, ensuring that they are tailored to the needs and circumstances of the local population.

iv. **Address disparities between rural and urban municipalities:** The significant difference in fiscal and economic performance between rural municipalities and urban municipalities calls for targeted interventions. Rural municipalities, which tend to collect less internal revenue and spend more on current expenditures, may benefit from targeted financial support and capacity-building initiatives. The government should consider implementing policies that address the unique challenges faced by rural municipalities, such as providing financial incentives, improving infrastructure, and supporting local economic development initiatives. Additionally, efforts should be made to improve revenue collection mechanisms in rural areas to reduce disparities and promote more equitable development.

v. **Enhance fiscal management practices:** To improve overall fiscal discipline, local governments should be encouraged to adopt best practices in fiscal management. This includes implementing robust budgeting processes, ensuring transparency in financial reporting, and regularly monitoring and evaluating fiscal performance. Training and capacity-building programs for local government officials can further enhance their ability to manage fiscal resources effectively.

In conclusion, implementing these recommendations can help local governments in Nepal improve their fiscal and economic performance, enhance accountability, and promote more equitable development across different regions. By addressing the challenges identified in this study and leveraging the opportunities for improvement, policymakers can contribute to the overall betterment of governance and development outcomes in Nepal.

Write a brief paragraph on Possible extension, concept and method both highlight but subtle ways.

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