



OECD Multi-level Governance Studies

Making Decentralisation Work

A HANDBOOK FOR POLICY-MAKERS



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Foreword

Decentralisation is among the most important reforms of the past 50 years. Implemented to varying degrees in a majority of developed and developing countries around the world, decentralisation has profound implications due to its complex and systemic nature. Engaging in a decentralisation process affects all spheres of society, from the nature and the quality of governance, to a national wealth and economic growth and, more broadly, to citizen well-being.

The 2019 OECD report “Making Decentralisation Work: a Handbook for Policy-Makers” provides one of the most comprehensive overviews on the current trends in the decentralisation policies of OECD countries and beyond, and on the ways to make decentralisation work. It argues that the question should not be whether decentralisation is good or bad in itself, but that decentralisation outcomes – in terms of democracy, efficiency, accountability, regional and local development – depend greatly on the way decentralisation is designed and implemented.

The report argues that decentralisation should not be considered a panacea for any problem a country may face, nor should it be seen as an objective in and of itself. Rather it is a means to achieve certain goals. Empirical research and a number of country examples show that decentralisation can be conducive to public sector efficiency, democratisation and political stability. There are also examples of failures with decentralisation, when the reforms were not properly designed and implemented, and where the multi-faceted dimension of the process was not well understood.

The report identifies 10 guidelines for decentralisation to work and be conducive to regional and local development. Beyond the guidelines, the report proposes concrete tools for policy-makers, including detailed sets of recommendations, checklists, pitfalls to avoid and examples of good practices, both in unitary and federal countries.

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The report was written by Dorothée Allain-Dupré, Isabelle Chatry and Antti Moisio from the OECD Secretariat, Decentralisation, Public Investment and Subnational Finance Unit in CFE. The report includes inputs from Varinia Michalun as well as comments by Rudiger Ahrend, Joaquim Oliveira Martins, Yingyin Wu, Isidora Zapata, from the OECD Secretariat.

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The report was co-ordinated and supervised by Dorothée Allain-Dupré, Head of Unit, Decentralisation, Public Investment and Subnational Finance. This unit is in the Economic Analysis, Statistics and Multi-level Governance Section, led by Rudiger Ahrend, in CFE.

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Executive summary

Decentralisation is among the most important reforms of the past 50 years. This report argues that the question should not be whether decentralisation is good or bad in itself, but that decentralisation outcomes – in terms of democracy, efficiency, accountability, regional and local development – depend greatly on the way decentralisation is designed and implemented.

Making the most of decentralisation for regional development is particularly crucial in the current context of a “geography of discontent” characterised by growing divides between places that feel left behind by globalisation and technological change and those that may benefit from the opportunities offered by megatrends. Dysfunctional decentralisation systems are part of the story behind the crisis that some democracies are facing: it is thus critical to find ways to make decentralisation systems work more effectively.

What are the current trends in decentralisation?

Decentralisation refers to the transfer of powers and responsibilities from the central government level to elected authorities at the subnational level (regional governments, municipalities, etc.) and that have some degree of autonomy. Decentralisation covers three distinct but interrelated dimensions: political, administrative and fiscal. There has been a path towards decentralisation in a majority of OECD countries over the past decades. In two thirds of OECD countries, decentralisation processes have resulted in an increase of economic importance of subnational government, measured both as a spending share of GDP and share of total public spending between 1995 and 2016.

Today, regions and cities represent account for 40.4% of public spending and 56.9% of public investment in the OECD. Regions and cities play an increasing role in key policy areas linked to megatrends, such as transport, energy, broadband, education, health, housing, water and sanitation. They are responsible, for example, for 64% of environment and climate-related public investment.

The forms and extent of decentralisation vary greatly from one country to another. The financing systems for subnational governments also vary significantly, cutting across federal versus unitary distinctions. On weighted average, taxes represented the number one source of revenues for subnational governments in the OECD (45%), followed by grants and subsidies (37%).

But, decentralisation is too often understood as a simple increase in the power of local governments. The reality is much more complex, as most responsibilities are shared across levels of government. Decentralisation is also about reconfiguring the relationships between the central government and subnational governments towards a greater cooperation and a strategic role for national/federal governments.

Decentralisation trends around the world have gone hand in hand with an upscale in subnational governance through municipal cooperation, metropolitan governance, and the

strengthening of regions. Municipal fragmentation has driven policies encouraging or imposing amalgamations and municipal cooperation. However, it remains high in some countries. Municipalities having less than 5 000 inhabitants represent 44% of all municipalities in the OECD. In 10 countries, this ratio exceeds 80%. The number of metropolitan governance authorities created has increased, regardless of type, in particular since the 1990s. The rising role of administrative regions has also been striking: of the 81 countries, 52 experienced a net increase in the degree of regional authority since the 1970s (as measured by the Regional Authority Index).

In parallel to decentralisation, there has also been an increase in asymmetric decentralisation, i.e. the fact that governments at the same subnational government level have different political, administrative or fiscal powers. While asymmetric decentralisation appears more “natural” in federal countries, it is increasing in unitary countries.

Making the most of decentralisation's benefits

How decentralisation is designed and implemented has a major impact on its outcome. Decentralisation may expand citizen participation by bringing government closer to citizens and allow to best tailor public service provision to meet citizens' needs. While correlations do not allow for causal conclusions, certain measures, such as GDP per capita show a positive correlation with decentralisation. Revenue decentralisation – more than spending decentralisation – appears to be more strongly associated with income gains. Recent empirical evidence indicates that revenue decentralisation could be associated with smaller regional economic disparities.

Anticipating and minimising the risks

Central/federal governments are responsible for the framework conditions that will determine how decentralised systems operate. A lack of sufficient administrative, technical or strategic capacities is one of the bigger challenges in the field of decentralisation. Building capacities takes time and needs a long-term commitment from central and subnational governments.

The fiscal dimension is very often decentralisation's missing link. Unfunded or under-funded mandates – where subnational governments have the responsibility to provide services or manage policies without the requisite resources – are common.

Overlapping assignments between levels of government is another important challenge in decentralised systems. A lack of clarity in the assignment of responsibilities makes service provision and policy making more costly; it may also contribute to a democratic deficit.

Decentralisation may result in a loss of certain economies of scale and fragmentation of public policies. Determining optimal subnational unit size is therefore of utmost importance. However, it is a context-specific task; it varies not only by region or country, but by policy area, as well. National governments play an important role in establishing legal, regulatory arrangements and incentives to foster the cooperation across jurisdictions.

Ten guidelines for effective decentralisation conducive to regional development

The policy experiences and research results that have accumulated over the past decades can help policy makers implement decentralisation reforms in a way that avoids the major pitfalls. When properly designed and implemented, there is evidence that decentralisation policies have a number of benefits, from improved subnational public service delivery and citizen engagement, to a positive impact on growth and well-being.

To assist countries in identifying the conditions that help make decentralisation work, this report proposes ten guidelines for implementing decentralisation, which apply both to federal and unitary countries. The guidelines are more than just recommendations. Each section covers the rationale of each guideline, offers practical guidance, identifies pitfalls to avoid, highlights good practices and includes a checklist for action.

Chapter 1. Key findings

This chapter provides a summary of the key findings from the report. It highlights that decentralisation is among the most important reforms of the past 50 years, and has profound implications due to its complex and systemic nature. The question is not whether decentralisation is good or bad in itself, but that decentralisation outcomes – in terms of democracy, efficiency, accountability, regional and local development – depend greatly on the way decentralisation is designed and implemented. The report identifies ten guidelines for decentralisation to work and be conducive to regional development.

Sometimes called a “silent” or a “quiet” revolution, decentralisation is among the most important reforms of the past 50 years. It is implemented to varying degrees in a majority of developing and developed countries and has profound implications due to its complex and systemic nature. Engaging in a decentralisation process affects all spheres of society, from the nature and the quality of governance to national wealth and economic growth and, more broadly, to citizen well-being.

This report focuses on current trends in the decentralisation policies of OECD countries and beyond, and on ways to make decentralisation work. It argues that the question should not be whether decentralisation is good or bad in itself, but that decentralisation outcomes – in terms of democracy, efficiency, accountability, regional and local development – depend greatly on the way decentralisation is designed and implemented. Decentralisation should not be considered a panacea for any type of problem a country may face, nor should it be seen as an objective in and of itself. Rather it is a means to achieve certain goals. Empirical research and a number of country examples show that decentralisation can be conducive to public sector efficiency, democratisation and political stability. There are also examples of failures with decentralisation, when the reforms were not properly designed and implemented, and when the multi-faceted dimension of the concept was not well understood.

Making the most of decentralisation for regional development is particularly crucial in the current context of a “geography of discontent” and growing divides between places that feel left behind by globalisation and technological change and those that may benefit from the opportunities offered by megatrends. Dysfunctional decentralisation systems are part of the story behind the crisis of democracies: it is thus critical to find ways to make decentralisation systems more effective.

The report identifies ten guidelines for decentralisation to work and be conducive to regional development. Beyond the guidelines, the report proposes concrete tools for policy-makers, including detailed sets of recommendations, checklists, pitfalls to avoid and examples of good practices, both in unitary and federal countries.

What is decentralisation?

Although widespread and extensively analysed, decentralisation is often understood in different ways and applied in different scopes. Decentralisation refers to the transfer of powers and responsibilities from the central government level to elected authorities at the subnational level (regional governments, municipalities, etc.), having some degree of autonomy. Decentralisation is also about reconfiguring the relationships between the central government and subnational governments towards a more co-operative and strategic role for national/federal governments. It is also a multi-dimensional concept, as decentralisation covers three distinct but interrelated dimensions: political, administrative and fiscal.

The forms and extent of decentralisation vary greatly from one country to another. Depending on the country, there are also varying degrees of upward and downward accountability and varying ranges of central government control.

At the global level, the OECD-UCLG World Observatory on Subnational Government Finance and Investment has identified that subnational expenditure amounted to 9% of gross domestic product (GDP), 24% of public expenditure and 40% of public investment (OECD-UCLG, 2016^[1]).

In OECD countries, subnational governments represent a larger share of public spending, accounting in 2016 for 16.2% of GDP, 40.4% of public spending and 56.9% of public investment. Education represents the largest spending areas (25% of subnational expenditure), followed by health (18%), general public services (administration), social protection and economic affairs/transport).

Rather than a clear-cut separation of responsibilities, most responsibilities are shared among levels of government, and the trend toward shared responsibilities has increased over the past decades. The need to share responsibilities may arise for functional reasons – as is common between municipal and regional tiers around issues of transport and infrastructure, environment and water, culture and tourism, communication, or economic development. It may also arise for financing reasons such as for social services. Overall, there is greater variation across countries in the distribution of competencies at the regional level, and less variation at the local level.

The financing systems for subnational governments vary significantly. Countries can be grouped into four families based on both their degree of subnational spending and their tax level characteristics, which cut across federal versus unitary distinctions. In 2016, taxes represented the number one source of revenues for subnational governments in the OECD on a weighted average (45%), followed by grants and subsidies (37%). The degree of tax revenue is not necessarily an indication of tax autonomy, as some taxes are also shared with the central government. Tax autonomy depends on many factors, including the ability to set or modify tax rates and bases. The same is true for the degree of spending power, as often spending covers delegated functions which are highly constrained by central government regulations and fiscal discipline rules.

Measuring decentralisation is complex. Fiscal indicators are useful for providing a macroeconomic view of decentralisation but remain partial – only focusing on fiscal aspects – and may also lead to a distorted interpretation of the reality, over-estimating the real spending and taxing power of subnational governments. They must be completed by complementary approaches and institutional indicators to better understand the fiscal power of subnational governments. In particular, OECD subnational spending power indicators show that spending authority is quite low in a number of countries, and is lower in health than in housing, transport and education.

Current trends in decentralisation

Although the measurement of decentralisation is complex, fiscal and institutional indicators converge on the fact that the overall trend has been towards decentralisation, despite some exceptions.

Decentralisation reforms are and have been implemented for a wide variety of political, historical, and economic reasons that vary greatly across countries. Several moves towards decentralisation have been mainly motivated by the quest for more local democratic control, as well as by greater efficiency in public service delivery and accountability for regional and local development policies. Mega-trends such as information revolution, digitalisation, the globalisation of economic activity and urbanisation, also contribute to the stronger role played by subnational governments.

Paths to decentralisation vary considerably across countries, from “big bang” approaches to incremental approaches or “waves” of reform. Engaging in a decentralising reform is ultimately a political issue and thus should be conceived and pursued as part of a broader strategy of territorial development and broader public

governance reforms. Decentralisation should also be viewed in a more comprehensive way, including interactions between public entities and private stakeholders, in particular citizens, businesses and non-governmental organisations. Decentralisation reforms are often accompanied by other types of multi-level governance reforms, notably territorial and public management reforms. In all cases, decentralisation systems require regular review and adjustment.

Several complementary trends in decentralisation stand out:

1. **Increased subnational spending and revenues:** In two thirds of OECD countries, decentralisation processes have resulted in an increase of economic importance of subnational government, measured both as a spending share of GDP and share of total public spending between 1995 and 2016.

On the revenue side, tax revenues have slightly increased both as a share of GDP and in total public tax revenues. Subnational spending and revenue have increased – and this was amplified in some countries by the global financial crisis. Although the real spending power of subnational governments is more limited than what financial indicators show, more comprehensive indicators, such as the Regional Authority Index and the Local Autonomy Index, also indicate an increase in the degree of authority of regions and municipalities over the past decades.

2. **Upscale in subnational governance** through municipal co-operation, metropolitan governance and the strengthening of regions (regionalisation):

- **Municipal fragmentation** has been the driver of policies encouraging or imposing amalgamations. It has also motivated policies fostering inter-municipal co-operation as a way of generating economies of scale, efficiency gains and cost savings. Today, inter-municipal co-operation is widespread in the OECD, benefiting rural and metropolitan alike.
- The number of metropolitan governance authorities of all types created has increased, in particular since the 1990s. Currently, around two-thirds of the metropolitan areas in the OECD have a metropolitan governance body.
- The rising role of regions: of the 81 countries covered by the Regional Authority Index, 52 experienced a net increase in the degree of regional authority and only 9 experienced a net decline. The main objectives are to generate economies of scale in public service provision, for example in the health sector, and public transport sectors. The objectives are also to design and implement integrated regional development strategies that take into account urban-rural linkages. Regionalisation trends increase the need for co-ordination across government tiers and the need for clarification in the assignment of responsibilities, to avoid overlap.

3. **Increased asymmetric decentralisation**, i.e. the fact that governments at the same subnational government level have different political, administrative or fiscal powers. Whereas between the 1950s and the 1970s asymmetric arrangements happened mostly at a regional level, the present trend seems to apply asymmetric decentralisation in major urban areas. While asymmetric decentralisation appears more “natural” in federations, it is increasing in unitary countries, based on new motives. There is thus a greater convergence between unitary and federal countries in differentiated governance at the subnational level.

Observed experience indicates that once adopted, asymmetric arrangements are kept on a long-term basis.

In parallel to these trends affecting subnational governments, the role of central governments has evolved. Decentralisation implies a renewed role for central governments. Being more strategic, this role is focused on setting the conditions for proper co-ordination and alignment of policy objectives, monitoring the performance of regions and cities, and ensuring balanced development of all parts of the national territory, through active regional development policies. Given that most responsibilities are shared, decentralisation policies are about managing mutual dependence to achieve common objectives. Decentralisation reforms involve a shift from a direct role in service delivery to one of enabling, advising and assisting, ensuring consistency and facilitating the work of subnational governments. This requires building new capacity at the central government level, able to cope with these new functions, which cover a large area of sectors.

The impact of decentralisation on the central government is often underestimated. Failing to take the full measure of this issue may be detrimental to the reforms, slowing down or modifying the reform process.

Making the most of decentralisation's benefits

The way decentralisation is designed and implemented has a major impact on its associated outcomes. The benefits depend on the system as a whole, including the adequate capacity of subnational governments, accountability of local public decision-making and sound framework conditions.

The benefits and challenges of decentralisation can be direct or indirect. Direct effects result from enhanced allocative efficiency and may include improvements in service levels, quality and efficiency of public services. Indirect effects of decentralisation, such as faster economic growth or better stability of the society, result from direct outcomes of decentralisation such as better education or higher participation in political decision-making. Since the indirect effects of decentralisation are affected by a variety of factors, the role of decentralisation is, of course, harder to separate from other trends and policies.

While country statistics and correlations do not allow for causal conclusions, subnational fiscal power is positively associated with economic activity. In particular, measures such as GDP, public investments made in physical and human capital and education outcomes show a positive correlation with decentralisation. Revenue decentralisation appears to be more strongly associated with income gains than spending decentralisation. In addition, country examples and empirical research results show that decentralisation can be conducive to public sector efficiency, democratisation and political stability. Decentralisation has the potential to support and expand citizen participation by bringing government closer to citizens and by making government more easily accessible. In certain cases, decentralisation can be a “glue” that holds countries together.

Recent empirical evidence indicates that revenue decentralisation could be associated with smaller regional economic disparities. This could be because own-source revenue may spur growth especially in poorer regions and enhance the convergence process towards the best performing regions. Another potential benefit of decentralisation is the ability to carry out more effective regional development policies, as

local and regional actors are better able to design regional policies that respond to local needs. Institutional quality seems to explain part of the story: decentralisation appears to foster convergence when institutional quality is high, while it tends to exacerbate territorial disparities in environments with low institutional quality.

Decentralisation may also diminish opportunities for rent-seeking and corruption in public administration. For instance, a larger subnational share of public expenditures has been found to correlate with lower corruption. Again, these results depend on the way decentralisation is designed and implemented. For example, very complicated multilevel governance models with unclear assignments have been found to be more prone to corruption.

Finally, decentralisation may provide a useful way for experimenting with public policies. At best, “learning by doing” processes of decentralised policy innovation can result in important information spillovers from good practices. The “information externalities” created by decentralisation can benefit not just subnational governments themselves but also central government.

Anticipating and minimising the risks

Central/federal governments are responsible for the framework conditions that will determine how decentralisation systems operate. There are some challenges associated with both the design and implementation of decentralisation that need to be carefully addressed.

From a general aspect, decentralisation presents a challenge to subnational governments because it requires certain economic, political and administrative capacities. The lack of sufficient administrative, technical or strategic capacities is probably one of the bigger challenges in the field of decentralisation. Building capacities, including “learning-by-doing”, should be a priority. This takes time and therefore needs a long-term commitment from central and subnational government levels. There are a number of ways to strengthen government capacities at all levels, and the capacity building policies need to be tailored to the various needs of regions. Such policies require the right framework conditions for decentralisation to be in place.

The fiscal dimension is very often the weak or even missing link of decentralisation. One of the most frequent challenges, particularly in developing countries or countries at an early stage of decentralisation, but also in developed countries, is the misalignment between responsibilities allocated to subnational governments and the resources available to them. Unfunded or under-funded mandates – where subnational governments are responsible for providing services or managing policies but without the requisite resources – are common.

A high reliance on central government transfers may also reduce subnational government incentives for responsible fiscal behaviour. Subnational governments need own-source revenues because this contributes to accountability and efficiency of local public service provision. While a general rule for the optimal degree of tax autonomy is difficult to define, local authorities should rely on their own revenues for financing their services at the margin.

Another important challenge of decentralisation is formed by overlapping assignments between levels of government. Lack of clarity in the assignment of responsibilities makes service provision and policymaking costlier; it also contributes to a

democratic deficit by creating confusion among citizens regarding which agency or level of government is responsible. Unbalanced decentralisation, where the various policy areas are decentralised in different ways, can also weaken regional development policies.

Decentralisation may result in loss of certain economies of scale and fragmentation of public policies. This could happen especially if subnational governments are unable to co-operate with each other. Determining optimal subnational unit size is a context-specific task; it varies not only by region or country but by policy area, as well. National governments have an important role in establishing legal, regulatory arrangements and incentives to foster co-operation across jurisdictions, in particular within functional regions.

Ten guidelines for effective decentralisation conducive to regional development

The question is not whether decentralisation is good or bad in itself, rather it is a question of the conditions under which decentralisation can promote local democracy, efficient public service delivery and regional development. The policy experiences and research results that have accumulated over the past decades can help policymakers to implement decentralisation reforms in a way that avoids the major pitfalls. When it is properly designed and implemented, there is evidence that decentralisation policies have a number of benefits, from improved subnational public service delivery and greater citizen engagement to reduced corruption and a positive impact on growth.

To support countries in identifying the conditions that help make decentralisation work, the OECD has developed ten guidelines for implementing decentralisation. The guidelines are more than just recommendations. Each section covers the rationale of each guideline, practical guidance, pitfalls to avoid, good practices and a checklist for action, tailored to both federal and unitary countries. They are presented in a summarised version below:

Guideline 1: Clarify the responsibilities assigned to different government levels

- The way responsibilities are shared should be explicit, mutually understood and clear for all actors. Equally important is clarity in the different functions that are assigned within policy areas – financing, regulating, implementing or monitoring. Since multi-level governance systems are constantly evolving, a periodic review of jurisdictional assignments should be made to ensure flexibility in the system.
- Clear assignment is critical for accountability, monitoring and effectiveness of investment and service delivery policies. The more a responsibility area is shared across different government levels, the greater clarity is needed to reduce duplication and overlaps.
- Clarity does not mean that shared responsibilities should be avoided, as this is by definition impossible. It means that the way responsibilities are shared should be explicit, mutually understood and clear for all actors, including citizens
- The way different responsibilities across policy areas are decentralised should be balanced.

Guideline 2: Ensure that all responsibilities are sufficiently funded

- Access to finance should be consistent with functional responsibilities. Division of financing responsibilities should ensure that there are no unfunded or under-funded assignments or mandates.

Guideline 3: Strengthen subnational fiscal autonomy to enhance accountability

- Subnational governments should have a certain degree of autonomy in the design and delivery of their public service responsibilities within the limits set by normative regulations, such as minimum service standards.
- Subnational governments need own-source revenues beyond grants and shared tax revenues – and they need to develop other sources of revenue to have a balanced basket of revenues.

Guideline 4: Support subnational capacity building

- Central government should assess capacity challenges in the different regions on a regular basis. Policies to strengthen capacities should be adapted to the various needs of territories. Governments should seek to reinforce the capacities of public officials and institutions in a systemic approach, rather than adopting a narrow focus on technical assistance.
- Staff training in the basics of local public financial management should be established. Open, competitive hiring and merit-based promotion should be ensured.
- Special public agencies accessible to multiple jurisdictions should be encouraged in areas of needed expertise (e.g. regional development agencies, PPP units).

Guideline 5: Build adequate co-ordination mechanisms across levels of government

- Since most responsibilities are shared, it is crucial to establish governance mechanisms to manage joint responsibilities. Creating a culture of co-operation and regular communication is essential for effective multilevel governance and successful long-term reform. Tools for vertical co-ordination include for example dialogue platforms, fiscal councils, standing commissions and intergovernmental consultation boards, and contractual arrangements.
- It is important to avoid multiplying co-ordination mechanisms with no clear role in the decision-making process.

Guideline 6: Support cross-jurisdictional co-operation

- Horizontal co-ordination can be carried out using specific matching grants, and by promoting inter-municipal and interregional co-operation. Metropolitan governance should be promoted as well. The legal system at the national level should allow such tools.
- Rural-urban partnerships should be promoted as a form of cross-jurisdiction collaboration to enhance inclusive growth by bringing multiple benefits, such as expanding the benefits of agglomeration economies, to overcome co-ordination failures and strengthen capacity.

Guideline 7: Strengthen innovative and experimental governance, and promote citizens' engagement

- Citizens should be empowered through access to information. Ensure that elected local councils have the ownership and control of citizen participation and engagement initiatives.
- Participatory budgeting has the potential to strengthen inclusive governance.

Guideline 8: Allow and make the most of asymmetric decentralisation arrangements

- Asymmetric decentralisation should be supported by effective vertical and horizontal co-ordination mechanisms and needs to go hand in hand with an effective equalisation system. An asymmetric decentralisation approach should be based on dialogue, transparency and agreements between all main stakeholders, and be part of a broader strategy of territorial development.
- The way asymmetric responsibilities are allocated should be explicit, mutually understood and clear for all actors. To the greatest extent possible, participation in an asymmetric arrangement should remain voluntary.

Guideline 9: Consistently improve transparency, enhance data collection and strengthen performance monitoring

- National governments should develop performance-monitoring systems to monitor decentralisation and regional development policies: they need to remain simple with a reasonable number of requirements/indicators.
- Higher level governments need to monitor subnational performance in critical service areas based upon a minimum set of standardised indicators and provide timely feedback, as well as benchmark inter-local performance in service delivery.
- Subnational governments need to be subject to higher-level regulations and fiscal rules to ensure fiscal discipline and fiscal sustainability.

Guideline 10: Strengthen national regional development policies and equalisation systems and reduce territorial disparities

- The equalisation programme must not be looked at in isolation from the broader fiscal system, especially conditional transfers. Equalisation arrangements need to be carefully designed to promote the tax and development efforts of subnational governments. Fiscal equalisation policies need in particular to be accompanied by pro-active regional development policies to offset the potential negative incentives of such systems.

Reference

OECD-UCLG (2016), *Subnational Governments Around the World: Structure and Finance*, [1] <http://www.oecd.org/regional/regional-policy/sngs-around-the-world.htm>.

Chapter 2. Understanding decentralisation systems

This chapter provides a definition of decentralisation, which covers three interdependent dimensions: political, administrative and fiscal. There can (or should) be no fiscal decentralisation without political and administrative decentralisation. The chapter clarifies the scope of the decentralisation concept, which is often confused with deconcentration for example. Finally, the chapter provides a comprehensive picture of the diversity in territorial organisation and decentralisation systems in OECD countries and beyond.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

What is decentralisation and how can it be measured? Although widespread and extensively analysed, decentralisation often has different meanings and different scopes. Several definitions exist reflecting different understandings of decentralisation, which adds to an already complex reality. This also reflects the diversity of decentralised governance systems around the world. The forms and extent of decentralisation vary greatly from one country to another – and even within the same country. Large variations exist in terms of responsibilities carried by subnational governments, of local decision-making powers, of resources available to meet the needs, including the ability to raise own-source revenues. There are also varying degrees of upward and downward accountability and varying ranges of central government control. The heterogeneity of experiences on the ground also explains the great difficulty in measuring (and assessing) decentralisation. Fiscal indicators, although useful, remain insufficient to reflect this diversity and have to be complemented by other types of institutional and governance indicators to get the facts right about decentralisation.

A multi-dimensional concept with different motivations

What is decentralisation? (and what it is not)

It is important to clarify the scope of the concept of decentralisation, since it is often confused with other concepts, such as deconcentration, devolution and delegation. The latter two are different degrees of decentralisation (Rondinelli, Nellis and Shabbir Cheema, 1983^[1]). Some countries associated the “decentralisation” concept with specific dimensions like delegation or localism, but the full decentralisation concept is broader. Overall, there are no clear-cut frontiers within decentralised governance systems. Rather, there are different degrees of decentralisation, depending on the extent of political, administrative and financial powers that have been transferred to lower levels of government, and on the balance of central-subnational relations.

Decentralisation and devolution

Devolution is a subcategory of the decentralisation concept. It is a stronger form of decentralisation as it consists of the transfer of powers from the central government to lower-level autonomous governments, which are legally constituted as separate levels of government. This was the path chosen by the United Kingdom in 1998, when the three devolved nations of Northern Ireland, Scotland and Wales were established, with a directly-elected “national assembly”/parliament and their own government. Major governing power and responsibilities were transferred to them, creating an asymmetric decentralisation system between devolved nations (with different powers) and England (no regional governments).

Decentralisation and federalisation

The next stage after devolution is federalisation, although some federal countries may be in reality quite centralised systems, with few powers exercised by subnational entities (Box 2.1).

Box 2.1. Decentralisation in federal and unitary countries

Decentralisation processes take different forms depending on the form of the state, i.e. mainly unitary or federal (including confederations), although an intermediate form of “quasi-federalism” exists in some countries. A minority of countries have a federal system of government: of the 193 UN member states, 25 are governed as federal countries (40% of the world population) and 168 are governed as unitary states (Forum of Federations: <http://www.forumfed.org/countries/>).

Federal countries may not be the most decentralised (“centralised federalism”) and some unitary states may be more decentralised than federal ones.

In addition, in federal countries, the degree of decentralisation may differ within the same country as state constitutions and legal systems for local governments may vary from one state government to another. Local government autonomy can differ greatly depending on their state (e.g. in India).

Federal countries

In federal countries (or federations), sovereignty is shared between the federal government and self-governing regional entities (the federated states), which have their own constitution in most cases (Canada is an exception), parliament and government. In a federation, the self-governing status of the component states may not be altered by a unilateral decision of the federal government.

Powers and responsibilities are assigned to the federal government and the federated states either by provision of a constitution or by judicial interpretation. In general, federal governments have exclusive and listed responsibilities such as foreign policy, defence, money and criminal justice system while federated states have extensive competencies.

In addition, in most federal countries, in particular, older ones, local governments are “creations” of the federated states and fall directly under their jurisdiction (this is not the case in all federations, e.g. Brazil where municipalities are not subordinate to the states in which they are located). Local government status, organisation, responsibilities and financing are defined by state constitutions and laws, and often differ from one state to another. Governed by state legislation, local governments do not have independent relations with the federal government. Local government reforms are decided by the federated states and not the federal power, which has no say on those matters (e.g. Australia, Canada and the United States).

Unitary countries

A unitary state is a state governed as a single power in which the central government is ultimately supreme. The unitary states are “one and indivisible” entities and sovereignty is not shared. This means that citizens are subject to the same single power throughout the national territory.

This does not preclude the existence of subnational governments, also elected directly by the population and with some political and administrative autonomy. But subnational governments exercise only the powers that the central government chooses to delegate or devolve. Unitary states are thus more or less decentralised, depending on the extent of subnational powers, responsibilities and resources, and the degree of autonomy they have over these different elements. In a unitary state, subnational units can be created and abolished and their powers may be broadened and narrowed by the central government.

Some unitary countries recognise autonomous regions and cities, which have more powers than other local governments because of geographical, historical, cultural or linguistic reasons.

Quasi-federal countries

Between these two main forms, there is an intermediate situation, that of “quasi-federal”. This status of “quasi-federation” is however not recognised as such. It applies to unitary countries with federal tendencies, i.e. having some characteristics of a federal country. Autonomous regions have less room to define and reform local government functioning than regions in federations. Basic elements of local government functions and financing are often written out in national constitutions. Even if substantial autonomy is given to autonomous regions in relation to lower tiers through primary and/or secondary legislative powers, it is often a competency that is shared with the central power. This is the case in South Africa and Spain. Spain is constitutionally a unitary state but in reality, a quasi-federation with regions having a large degree of autonomy. Organising the municipalities and provinces and changing municipal boundaries within the regional territory is the exclusive responsibility of the Autonomous Communities, but their functions and finances are decided within the framework of the national law (Article 148 of the constitution).

Sources: OECD (2017^[2]), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, <https://doi.org/10.1787/9789264272866-en>; OECD-UCLG (2016^[3]), *Subnational Governments around the World: Structure and Finance*, <http://www.oecd.org/regional/regional-policy/sngs-around-the-world.htm>.

Decentralisation and localism

Decentralisation may be approached in a broader sense such as in England (United Kingdom) with the 2011 decentralisation reform, called “localism”. However, localism should not be confused with decentralisation in its traditional meaning. Being part of the broader “big society” (vs. “big government”) project designed by the British government, the reform consisted in transferring several responsibilities from the state not only to local authorities but also to civil society, such as co-operatives, neighbourhood communities, citizen and volunteer groups, charities, social enterprises, etc., calling for a better “participatory governance” and greater community empowerment.

Decentralisation and delegation

Delegation is a form of decentralisation, but is milder than devolution. It involves transferring some decision-making and administrative authority for well-defined and specific tasks from the central government to semi-autonomous lower-level units, such as state-owned enterprises, or urban and regional development corporations (UNDP, 1999^[4]). Functions can be delegated through regulations or contracts. Semi-autonomous entities remain under the indirect control of the central government and their delegated tasks may be withdrawn in a unilateral manner.

Decentralisation and deconcentration

Decentralisation and deconcentration are sometimes used interchangeably. However, they are profoundly different. In the first case, there is a transfer of power from the central government to autonomous/elected subnational governments. In the second case, there is

a geographic displacement of power from the central government to units based in regions (territorial administration of the central government, line ministerial departments, territorial agencies, etc.). These deconcentrated state services are part of the national administration and represent the central government at the territorial level. Unlike subnational governments, deconcentrated state services are a hierarchical part of the central government level. They are not legal entities or corporate bodies. This means that deconcentrated territorial bodies do not have their own political leadership and decision-making power. They do not have their own budgets, which are typically included in the national budget. They do not raise revenues, cannot incur liabilities by borrowing on their own or engage in financial transactions and do not have their own assets. Their staff is part of the national civil service (OECD, 2018^[5]; 2017^[2]; Boex, 2011^[6]).

In practice, distinguishing between decentralisation and deconcentration systems is a challenge. In many countries, decentralised and deconcentrated systems co-exist, such as in Estonia, Finland, France, Italy, Poland and Sweden. Decentralisation does not mean that the central government cannot maintain certain functions at the local level or make them evolve and adapt to institutional changes in the governance system. Depending on the country, the role of state representatives at the territorial level in a decentralised system can, however, differ, from a representational function to a more significant role. State territorial representatives may thus be responsible for implementing national policies at the regional and local levels, ensuring that they are in line with subnational government policies. In some countries, state territorial representatives also carry out legal and fiscal oversight functions over local government actions. They may also play a co-ordination role between the different stakeholders, acting as a “pivot” of the administrative system, facilitating multi-level government dialogue on the ground, and sometimes acting as an advisor and “mediator” able to reconcile different perspectives. Finally, deconcentrated state services may also provide national public services at the territorial level.

In France for example, despite the different decentralisation laws, the national government is still very active on the local scene, playing a leading role in many areas. It has maintained, at both regional and departmental levels, a strong and powerful prefectoral administration led by a prefect (*préfet*), as well as local directorates of various ministries placed under their authority, so-called “deconcentrated services”. According to the constitution, the prefect is the direct representative of the prime minister and every minister at the departmental level, implementing government policies and their planning. The prefect is responsible for national interests, administrative supervision and compliance with laws and is in charge of public order (OECD, 2017^[2]).

In some countries, the co-existence of decentralised and deconcentrated systems may be even more accentuated, resulting in an intricate system of governance. This can be very confusing, generate tension and reduce transparency and accountability. In some countries, subnational governments are “mixed” or “dual” entities (i.e. both deconcentrated and decentralised), where the same subnational body is both a deconcentrated administration representing the central government (the executive power) and an elected autonomous self-government (the deliberative power). This is the case in Turkey and Ukraine (OECD, 2018^[5]).

So, what is decentralisation?

Decentralisation refers to the transfer of powers and responsibilities from the central government level to elected authorities at the subnational level (regional governments,

municipalities, etc.), having some degree of autonomy. Subnational governments are a legal entity directly elected by universal suffrage and having their own budget, staff and decision power. Both devolution and delegation of tasks fulfil this definition, but to different degrees.

Box 2.2. Defining decentralisation: The OECD approach

The definition of decentralisation used at the OECD is the following: “*decentralisation consists in the transfer of a range of powers, responsibilities and resources from central government to subnational governments, defined as legal entities elected by universal suffrage and having some degree of autonomy*”. Subnational governments are thus governed by political bodies (deliberative assemblies and executive bodies) and have their own assets and administrative staff. They can raise own-source revenues, such as taxes, fees and user charges and they manage their own budget. Subnational governments have a certain decision-making power, in particular, they have the right to enact and enforce general or specific resolutions and ordinances.

In this definition, decentralisation is not only about transferring powers, responsibilities and resources. It is also about reconfiguring the relationships between the central government and subnational governments towards more co-operation and co-ordination. Managing “mutual dependence” requires a profound change of structure, practice and culture within the central government itself, which represents substantial challenges for central governments around the world (Devas and Delay, 2006^[7]).

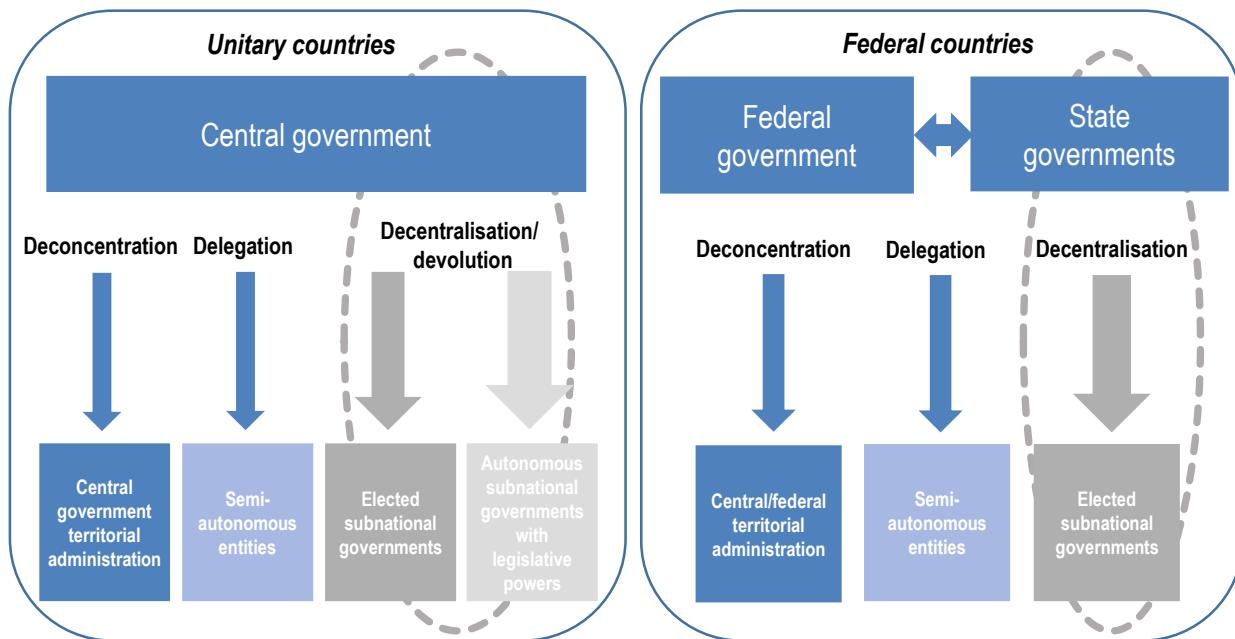
Overall, this definition is associated with the concept of Local Self-Government as defined in the European Charter of Local Self Government (1985), in UN-Habitat’s International Guidelines on Decentralisation and Strengthening of Local Authorities (2007) and, more recently, in the African Charter on the Values and Principles of Decentralisation, Local Governance and Local Development (2014).

Sources: OECD (2018^[5]), *Practical Methodological Guide for the World Observatory on Subnational Government Finance and Investment*, OECD, Paris; Boex, J. (2011^[6]), *Exploring the Measurement and Effectiveness of the Local Public Sector: Toward a Classification of Local Public Sector Finances and a Comparison of Devolved and Deconcentrated Finances*.

It is important to note that decentralisation may also be territorial or functional. Subnational governments are not always defined by their territory, i.e. the geographic boundaries within which they exercise their authority and carry out their responsibilities. While they are elected, subnational governments can also be defined just by the specific functions they perform. Examples of these “special-purpose subnational governments” are school boards, transport districts, water boards and sanitation districts. This is also known as “functional decentralisation” as opposed to “territorial decentralisation”. In the United States, for example, the Census Bureau recognises five basic types of local government, including two special purpose governments: school districts and “special district governments”. Legislative provisions for school district and special district governments are diverse and the basic pattern of these entities varies widely from state to state (OECD, 2018^[5]; Department of Commerce (U.S. Census Bureau), 2012^[8]). In Korea, the local government system comprises 17 educational offices, which are independent elected entities. In the Netherlands, Regional Water Authorities (RWAs) are

subnational government bodies and their autonomous tasks are defined in the Regional Water Authorities Act (*Waterschapswet*).

Figure 2.1. Defining decentralisation in unitary and federal countries



A multidimensional process

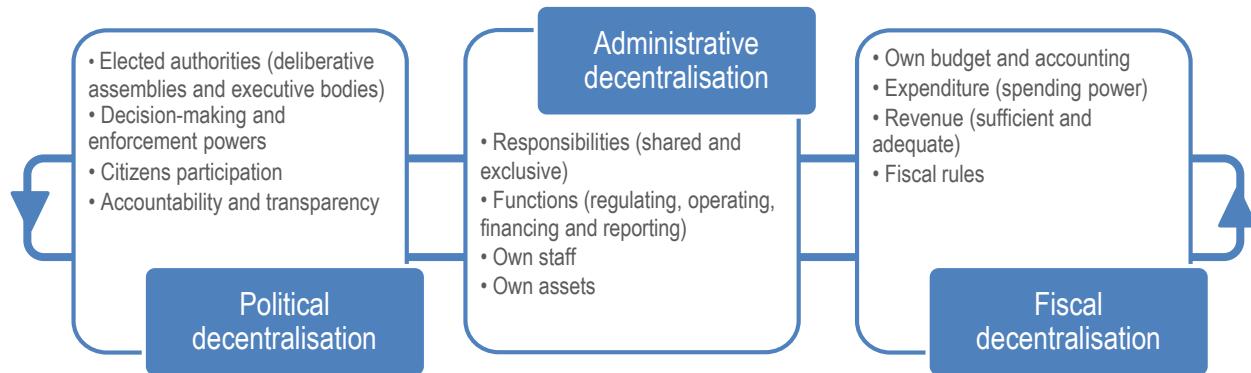
The concept of decentralisation covers three dimensions: political, administrative and fiscal. These dimensions are inter-dependent: there can (or should) be no fiscal decentralisation without political and administrative decentralisation. On the other hand, without fiscal decentralisation, political and administrative decentralisation are meaningless.

- **Political decentralisation** sets the legal basis of decentralisation. It involves a new distribution of powers according to the subsidiarity principle, between different tiers of government, with different objectives, and often with the aim of strengthening democracy. Thus, it refers to the way in which subnational administrators are selected – i.e. by appointment or by election.
- **Administrative decentralisation** involves a reorganisation and clear assignment of tasks and functions between territorial levels in order to improve the effectiveness, efficiency and transparency of national territorial administration. It generally relates to the transfer of planning, financing and management decisions on some public functions to lower levels of government.
- **Fiscal decentralisation** involves delegating taxing and spending responsibilities to subnational tiers of government. In this case, the degree of decentralisation depends on both the amount of resources delegated and the autonomy in managing such resources. For instance, autonomy is greater if local governments can decide on tax bases, tax rates and spending allocations.

In theory, these three dimensions – the distribution of powers, responsibilities and resources – are complementary and closely interconnected (Figure 2.2). Links should be

carefully considered to maximise the chance of success (Chapter 5). In practice, finding the right balance between these dimensions, and finding the right sequencing, represent major challenges to making the most of decentralisation reform. There are often one or two missing links and bad sequencing. For example, the political dimension is often insufficiently considered in some decentralisation processes, with little democratic legitimacy of subnational governments, no real accountability mechanisms or weak citizen involvement at the local level.

Figure 2.2. Political, administrative and fiscal decentralisation



Motivations for decentralisation

Decentralisation reforms are and have been implemented for a wide variety of reasons. According to Ivanayna and Shah, “hugely complex factors such as political transition in Eastern Europe, the end of colonialism, the globalisation and information revolution, assertion of basic rights of citizens by courts, divisive politics and citizens’ dissatisfaction with governance and their quest for responsive and accountable governance have been some of the contributing factors in gathering this storm” (2014^[9]). As Hooghe et al. (2016^[10]) point out, decentralisation trends are also the result of unravelling the excessive centralisation brought about by authoritarianism, nationalist state building and wars over the course of the late 20th century.

Decentralisation has also been implemented as part of state reforms to improve efficiency and quality of public services, to enhance regional and local productivity and growth, to meet fiscal consolidation objectives in the aftermath of the recent economic crisis, or in response to the institutional programmes of supranational organisations. Sometimes the motivations are not positive, as a number of countries have decentralised expenditures to shift deficit downwards. Historically, highly decentralised states were often the result of compromises required in countries with a diverse population, in part to ensure political stability.

The rising decentralisation paradigm has been driven by three main categories of factors: political drivers, economic drivers and megatrends.

Decentralisation is primarily a political choice

Engaging in a decentralising reform is ultimately a political issue and thus should be conceived and pursued as part of a larger political reform process, including, for example, territorial development reforms, reforms of the judiciary, civil service and regulatory frameworks, while also building greater accountability and reducing political instability.

In theory, decentralisation reforms promote a new conception of governance no longer based on hierarchical, top-down and vertical relations but adding a bottom-up and co-operative perspective, with more transparency, accountability and participation, in particular by citizens. The principles of local democracy and subsidiarity defined as the “precept [...] that public policy and its implementation should be assigned to the lowest level of government with the capacity to achieve the objectives” form the fundamental basis of this political choice (Oates, 1999^[11]). Decentralisation is enshrined in several national constitutions, as a fundamental principle to deepen democracy, improve the balance of power between higher and lower levels of government and ensure the effective participation of citizens in decision-making (Box 2.3).

In theory, democratisation is the basis for genuine decentralisation as decentralisation involves local elections based on pluralism and greater participation of citizens. In practice, as noted above, local democracy may be neglected as well as mechanisms allowing real involvement of the population in local affairs. Restoring or building democratic systems has been a strong incentive for decentralisation in several Asian, Latin American and Central and Eastern European countries. In Korea, decentralisation started in 1987 with the “Declaration for Democratisation” and gained momentum in 1988 with the reform of the Local Autonomy Act, followed by the organisation of the first local elections in 1991 and 1995.

Several moves towards decentralisation around the world have been motivated by this quest for more local democratic control. In Asia, achieving more democratic political outcomes has also been a strong incentive for decentralisation in several countries such as i.e. India, Indonesia or Korea with pro-democratic movements and popular mobilisation rejecting centralised autocratic governments and dictatorships. In Japan, the push for decentralisation started during the post-World War II period and was viewed as a means of achieving more democratic political outcomes. The promotion of a democratic system of local government was part of the national agenda (Chatry and Vincent, forthcoming^[12]).

The same occurred in Central and Eastern European countries in the early 1990s as a reaction to the failures of the communist centralised state over the previous four decades and in several Latin American countries where the return to democratic government was associated with decentralisation. In Africa, South Africa’s decentralisation process was an essential component of its transition from apartheid to democracy (OECD, 2008^[13]; 2011^[14]).

Decentralisation has also been a way to ensure greater political stability by preventing the disintegration of the “nation-state” in countries with strong regional identities or in reconstructing countries afflicted by conflicts, such as Ukraine (OECD, 2018^[15]).

Box 2.3. Decentralisation, a constitutional principle in several countries

Decentralisation is enshrined in several national constitutions, as a fundamental principle to deepen democracy, improve the balance of powers between higher and lower levels of government and ensure the effective participation of citizens in decision-making. In theory, this constitutional status protects subnational governments’ democratic structure and functioning from central government interference or dismissal. The constitution thus represented a safeguard against arbitrary dismissal of local government (Shah, 2017^[16]).

In Peru for example, the current decentralisation process started in 2002, when congress, driven by democratic and economic objectives, constitutionally declared Peru a “decentralised state” (Article 43 of the constitution). In Colombia, the adoption of the new constitution in 1991 significantly enhanced the process of decentralisation, declaring that “Colombia is a legally organised social state under the form of a unitary, decentralised Republic with autonomous regional entities” (OECD, 2014^[17]; 2016^[18]).

In federal countries, the federal constitution is the key to defining the rules that determine power sharing between the federal government and state governments, including fiscal arrangements. However, the federal constitution does not always take into consideration the principle of decentralisation at the local government level. In Australia for example, municipalities are not explicitly recognised by the Commonwealth Constitution, despite failed or abandoned referendums proposing constitutional recognition in 1974, 1988 and 2013. In some federations, however, the guaranteed principle of local self-government is set out in the federal constitution, e.g. Austria, Belgium, Germany, Mexico and Switzerland.

Economic motivations are also important drivers of decentralisation

The economic approach to decentralisation emphasises the improvement of local public services. The idea is that local governments have better information regarding local spending needs and preferences, and hence may better satisfy certain needs of the population, at a lower cost, than the central administration (Chapter 4).

The motivations for decentralisation may be to increase efficiency in public service provision, to better use public resources and to ensure spending effectiveness (particularly in the context of public finance crises and against a backdrop of tight budget constraints), to increase equity in access and services and tailor policies to local contexts and population needs. These have been important motivations for the support of decentralisation by multilateral organisations, such as the International Monetary Fund (IMF) and the World Bank.

Mega-trends and decentralisation

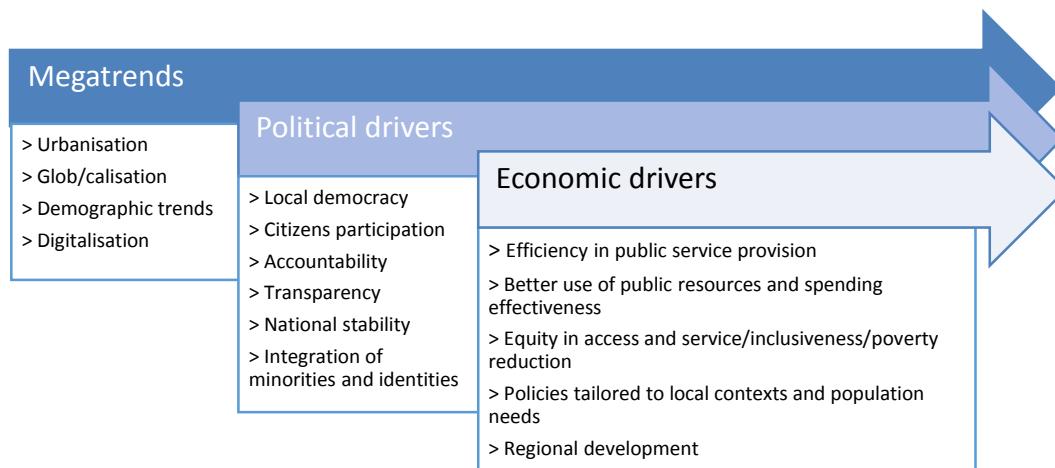
Mega-trends linked to digitalisation, the globalisation of economic activity and urbanisation, and contribute to the stronger role of subnational governments. Globalisation implies that free movement of capital between and within countries also means that cities can compete for foreign investment, a task once monopolised by central governments (Olowu, 2003^[19]). On the other hand, globalisation has provoked a revival of local cultural identities, resulting in a growing economic and political power of subnational entities. In recent years, the role of nation-states has been re-emphasised in a context of backlash against globalisation. In this context of democratic crisis in many countries, the role of local governments has also been emphasised as the closest level of government to citizens, and a way to better echo citizens’ demands and needs. Going “local” may be an answer to the forces that are “global”. The relationship between the global and the local is often referred to as “glocalisation” (Sharma, 2018^[20]).

Urbanisation is another major global trend that affects decentralisation. Today, more than 50% of the world’s population lives in cities. This figure is projected to reach 85% by 2100. Within 150 years, the urban population will have increased from less than 1 billion in 1950 to 9 billion by 2100. This period of rapid urbanisation will also have

experienced the rise of the megacity, which is defined as a metropolitan area with a total population in excess of 10 million people. In 1950, New York and Tokyo were the only megacities, but by 2014 their number had increased to 28 (OECD, 2015[21]). Cities are growing in terms of population, infrastructure and networks. They are becoming more and more complex.

The **information revolution and digitalisation** have weakened the ability of governments to control information flows. Information and communication technology (ICT) and other technological changes (blockchain, geographic information system (GIS), robotics) have also multiplied the opportunities for local governments to improve the ways they communicate and involve citizens (e-democracy and ICT-based participation, accountability and transparency in local governance). Digital tools also help governments provide local public services (e-government), manage public resources in a more efficient manner (e.g. for tax collection), improve staff capacity and management and adopt new public management models. ICT can improve the relationships between the central and subnational governments, facilitating the shift towards more decentralised governance practices.

Figure 2.3. Drivers for decentralisation



Different paths to decentralisation

Big bang vs. incremental approaches

Decentralisation reforms can be carried out in different ways: with a “big bang” approach, or step-by-step in an incremental manner or in waves (e.g. Japan with First and Second Decentralisation Promotion Reforms or France with the three “Acts on Decentralisation” from 1982 to 2015).

A “big bang” approach has two defining characteristics: i) it entails a holistic (comprehensive) and integrated approach of the three main components of decentralisation (political, administrative and fiscal); ii) it is rapidly implemented over a short period. One of the main objectives of this approach is to ensure that major measures to implement political, administrative and fiscal decentralisation will be adopted as a single package, without missing components, and that “all pieces of the puzzle fit together – i.e. the desired balance in autonomy and accountability is achieved while providing incentives for cost efficiency”. “Lightning speed” represents the best use of this

window of opportunity, as in all reforms there are losers, who can take advantage of a long period to get organised and build coalitions to circumvent or block the reform (Shah and Thompson, 2004^[22]).

However, a “big bang” approach may have some drawbacks. It can be perceived as imposed from the centre too rapidly, and at the risk of being rejected as a transplant that has not been successful. Several countries have had to step back because the decentralisation process was too rapid and strong. This was the case, for example, in Central and East European countries, as well as in many developing countries. Some decentralisation laws have never been implemented, or only partially because the agenda was too ambitious and unrealistic.

An incremental approach has some advantages. Introducing the different measures in sequence can help their implementation, as well as facilitate necessary adjustments. It can also permit a progressive upgrade of subnational government capacities, ensuring that they will be more capable of handling newly assigned responsibilities and effectively managing their resources. A gradual reform process can give more opportunities to convince and engage citizens in the process, to gain support and build greater consensus through consultations, information, public debates, etc. Finally, each step can create an impetus for further reforms from the central government, local authorities and civil society.

Pilot experiments (e.g. the free commune experiments in Denmark, Finland and Sweden) and experimental regionalisation (e.g. in Finland, France and Sweden) represent interesting approaches to decentralisation, as they can demonstrate the effectiveness of reforms and pave the way for further change on a larger scale (OECD, 2017^[21]).

Regardless of the path chosen, decentralisation is a never-ending process: modifying the governance system implies continually adapting to the new system. In an already decentralised system, decentralisation is more a process of reconfiguration of the multi-level system. It can take place without major transfers of responsibilities but more adjustments of the current system with some reassessments of functions or fiscal resources such as in France and the Netherlands.

Decentralisation is also a dynamic process. Drivers for reforms may thus vary over time depending on the political, economic, social and budgetary contexts. Some factors may be cyclical depending on economic circumstances. For example, the 2008 global crisis accelerated decentralisation reforms.

Moreover, international experiences show that design and implementation are the most challenging phases of decentralisation reform. Many decentralisation reforms have stalled, failed and been cancelled, postponed or even reversed. Others have been modified and adjusted along the way, or partially implemented. To generate expected benefits, additional and complementary reforms are often needed to correct potential deviations and improve multi-level governance mechanisms.

Top down or bottom up approaches

Decentralisation reform may be carried out in top-down or bottom-up ways. Historically, bottom-up decentralisation processes have been a dominant mode of decentralisation in North America and Northern Europe. Today, there are few examples of a bottom-up approach. Regional reform in Sweden is one of these examples, with reforms promoted by the top but by leaving the “bottom” to decide. Unlike many countries, the Swedish government did not impose a single regionalisation model, but

experimented with “pilot regions” and permitted heterogeneity across regions in terms of governance bodies and regional responsibilities. This approach towards regionalisation has created scope for learning, fine-tuning the reform and fostering consensus (OECD, 2017_[23]). A top-down approach, through which the national government decides to shift part of its responsibilities downwards, is more frequent and has been the dominant process of decentralisation followed in Southern Europe and all developing and transition countries (Shah and Thompson, 2004_[22]). In these countries, however, there are some cases where decentralisation has been pushed forward by local and regional elites as a strategy for mobilising and maintaining regional power bases (Devas and Delay, 2006_[7]).

In the case of the top-down approaches, the reasons to decentralise were far from political or economic (local democracy, accountability, efficiency, etc.) but more focused on short-term considerations (political calculations, shifting responsibility for unpopular measures, moving fiscal burdens to the bottom). This was, for example, the case in some countries during the recent financial crisis, when some social tasks were decentralised without real fiscal compensation, hence forcing local governments to play a “social buffer” role (“decentralisation of the crisis”). Most of the time, this type of approach results in an incomplete decentralisation process, with either the political or the fiscal dimensions missing.

Decentralisation reforms have also been strongly promoted (or even imposed) by the international community (e.g. multilateral banks, international agencies and donors). In 2008-09, the support to Greece from the European Central Bank, the European Commission and the IMF included territorial and institutional reforms (e.g. the Kallikratis reform). The goal was to streamline territorial organisation and to reduce and optimise public spending by reinforcing decentralisation. Decentralisation has also been advocated in Africa and Asia by multilateral banks, international agencies and donors concerned by the failure of central governments to efficiently deliver services and address poverty. Endorsing the economic arguments for decentralisation, sometimes coincided with the liberal agenda of reducing the role of the central government under the banner of “good governance”, but with mixed results, as pre-conditions for effective decentralisation were not met (Devas and Delay, 2006_[7]; Shah and Thompson, 2004_[22]) (see Chapter 4).

Decentralisation often goes hand in hand with other reforms

Decentralisation is not only a public sector reform. It should be viewed in a comprehensive and “polycentric” way, including the observation of interactions between public entities and private stakeholders (profit or non-profit), in particular citizens and businesses (Ostrom, 2010_[24]). Decentralisation reforms are often accompanied by other types of multi-level governance reforms, notably territorial and public management reforms (OECD, 2017_[2]). These three categories of reform are often interrelated and complementary (Box 2.4 and Figure 2.4).

A territorial reform can be partly driven by a decentralisation reform. An increasing number of tasks transferred to local governments may put pressure to increase their size and capacity in order to cope with the additional responsibilities. This is the case with the current Ukrainian reform, where municipal amalgamation represents a first step and “a platform for decentralisation” (OECD, 2018_[15]). To receive new responsibilities and funding, municipalities have to merge into unified territorial communities.

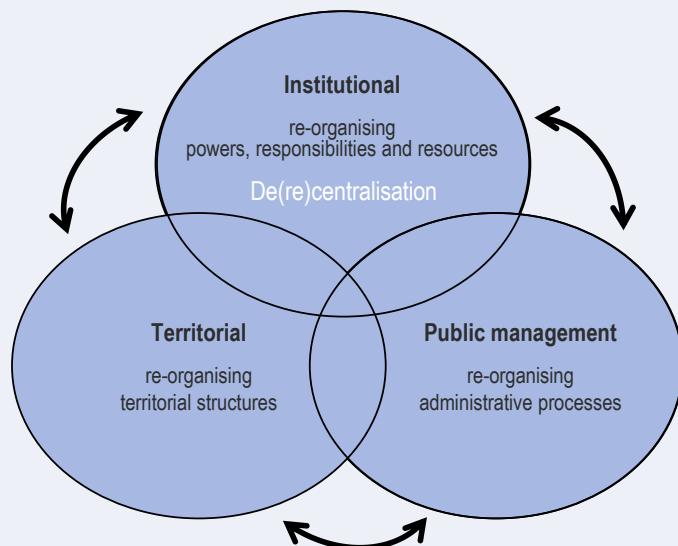
Box 2.4. Institutional, territorial and management reforms: Three main categories of multi-level governance reforms

Institutional reforms aim at re-organising powers and responsibilities across levels of government. They thus include either decentralisation or recentralisation processes, consisting in the transfer of tasks, assets, human and fiscal means from the central government to subnational governments and vice versa, and redefining relationships across levels of government.

Territorial reforms aim at re-organising territorial structures, often by updating and “re-scaling” regional and local government administrative areas, hence modifying their geographic boundaries. Their goal is to reach a better match between the size of subnational structures and their responsibilities and functions.

Public management reforms aim at re-organising subnational government administrative and executive processes, including human resources management, financial management, e-government, etc.

Figure 2.4. Institutional, territorial and management reforms are closely interrelated



Source: OECD (2017_[2]), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, <https://doi.org/10.1787/9789264272866-en>.

The reverse is also true, i.e. a decentralisation reform partly driven by a territorial reform. In France, for example, the 2015 regional reform was first and foremost a reform consisting of amalgamating 22 existing regions into 13 regions to build larger and stronger regions. The rationale behind the reform was to generate savings and reach efficiency gains, build more homogenous regions from a socio-economic point of view and grant them sufficient recognition to engage in international and European co-operation. Eight months later, the law on the “Delimitation of Regions” was followed by another law that modified the allocation of responsibilities across levels of government, including the strengthening of regional responsibilities.

Finally, public management reforms may also be introduced in relation to institutional and/or territorial reforms, either simultaneously or successively, as they provide the opportunity to review and modernise management and governance processes.

Measuring decentralisation is a challenge

Competing definitions of decentralisation, its multi-dimensional nature and the heterogeneity of experiences on the ground explain the great difficulty in actually measuring decentralisation. Fiscal indicators are useful in providing a macroeconomic view of decentralisation but remain partial – only focusing on fiscal aspects – and may lead to a distorted interpretation of reality when they are not complemented by an analysis that goes beyond such indicators. Although crucial, fiscal indicators are insufficient to get the facts right about decentralisation, they must be completed by complementary approaches, including quantitative and qualitative indicators to determine the real magnitude of decentralisation, to correctly grasp the trends at play and to accurately assess the impact and the outcomes of decentralisation.

Subnational fiscal autonomy

The concept of fiscal autonomy is not easy to assess. Fiscal autonomy concerns both sides of the budget, expenditure and revenues. Spending power may be limited, either because subnational governments act as “paying agent”, carrying out a centrally defined spending agenda with little or no decision-making power or room for manoeuvre, or because regulations, norms and standards or budgetary rules impose ceilings or compulsory expenditures. Revenue autonomy is also a complex issue and goes beyond tax autonomy. It depends, for example, on the extent of discretion in intergovernmental transfers (from earmarked and conditional transfers to general-purpose grants based on a formula), on the type of taxes (from shared taxes with no or little taxing power to own-source taxes on which subnational governments have a certain power to set rates and bases), on the ability to set the level of tariffs, user charges or fees or on the possibility of raising revenues from local assets.

Fiscal autonomy also includes the capacity to access external funding (e.g. by borrowing, engaging in public-private partnerships). It also includes the capacity to manage budgets, to hire and fire staff, to choose the modes for delivering local public services as well as control and reporting mechanisms, performance assessments, etc. Finally, equalisation instruments may also limit the fiscal autonomy of subnational governments, especially horizontal equalisation (from wealthy jurisdictions to the poorer ones, also called the “Robin Hood principle”).

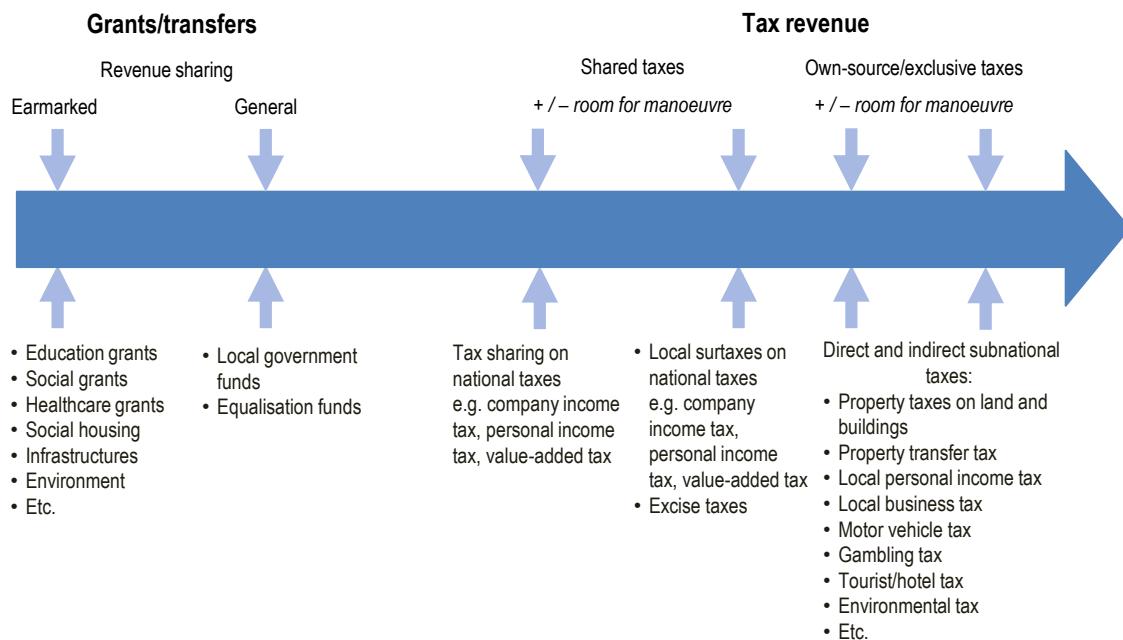
Revenue autonomy is at the core of decentralisation. The proportion of grants versus tax revenues in subnational revenue and the power on these sources of revenue is key. A particular challenge is to set up the vertical distribution of tax revenues among levels of government and to determine which taxes to assign to subnational governments, under what criteria, and with which degree of discretionary power over tax bases and rates.

It is important to underline that there are no clear-cut frontiers between the different sources of revenue. Rather, it more of a continuum with fuzzy delimitations, ranging from very little autonomy for earmarked grants (allocated for specific tasks or projects and coming with guidelines, stricter controls and reporting obligations) to high autonomy for own-source taxes when subnational governments have the power to set rates and bases (e.g. typically property taxes) (Figure 2.5). Even in this case, the ability to act on rates

and bases may also be regulated and restricted, reducing subnational government taxation power (e.g. through the imposition of caps, exemptions imposed by the central government, etc.).

Between these two extremes, there are various gradations from revenue sharing (general grants), tax sharing, local surtax (or surcharges) on national taxes such as personal income tax, corporate income tax or value-added-tax to tax revenue generation with more or less room for manoeuvre in terms of rates and bases (caps on rate for example or limited exemptions).

Figure 2.5. The continuum of subnational tax autonomy



The need to go beyond fiscal indicators to measure decentralisation

Fiscal indicators such as subnational shares in spending, revenue, and investment tell an important story about where money is spent, but do not fully capture all aspects of spending and revenue power. In particular, fiscal indicators can be misleading because decentralised expenditure can just be delegated expenditure made on behalf of the central government. In many countries, subnational governments have little spending autonomy, especially when they are the “paying agent” for the central government, for example to pay the teachers’ salaries or distribute social and welfare benefits to households, with no or little choice of how expenses are allocated (e.g. in Denmark in the social sector). Often, subnational governments do not have full autonomy and decision-making authority in their fields of responsibility, functioning sometimes more as agencies funded and regulated by the central government rather than as independent policymakers. Nordic countries, for example, are in practice likely to be less decentralised than they might appear from fiscal indicators (e.g. Denmark, Finland, Sweden). In many countries, a significant share of public spending takes place at lower levels of government, but this information on its own paints an incomplete picture of what subnational governments can actually do, autonomously, to affect the lives of those living in their territory.

Fiscal matters are one dimension of multilevel governance and they need to be complemented by other indicators to give a full picture of decentralisation systems. Several measures exist that address other dimensions as well.¹ The Regional Authority Index (RAI) and the Local Autonomy Index (LAI) are comprehensive attempts to measure the real degree of power of subnational governments – beyond fiscal indicators. They provide a picture of multi-level governance, which is closer to reality than what is seen when looking at fiscal indicators only.

The Regional Authority Index takes the region as the unit of analysis and covers 81 countries along 10 dimensions annually from 1950-2010 (Hooghe, Marks and Schakel, 2010^[25]; Hooghe et al., 2016^[10]). The RAI distinguishes between tiers of intermediate governance (see also Chapter 3).² The ten dimensions of the RAI include notably fiscal autonomy, borrowing autonomy, but also lawmaking, executive control (see Annex A). The Local Autonomy Index (LAI) follows, where applicable, the methodology of the RAI. The Local Autonomy Index (LAI) was developed for 39 European countries and it reports changes between 1990 and 2014.

Box 2.5. The Regional Authority Index and the Local Autonomy Index

The Regional Authority Index (RAI) tracks regional authority on an annual basis from 1950 to 2010 in 81 countries. The sample consists of all European Union member states, all OECD member states, all Latin American countries, 10 countries in Europe beyond the EU and 11 in the Pacific and South-East Asia. The unit of analysis is the individual region/regional tier. The dataset encompasses subnational government levels with an average population of 150 000 or more. Regions with a special autonomous statute or asymmetrical arrangements are also coded separately.

Regional authority is measured along ten dimensions: institutional depth, policy scope, fiscal autonomy, borrowing autonomy, representation, lawmaking, executive control, fiscal control, borrowing control and constitutional reform.

Primary sources (constitutions, legislation) are triangulated with secondary literature and consultation of country experts to achieve reliable and valid estimates. A regional data set contains annual scores for regional governments or tiers and a country data set aggregates these scores to the country level.

The RAI has proven to have a solid convergent content validity and has been used as a regionalisation or a multi-dimensional decentralisation measurement.

For the LAI, some adaptations had to be made to capture the specific characteristics of local government. For example, it is not appropriate to speak about non-deconcentrated local government or the endowment of an independent legislature because these aspects are parts of local self-government by definition (see the European Charter of Local Self-Government). Furthermore, more dimensions have been taken into account and some revisions of variables have been made (Andreas Ladner, 2016^[26]).

Sources: Hooghe, L. et al. (2016^[10]), *Measuring Regional Authority: A Postfunctionalist Theory of Governance*, Oxford University Press, Oxford; Regional Authority Index, <http://garymarks.web.unc.edu/data/regional-authority/>.

Ivanyna and Shah have also developed comprehensive measures of the degree of decision-making at the local level, i.e. the level of government closest to the people (2014^[9]). The dataset developed by Ivanyna and Shah covers 182 countries, and it captures institutional dimensions of political, fiscal and administrative autonomy enjoyed by local governments. These dimensions are then aggregated to develop a “decentralisation index” and are then adjusted for heterogeneity to develop a “government closeness index”. The analysis conducted on the basis of the index shows that decentralised local governance as measured by the government closeness index is associated with higher human development, lower corruption and higher growth.

A set of subnational spending indicators was developed in 2010 by the OECD Network on Fiscal Relations across Levels of Government, based on a detailed assessment of institutional, regulatory and administrative control which central government exerts over various subnational government policy areas (Bach, Blöchliger and Wallau, 2009^[27]). Five categories were established: policy, budget, input, output and monitoring and evaluation autonomy. They allow a better assessment of the differences between spending indicators, and the degree of authority of subnational governments in these selected policy areas.

Highly diversified decentralisation systems in the OECD and around the world

Subnational governments in the OECD

In 2018, there were, in OECD countries around 136 800 subnational governments, in 9 federal and quasi-federal countries and 26 unitary states. The number of subnational governments varies greatly across countries (Annex B). This number is not necessarily related to population size or density: France and the United States have approximately the same number of subnational governments. The same applies to the Czech Republic (or Switzerland) and Mexico, which have roughly the same number of subnational governments, although the Czech Republic is 11 times less populated than Mexico (and Switzerland 15 times).

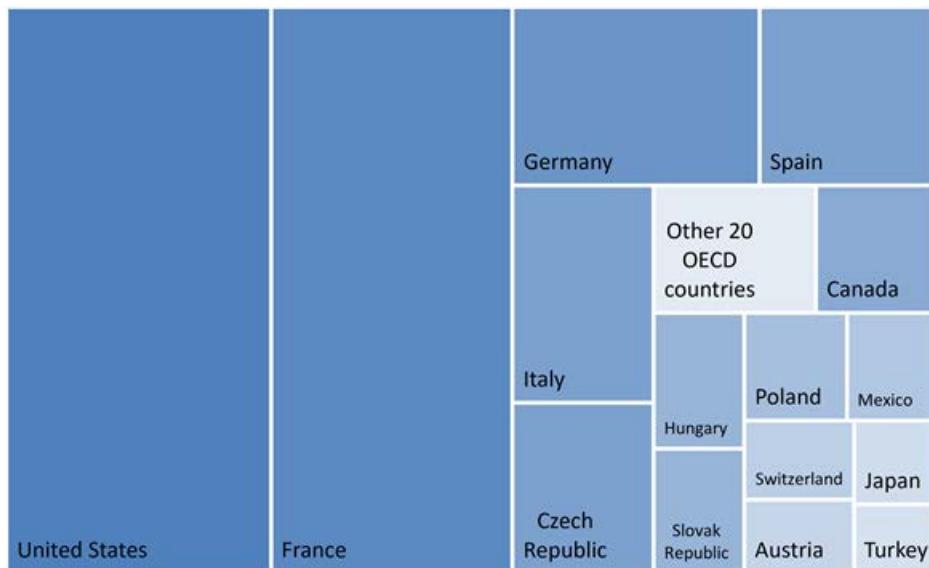
In total, France and the US account for 54% of all subnational governments in the OECD, followed by Germany, Spain and Italy with the next largest number of subnational governments. Twenty OECD countries account for less than 4% of all OECD subnational governments (Figure 2.6).

The high number of subnational governments reflects the high number of municipalities. There are around 132 300 municipalities in the OECD, 4 000 intermediate governments and 519 regions and state governments. Nine countries in the OECD have only one level of subnational governments, the one of municipalities. These countries are mostly small in terms of population and/or areas. Taken together, they represent 2.1% of the OECD total area and 2.7% of its population. Nineteen countries have two levels (municipalities and regions/states) and seven countries have three levels (municipalities, regions/states and an intermediate level between the two, e.g. *départements* in France, provinces in Spain, *Kreis* in Germany, counties in the United States). Italy belonged to this group until the 2014-15 reform, which abolished the provinces as directly elected subnational governments. Three-layer countries represent one-third of the OECD total area and half of its population.

Some OECD countries are characterised by particularly high municipal fragmentation, which makes the provision of local services inefficient and raises issues of equity in access to services, including varying quality. Municipal sizes vary greatly from one

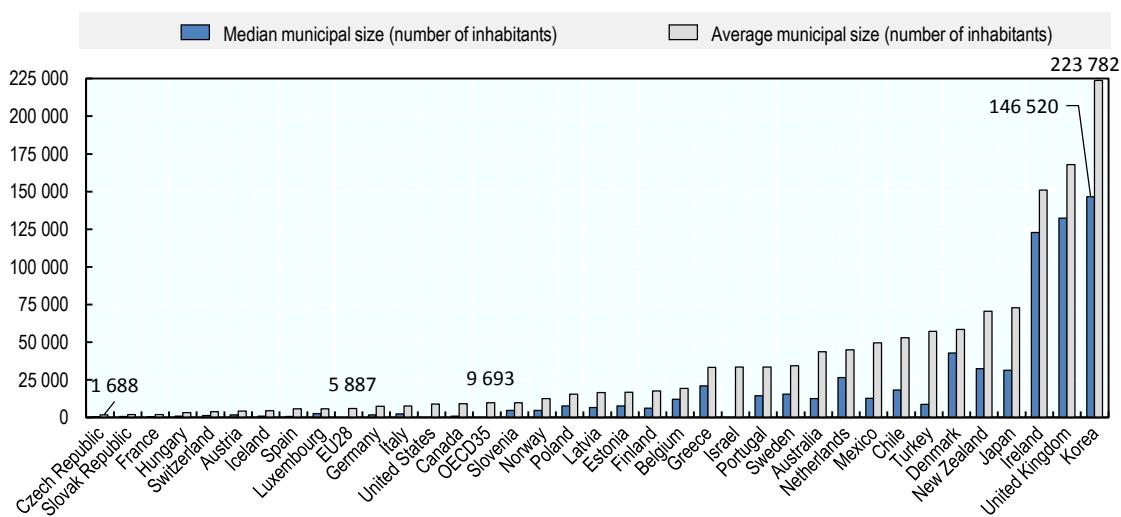
country to another as well as within one country. On average, the municipal size amounted to around 9 700 inhabitants in the OECD in 2017-18 (Figure 2.7), ranging from around 1 700 inhabitants in the Czech Republic to almost 225 000 inhabitants in Korea.

Figure 2.6. Number of subnational governments by country in the OECD in 2017-18



Source: OECD elaboration based on OECD (2018_[28]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

Figure 2.7. Average and median municipal size in the OECD and the EU in 2017-18

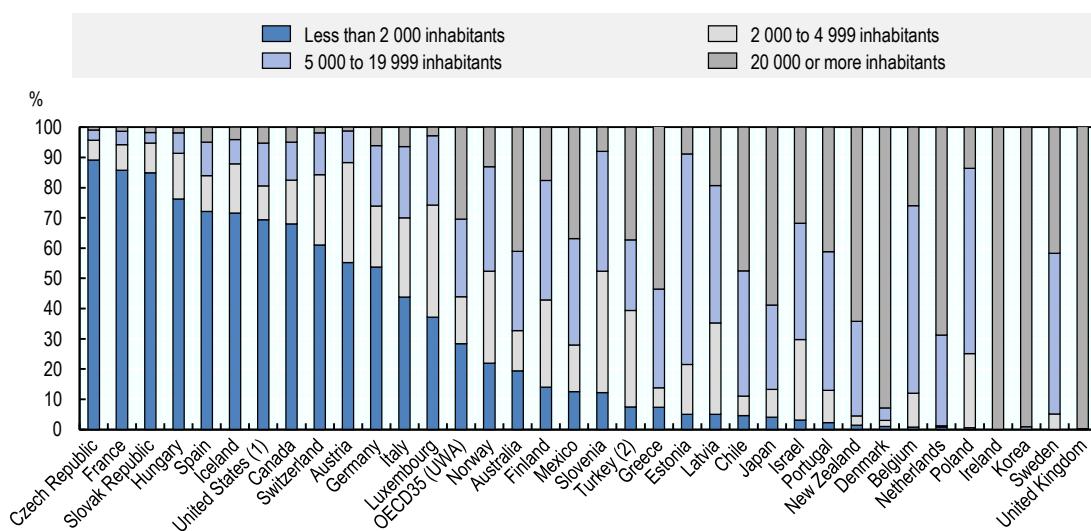


Source: OECD elaboration based on OECD (2018_[28]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

Most countries with large municipalities have a structured sub-municipal level that allows them to maintain a certain level of proximity and local democracy despite large municipal governments. These are for example characterised by civil “parish-type” municipal administrative subdivisions under public law and may have their own delegated budget and elected representatives (council, mayor). These may even have their own staff but do not have full local autonomy, as they are creatures of the municipality³. Such networks of localities exist in a variety of countries including Greece, Ireland, Korea, the Netherlands, New Zealand, Portugal and Slovenia.

Not only are municipal average and median sizes low in several OECD countries, but a fair number countries may also have a high proportion of very small municipalities, either in terms of population, geographic area, or both. In the Czech Republic, France and the Slovak Republic, more than 85% of municipalities have fewer than 2 000 inhabitants (Figure 2.8).

Figure 2.8. Municipalities by population size class in the OECD



1. Size-classes are slightly different: less than 2 499 inhabitants, 2 500 to 4 999, 5 000 to 24 999, 25 000 or more.
2. Metropolitan municipalities are not included to avoid double counting.

Source: OECD elaboration based on OECD (2018[28]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

Diversity in subnational government spending responsibilities

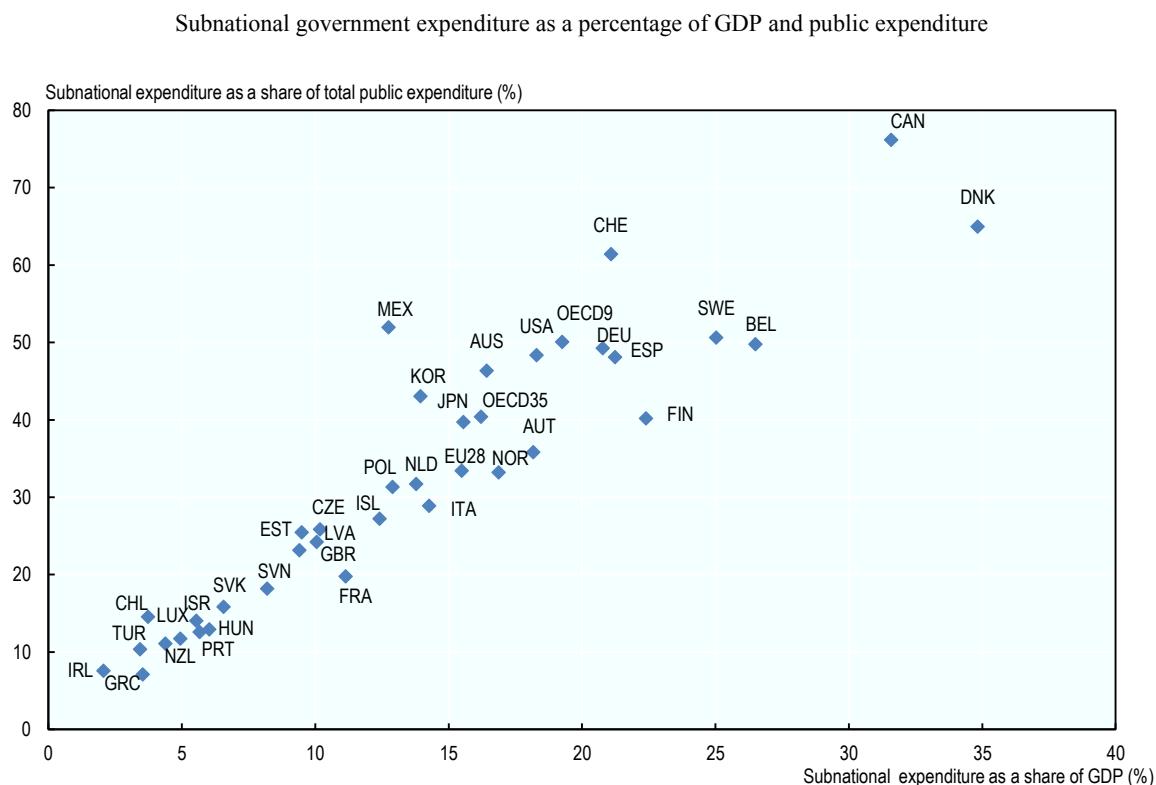
To get a sense of decentralisation systems, it is useful to see what fiscal indicators say in terms of subnational expenditures in the different policy areas. OECD countries have different levels of decentralisation measured either by the degree of spending decentralisation or by the tax revenues perceived by subnational governments.

Subnational governments represent a large share of public spending on average in the OECD. In 2016, subnational government expenditure accounted for 16.2% of gross domestic product (GDP) and 40.4% of public spending in the OECD. The importance of subnational governments in the economy is particularly evident when considering their role as employers. The lion’s share of public sector workers is employed by the

subnational level, with 63% of government personnel expenditure undertaken by subnational governments. Subnational governments also play a key role in public markets through their purchases of goods and services for intermediate consumption and commissioning of public works. In 2016, they accounted for 49.5% of public procurement in the OECD.

Subnational government spending responsibilities vary from one country to another, depending on whether the country is federal or unitary, its size and territorial organisation, the degree of decentralisation and the nature of responsibilities carried out in certain sectors. In fact, some spending areas, such as education, social services and health, generate a greater volume of expenses than others because they involve significant current expenditure (e.g. social benefits, teacher and social worker salaries, and hospital staff wages). When subnational governments are in charge of these responsibilities, this automatically results in a high level of expenditure. Yet, this does not necessarily mean a high level of decentralisation. In some cases, such expenditures are delegated from the central government. Subnational government expenditure can also be constrained by regulations, norms and standards, or budget balance targets.

Figure 2.9. Subnational governments are key policy actors across OECD, 2016



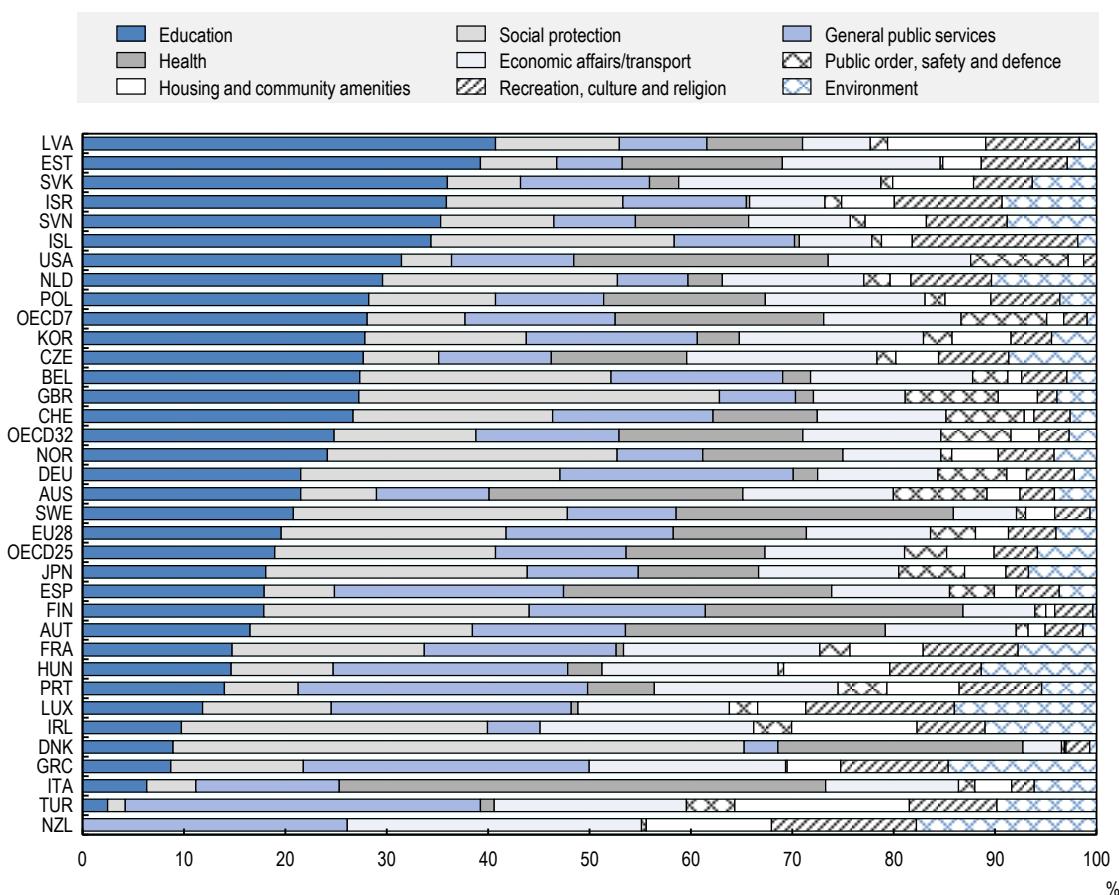
Note: 2015 data for Mexico, New Zealand and Turkey. IMF data for Australia and Chile.

Source: OECD elaboration based on OECD (2018^[28]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

In federal countries, subnational expenditures are, in most cases, higher than in unitary countries because they combine those of the state and local governments. Canada stands out. Some unitary countries have a high level of subnational spending as well, such as Denmark, Finland and Sweden. By contrast, in countries where local governments have limited competencies, the level of spending is also limited (e.g. Greece, Ireland, Luxembourg, New Zealand and Turkey).

The breakdown of subnational expenditure by economic function provides a measure of the subnational government role in several areas (Figure 2.10). Education represents the largest spending area, accounting for 25% of subnational government expenditure on average in the 32 OECD (4% of GDP). Health is the second highest budget item, accounting for 18% of subnational expenditure (2.9% of GDP). General public services (administration) and social protection sectors are the third largest subnational budget item, both representing 14% of subnational spending (2.3% of GDP). Just after social protection comes economic affairs sector (primarily transport, but also commercial and labour affairs, economic interventions, agriculture, energy, mining, manufacturing, construction, etc.). This spending area represents 13.6% of subnational spending in the OECD on average (2.2% of GDP).

Figure 2.10. Subnational government expenditure by area, 2016

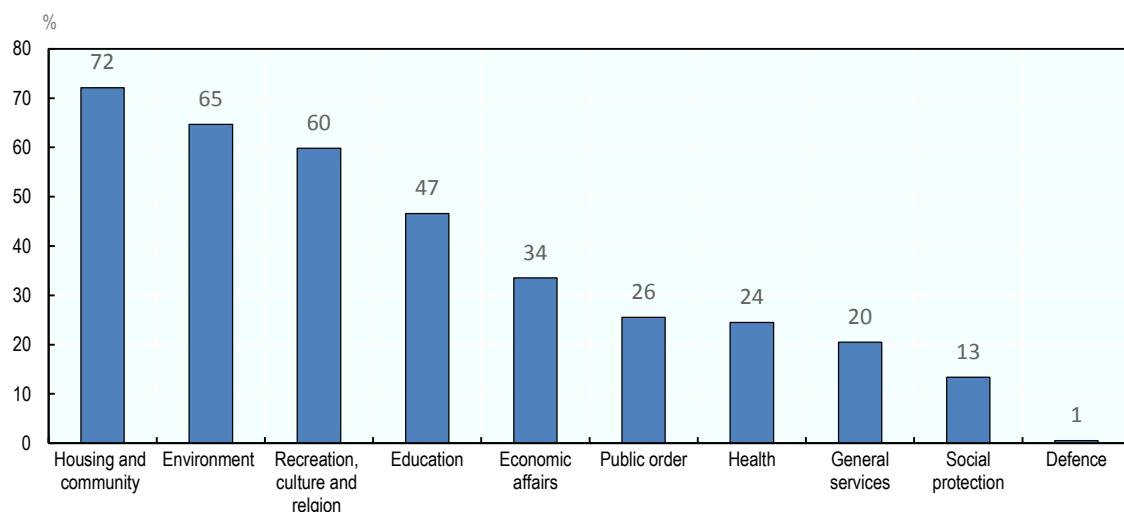


Note: Estimates from the IMF for New Zealand and Turkey. No data for Canada, Chile and Mexico.

Source: OECD elaboration based on OECD (2018[28]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

It is also interesting to look at the spending responsibilities across levels of government (Figure 2.9). In some areas, subnational governments are the main actors, accounting for more than 60% of public spending (housing and community amenities which include distribution of potable water, public lighting, waste collection; environment; recreation, culture and religion). In other areas, spending responsibilities are more likely to be shared with the central government. This is the case for education, economic affairs and transport, public order, health and social protection, although these sectors account for the largest shares of subnational expenditure. These averages mask wide variations from one country to another (OECD, 2018^[29]).

Figure 2.11. Subnational expenditure as a share of total public expenditure by economic function



Note: No data for Canada, Chile and Mexico. For the United States, data showed in the function “housing and community amenities” include the “environment protection” function data. OECD average is unweighted. The total of public spending is non-consolidated.

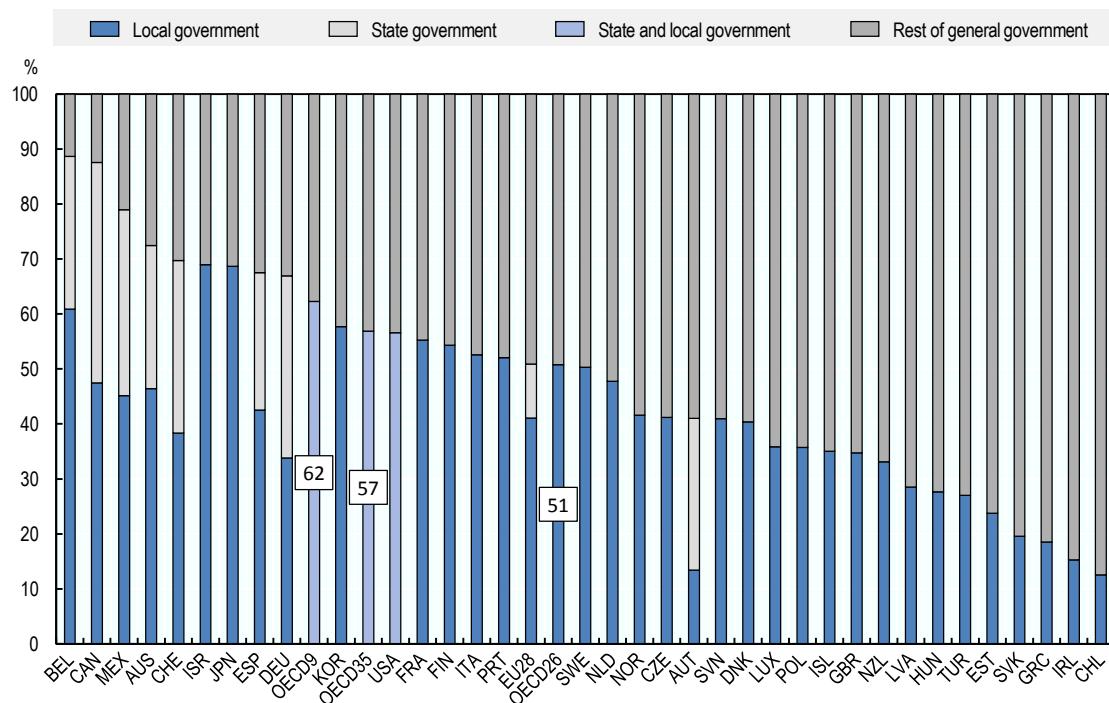
Source: OECD elaboration based on OECD (2018^[29]), *OECD Regions and Cities at a Glance 2018*, https://doi.org/10.1787/reg_cit_glance-2018-en.

Diversity in subnational public investment

In most OECD countries, subnational governments play a key role in public investment. Subnational investment represented 56.9% of public investment in 2016. However, national situations are very diverse. This ratio tends to be higher in federal countries than in unitary countries, although the role of subnational governments in unitary countries such as France, Israel, Japan and Korea is particularly high.

Figure 2.12. Subnational governments are key public investors across OECD, 2016

Subnational government investment as a percentage public investment



Note: 2015 data for Mexico, New Zealand and Turkey. IMF data for Australia and Chile.

Source: OECD elaboration based on OECD (2018[28]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

A diversity of financing models

There is a large variety of financing systems for subnational governments. Subnational funding models depend on a mix of criteria, including whether the state is federal or unitary, the degree and the type of decentralisation spending as well as economic, historical and cultural factors. The structure of subnational government revenue also varies greatly across countries (Figure 2.13).

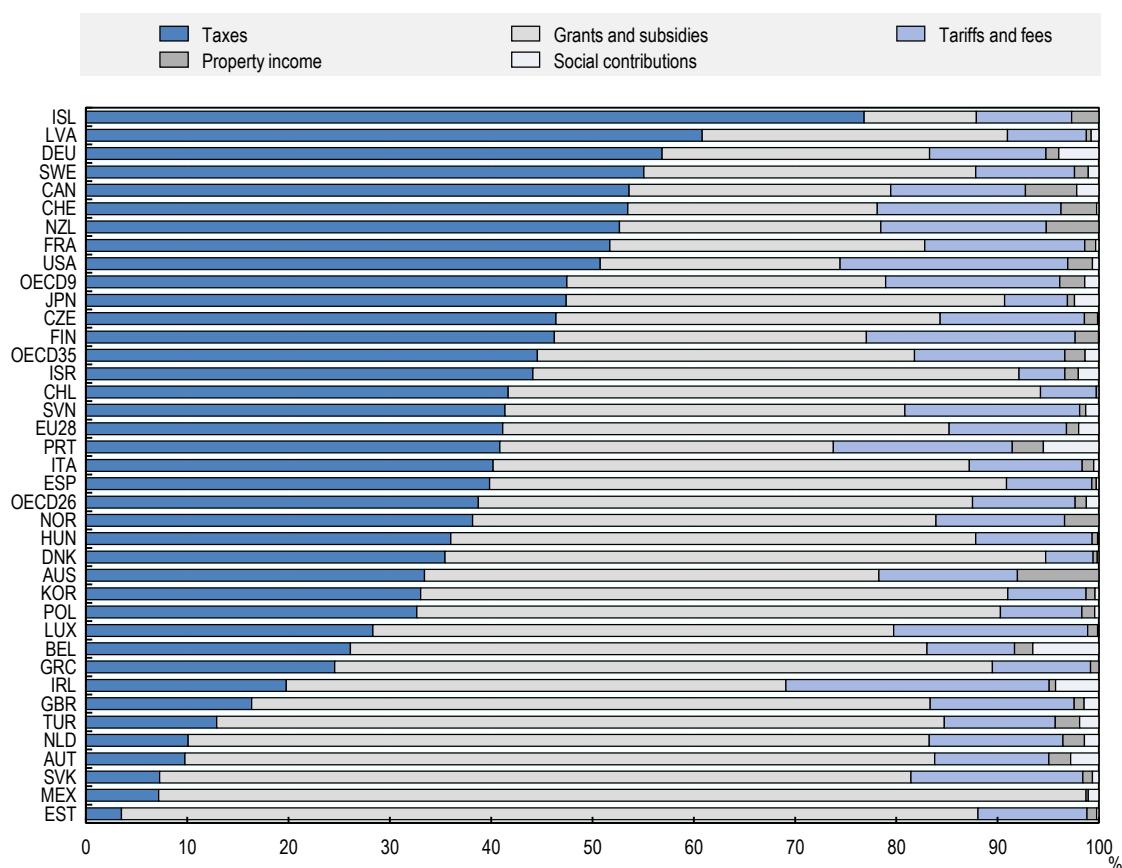
In 2016, taxes represent the main source of revenues for subnational governments in the OECD (45%) before grants and subsidies (37%). Revenue derived from local public service charges (tariffs and fees), property income (sale and operation of physical and financial assets) and social contributions represented 15%, 2% and 1% of subnational government revenue respectively.

The share of tax revenue in subnational revenue varies greatly from one country to another. It is a particularly significant share in some federal countries, where tax revenue frequently derives from own-source taxation and tax-sharing arrangements between the federal government and state governments, as well as local governments in some cases. In the US, there is no tax sharing system between the federal and the subnational governments. In two other federal countries, Austria and Mexico, tax revenue – regardless of whether from tax sharing or own-sources – contributed less than 10% of subnational revenue in 2016. In some unitary countries, tax revenue made up more than 52% of local revenue in 2016 (e.g. in France, Iceland, Latvia, New Zealand and Sweden).

At the opposite end, taxes amounted to less than 15% of local revenue in Estonia, the Netherlands, the Slovak Republic and Turkey.

The share of tax revenue is not an indication of tax autonomy, which depends on many factors – such as the right to introduce or to abolish a tax, to set tax rates, to define the tax base, or to grant tax allowances or relief to individuals and firms.

Figure 2.13. The structure of subnational government revenue varies greatly across countries, 2016



Note: Tax revenues in this figure exclude revenues from social security contributions, which are included in the OECD definition of taxes. Please see Section A2 of the OECD Interpretative Guide for further information. OECD26 and OECD9 respectively refer to unitary countries and federal countries.

Source: OECD elaboration based on OECD (2018[28]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

Countries can be grouped into four families based on their degree of subnational spending and tax level characteristics, which cut across federal versus unitary distinctions (Table 2.1).

Table 2.1. Categories of fiscal decentralisation by subnational expenditure and tax revenue

Spending decentralisation (as % of GDP and % of total public expenditure)		Tax revenue decentralisation (as % of GDP and % of total public tax revenue)	
Highly decentralised spending	Australia, Belgium, Canada, Denmark, Finland, Germany, Japan, Spain, Sweden, Switzerland, United States	High tax revenues	Canada, Denmark, Finland, Germany, Iceland, Japan, Spain, Sweden, Switzerland, United States
Medium decentralised spending	Austria, Colombia, Czech Republic, Estonia, France, Iceland, Italy, Korea, Latvia, Mexico, Netherlands, Norway, Poland, Slovenia, United Kingdom	Medium tax revenues	Australia, Belgium, Colombia, Czech Republic, France, Italy, Korea, Latvia, Norway, Poland, Slovenia
Low decentralised spending	Chile, Greece, Hungary, Ireland, Israel, Luxembourg, New Zealand, Portugal, Slovak Republic, Turkey	Low tax revenues	Austria, Chile, Estonia, Greece, Hungary, Ireland, Israel, Luxembourg, Mexico, New Zealand, Netherlands, Portugal, Slovak Republic, Turkey, United Kingdom

Sources: Allain-Dupré, D. (2018_[30]), “Assigning responsibilities across levels of government: Trends, challenges and guidelines for policy-makers”, <https://doi.org/10.1787/f0944eae-en>; OECD (2017_[31]), *Subnational Governments in the OECD: Key Data (brochure and database)*, OECD, Paris.

Table 2.2. Types of countries by level of decentralisation when measured by fiscal indicators

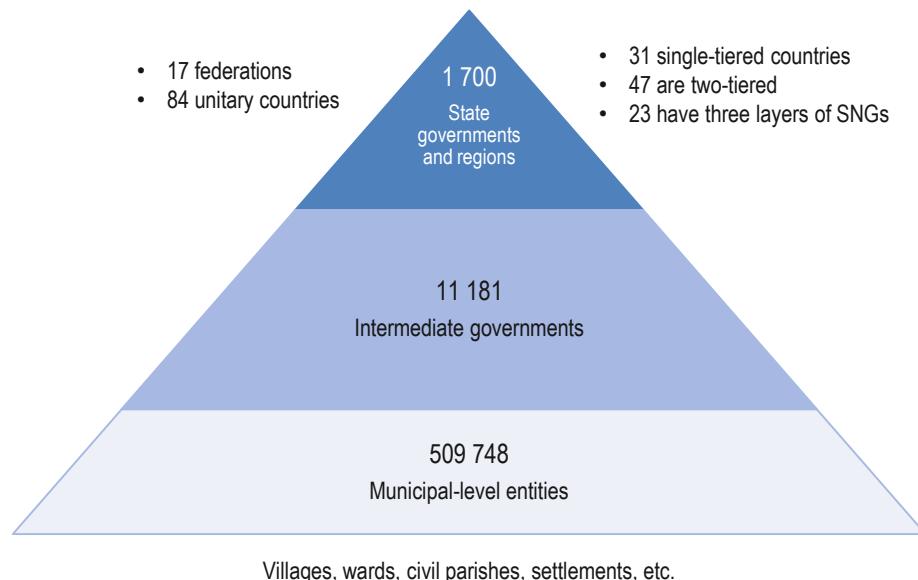
Most decentralised (Type 1) to most centralised (Type 4)

Type 1	High decentralised spending and high tax revenues	Australia, Belgium, Canada, Denmark, Finland, Germany, Japan, Spain, Sweden, Switzerland, United States
Type 2	Medium decentralised spending and medium tax revenues	Czech Republic, France, Iceland, Italy, Latvia, Norway, Poland, Slovenia, Korea
Type 3	Medium decentralised spending and low tax revenues	Austria, Estonia, Mexico, Netherlands, United Kingdom
Type 4	Low decentralised spending and low tax revenues	Chile, Greece, Hungary, Ireland, Israel, Luxembourg, New Zealand, Portugal, Slovak Republic, Turkey

Sources: Allain-Dupré, D. (2018_[30]), “Assigning responsibilities across levels of government: Trends, challenges and guidelines for policy-makers”, <https://doi.org/10.1787/f0944eae-en>; OECD (2017_[31]), *Subnational Governments in the OECD: Key Data (brochure and database)*, OECD, Paris.

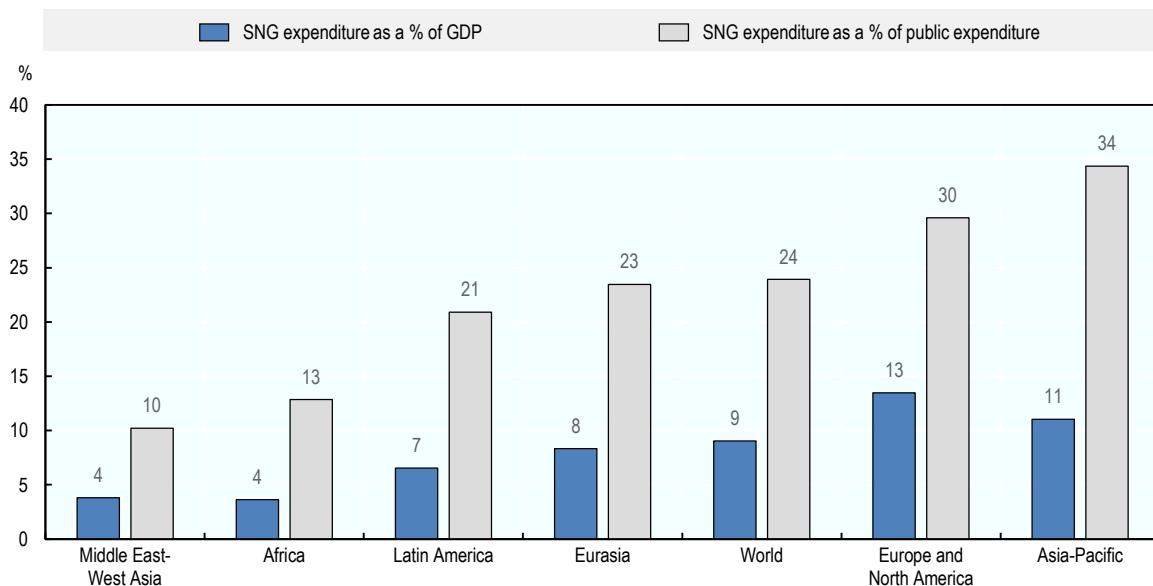
Subnational governments around the world

At the global level, the OECD-UCLG World Observatory on Subnational Government Finance and Investment identified approximately 523 000 subnational governments in 100 countries around the world, representing almost 6 billion inhabitants, i.e. 82% of world population and around 88% of the world GDP. There is a significant amount of diversity in subnational structures, which can affect how countries design and implement decentralisation reforms (Figure 2.14).

Figure 2.14. Subnational governments (SNGs) at the global level

Source: OECD elaboration based on OECD-UCLG (2016^[3]), *Subnational Governments around the World: Structure and Finance*, <http://www.oecd.org/regional/regional-policy/sngs-around-the-world.htm>.

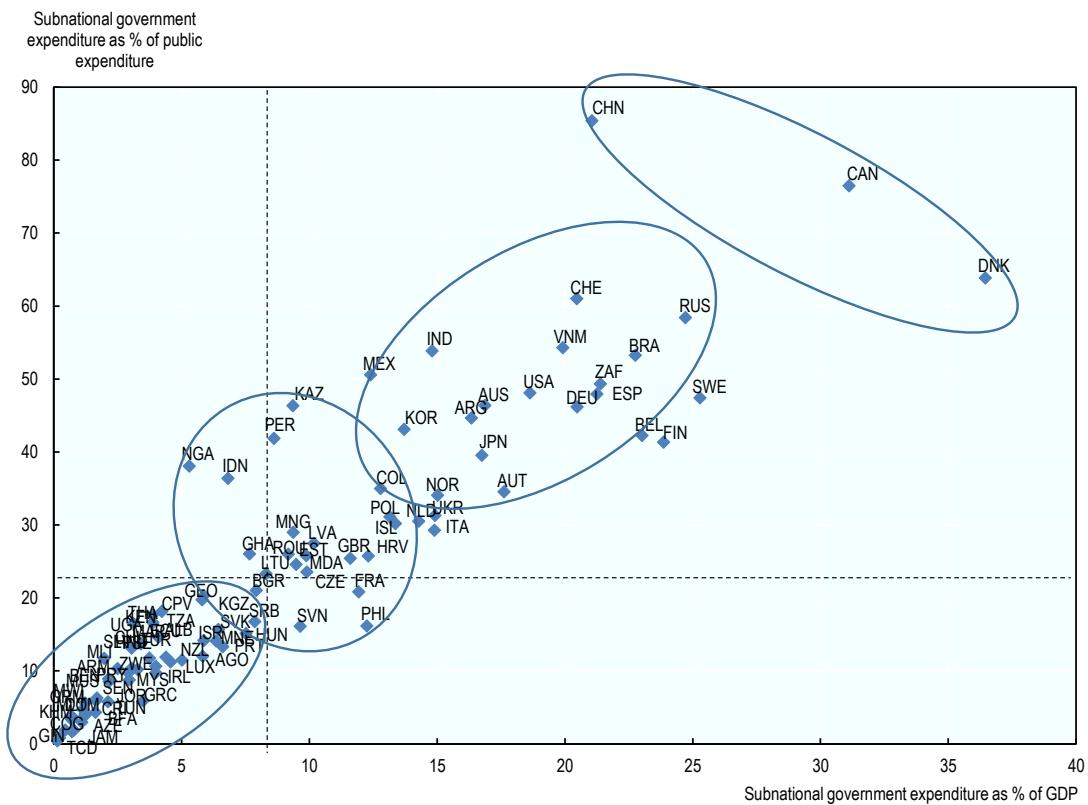
At a global level, subnational expenditure amounted to 9% of GDP and 24% of public expenditure in 2013-14 (OECD-UCLG, 2016^[3]). The level of subnational spending is uneven among world regions (Figure 2.15) and countries (Figure 2.16).

Figure 2.15. Subnational expenditure as a percentage of GDP and of public expenditure at the global level by main regional areas

Note: All averages are unweighted.

Source: OECD elaboration based on OECD-UCLG (2016^[3]), *Subnational Governments around the World: Structure and Finance*, <http://www.oecd.org/regional/regional-policy/sngs-around-the-world.htm>.

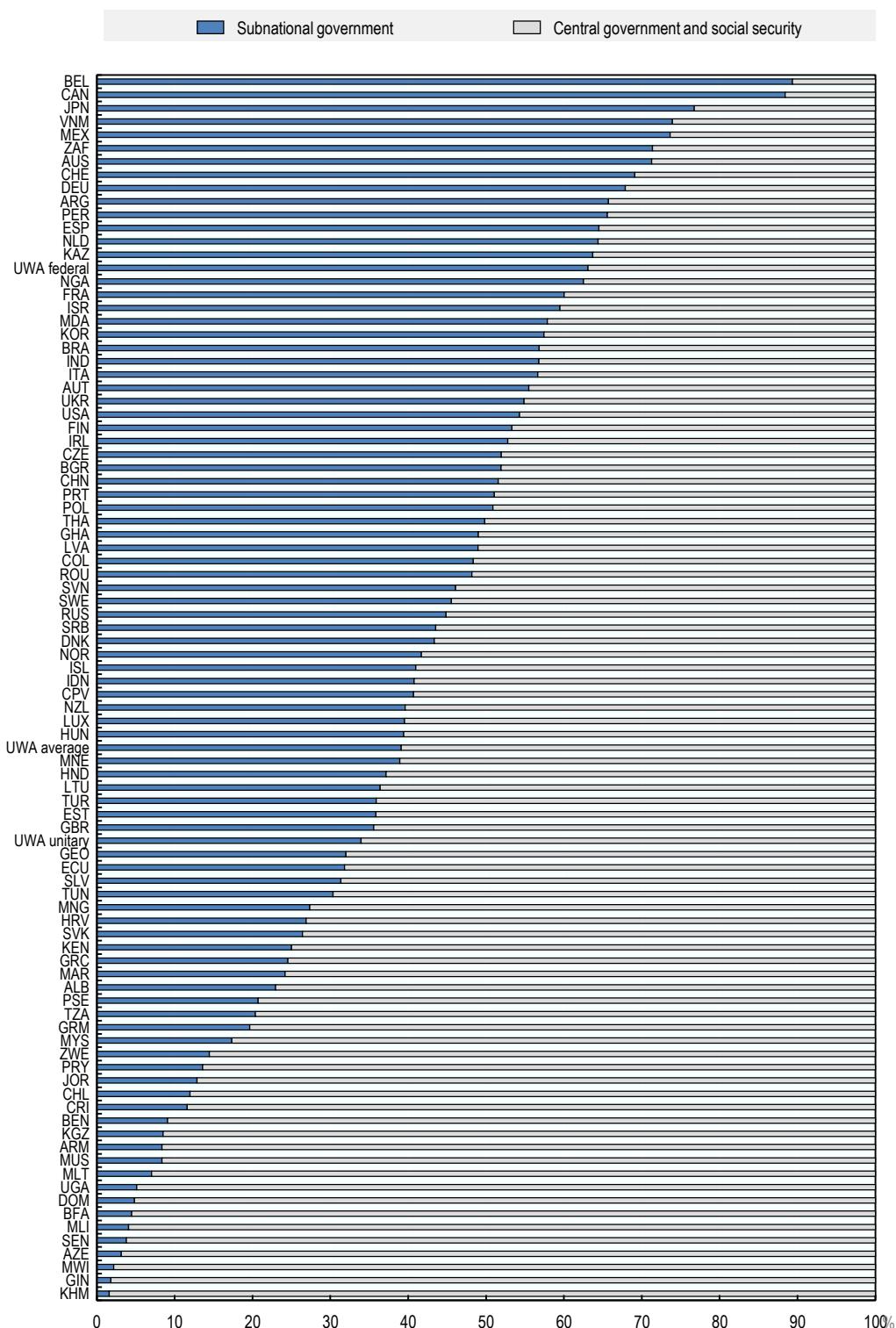
Figure 2.16. Subnational expenditure as a percentage of GDP and of public expenditure at the global level by country



Source: OECD (2018) Subnational governments in OECD countries: key data (brochure and database).

Subnational governments are also key public investors at the global level, accounting for 40% of public investment on average worldwide (1.5% of GDP). This indicates that worldwide public investment is a shared responsibility across levels of government, making its governance particularly complex. The OECD Council *Recommendation on Effective Public Investment across Levels of Government*, adopted in 2014, acknowledged the importance of better governance for public investment. It is relevant not only to OECD countries but also globally.

Figure 2.17. Subnational governments account for a large share of public investment worldwide



Source: OECD elaboration based on OECD-UCLG (2016^[3]), *Subnational Governments around the World: Structure and Finance*, <http://www.oecd.org/regional/regional-policy/sngs-around-the-world.htm>.

Assignment of responsibilities: Great variation at the regional level, less variation at the local level

The assignment of responsibilities depends on many factors, including a country's institutional structure. Some common trends in the assignment of responsibilities can be identified (Table 2.3). Overall, there is greater variation across countries in the distribution of competencies at the regional level and less variation at the local level (Allain-Dupré, 2018^[30]). In contrast to local governments, which are often general-purpose, it is not uncommon for intermediate tiers to be deconcentrated, possess dual executives, or have more limited autonomy, particularly in unitary countries. There are also single purpose or special purpose local jurisdictions in several countries (e.g. for education, health and sanitation boards and agencies, and public/private utilities).

Table 2.3. Breakdown of responsibilities across subnational government levels: A general scheme

Municipal level	Intermediary level	Regional level
<p>A wide range of responsibilities:</p> <ul style="list-style-type: none"> General clause of competence Eventually, additional allocations by the law <p>Community services:</p> <ul style="list-style-type: none"> Education (nursery schools, pre-elementary and primary education) Urban planning and management Local utility networks (water, sewerage, waste, hygiene, etc.) Local roads and city public transport Social affairs (support for families and children, elderly, disabled, poverty, social benefits, etc.) Primary and preventative healthcare Recreation (sport) and culture Public order and safety (municipal police, fire brigades) Local economic development, tourism, trade fairs Environment (green areas) Social housing Administrative and permit services 	<p>Specialised and more limited responsibilities of supra-municipal interest</p> <p>An important role of assistance towards small municipalities</p> <p>May exercise responsibilities delegated by the regions and central government</p> <p>Responsibilities determined by the functional level and the geographic area:</p> <ul style="list-style-type: none"> Secondary education or specialised education Supra-municipal social and youth welfare Secondary hospitals Waste collection and treatment Secondary roads and public transport Environment 	<p>Heterogeneous and more or less extensive responsibilities depending on countries (in particular, federal vs. unitary)</p> <p>Services of regional interest:</p> <ul style="list-style-type: none"> Secondary/higher education and professional training Spatial planning Regional economic development and innovation Health (secondary care and hospitals) Social affairs (e.g. employment services, training, inclusion, support to special groups, etc.) Regional roads and public transport Culture, heritage and tourism Environmental protection Social housing Public order and safety (e.g. regional police, civil protection) Local government supervision (in federal countries)

Source: OECD (2017^[32]), *Making Decentralisation Work in Chile: Towards Stronger Municipalities*, OECD Multi-level Governance Studies, <https://doi.org/10.1787/9789264279049-en>.

In many countries, the municipal level tends to manage community services. Municipal responsibilities are not always precisely defined. Regulations often refer to the general clause of competency or “subsidiarity principle”. This principle gives local authorities the explicit freedom to act in the best interests at the local level. In this case, laws rarely limit or specify local responsibilities but rather enumerate broad functions, unless a particular responsibility is devolved by law to another government level.

In two-tier subnational government systems, the regional level usually provides services of regional interest because it operates at a larger scale. These services benefit from economies of scale, generate spillovers, involve redistribution and are required to meet the same standards across the jurisdiction. The regional tier may also facilitate co-operation and strategic planning.

In three-tier systems, the breakdown can be complex, sometimes resulting in duplication, overlap and co-ordination challenges. However, over recent decades, the intermediate level has lost many of its powers and responsibilities in favour of regions, that gained more importance. In a majority of countries, intermediate governments are now mainly responsible for administrative and delegated tasks, and have small budgets and generally little to no taxing powers.

It is necessary to make the distinction between competencies and functions. For each responsibility area, different key functions can be distinguished: regulating, operating, financing and reporting. Regarding the financing function, another distinction can be made between current expenditure and investment. In the OECD, health, education and social protection and law enforcement draw heavily on subnational expenditure, with subnational governments in charge of paying medical staff, teachers, social workers and police officers or providing social benefits on behalf of the central government. Often, subnational governments act as “paying agents”, carrying out these delegated functions with little or no decision-making power or room for manoeuvre, and these spending responsibilities can represent a great burden on their budget.

Rather than a clear-cut separation of responsibilities, most responsibilities are shared across levels of government and the trend toward shared responsibilities has increased over the past decades (see Chapter 3). Because subnational governments are embedded in national legislative frameworks, truly exclusive competencies rarely exist, even in federal countries. Shared competencies emerge either through explicit legislation or through residual policy acquisition. The need to share responsibilities may arise for functional reasons – as is common between municipal and regional tiers around issues of transport and infrastructure, environment and water, culture and tourism, communication, or economic development. It may also arise for financing reasons such as for social services. This mutual dependence requires a clear assignment of functions, a clear understanding of who does what by all parties, and well-developed co-ordination mechanisms (see Chapter 5).

Notes

¹ See Ivanya and Shah (2014^[8]); Arzaghi and Henderson’s index of institutional decentralisation (2005); Brancati’s levels of political decentralisation (2008); Lijphart’s federalism index (1999); Treisman’s decision making decentralisation (2002); Woldendorp, Keman, and Budge’s autonomy index (2000).

² Except in the case of special capital districts that fall in the regional level, the RAI does not code municipal governance. It also does not make assessments of what territorial units are doing with their authority, but focuses on formal multilevel governance arrangements.

³ Except in Portugal, where “freguesias”(Portuguese designation for “civil parishes”) are local authorities with the constitutional guarantee of self autonomy”.

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Chapter 3. Current trends in decentralisation

This chapter highlights that there has been a path towards decentralisation in a majority of OECD countries over the past decades. The chapter also underlines that decentralisation trends around the world have often gone hand in hand with an upscale in subnational governance through amalgamations, inter-municipal cooperation, metropolitan governance, and the strengthening of regions. Municipal fragmentation has driven policies encouraging or imposing mergers or cooperation. In parallel, there has also been an increase in asymmetric decentralisation, i.e. the fact that governments at the same subnational government level have different political, administrative or fiscal powers. While asymmetric decentralisation appears more “natural” in federal countries, it is increasing in unitary countries. Finally, the chapter shows that decentralisation is too often understood as a simple increase in the power of local governments. The reality is much more complex, as most responsibilities are shared across levels of government. Decentralisation is about reconfiguring relationships between the central government and subnational governments towards a greater cooperation and a strategic role for national/federal governments.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

This chapter focuses on trends in decentralisation among OECD countries and around the world. Over the past 70 years, the overall trend has been in favour of greater decentralisation. It is sometimes called the “silent revolution” (Ivanyna and Shah, 2014^[1]). Indicators that measure the authority of administrative regions (Regional Authority Index, RAI) show that all world regions are experiencing an increase in the RAI: western countries (mostly European) since the 1960s/1970s; Asia and Pacific countries since the 1980s; and Latin American countries since the 1980s, though to a lesser extent (Hooghe et al., 2016^[2]). In Europe, the Local Autonomy Index (LAI) shows an increase of local autonomy between 1990 and 2005, especially in the Central and East European countries (Ladner, Keuffer and Baldersheim, 2016^[3]).

Several OECD countries, both federal and unitary countries, already have a solid, long-established tradition of subnational self-government. The decentralisation trend has intensified continuously over the last few decades, in particular in unitary countries. Some other countries have experienced a back and forth fluctuation between decentralisation and recentralisation.

The global crisis in 2008-09 led to a certain recentralisation in some countries, with an increase in central government grants to support subnational governments. This was only a temporary trend, however, as it was followed by important cuts in central government grants after 2010-11 in most countries. Many countries, including almost one-third of OECD members, introduced fiscal rules in order to control subnational expenditures in the wake of the crisis. It is also possible that this enhanced control calls for greater intergovernmental co-ordination, which boosts the bargaining power of subnational jurisdictions to influence national policymaking (de Mello, 2018^[4])

Several complementary trends in decentralisation stand out and should be understood in the context of the mutual dependence that exists among levels of government: i) increased subnational spending and revenues; ii) reinforced local autonomy (municipal authority); iii) an upscale in subnational governance through inter-municipal co-operation, metropolitan governance and the strengthening of regions; and iv) increased asymmetric decentralisation, i.e. the fact that responsibilities may vary across subnational governments.

Increased subnational spending and revenues in OECD countries

An increase in subnational spending

In two thirds of OECD countries, decentralisation processes have resulted in an increase of economic importance of subnational government, measured both as a spending share of GDP and share of total public spending between 1995 and 2016 (Figure 3.1). The highest increases over the last 21 years (1995-2016) were seen in Poland, Germany, Denmark, Belgium, Sweden and Spain. Spain, in particular, experienced the highest increase. In Spain, the education and health decentralisation process in the 2002 and 2005 resulted in an increase of 13 percentage points of the share of subnational government in public expenditure and of 5 percentage points in the subnational expenditure contribution to the GDP between 1995 and 2016. In Belgium, the significant increase of the weight in GDP (6 percentage points) and in public expenditure (11 points) is explained by the implementation of the 6th state reform of 2011 (in effect since 2014), which has devolved new responsibilities from the federal government to the regions and communities. In Sweden, there has been a continuous growth of subnational spending over the period. Swedish subnational government handles not just the “pure local public services” but also

many of the redistribution functions of a welfare state, such as education and healthcare (OECD, 2017^[5]). In Poland, the increase in subnational expenditure started prior to 1995, after the adoption of the 1990 Act on Municipality re-establishing municipal autonomy and gave them large responsibilities. There was a second peak in 1999 when the regional and intermediate levels were created to take care of several responsibilities such as education, health, social protection, transport and regional economic development, and then in 2009, when new tasks were transferred again to the regions.

In other OECD countries, the increase in subnational expenditure over the period may also be explained by the decentralisation process, such as in Germany, Denmark, Canada, etc. (see Annex C) although additional factors can explain this increase e.g. greater social needs, in particular with the crisis, an ageing population, increasing environmental and security norms and quality standards as well as the costs of services.

By contrast, several OECD countries have experienced a reduction in the share of subnational government (SNG) expenditure in GDP and/or in general government over the past two decades. In Hungary, there was the recentralisation reform, started in 2011-12 with the constitutional reform and the Local Government Law which led the central government to reorganise the Hungarian local government sector and take over many functions exercised previously by municipalities and counties. As a result, Hungary went from being quite decentralised compared to other OECD countries to being among the most centralised. In 2010, subnational expenditure amounted to 25% of public expenditure, i.e. 12% of GDP to respectively 13% and 6% in 2017, a reduction by half in both cases (OECD, 2018^[6]).

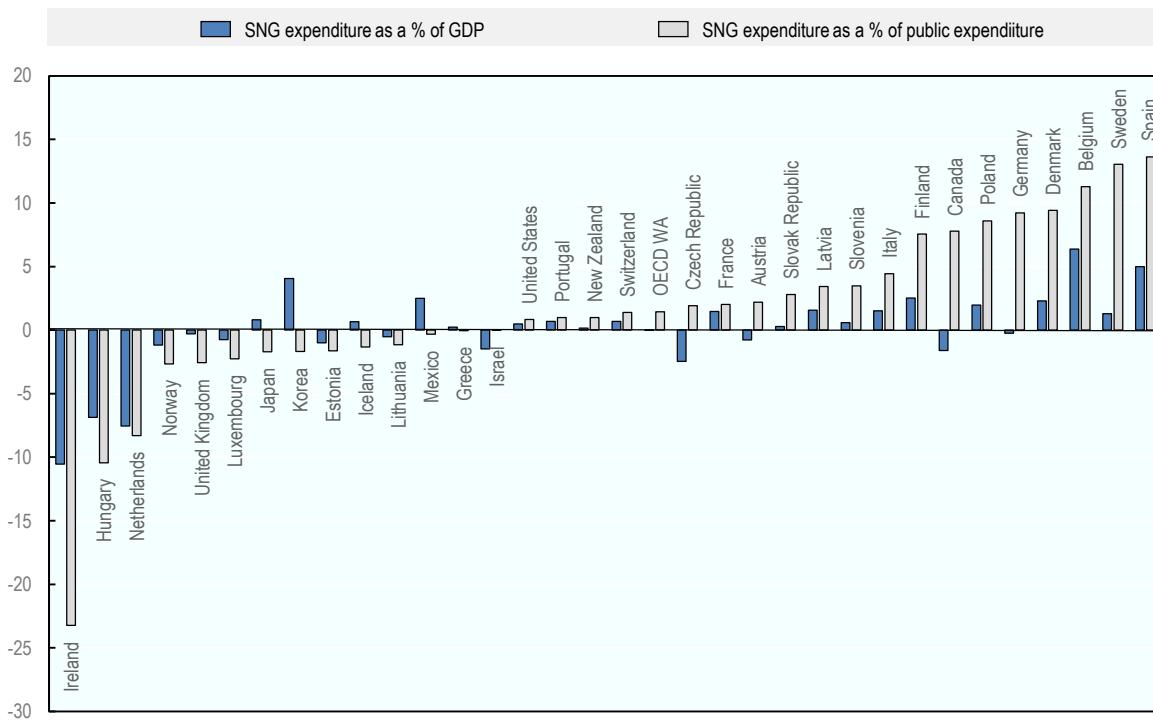
This decrease in subnational spending may also be the result of other trends, in particular since the global crisis that put subnational budgets under strong pressures. Therefore, in several countries, a decrease in subnational spending can be explained more by the effects of fiscal consolidation measures (spending cuts, savings programmes) or public management reforms aimed at seeking effectiveness and cost-efficiency (pooling of services and shared services agreements, performance assessments, public staff reforms, assets management, etc.) than a recentralisation process per se.

The case of Ireland is in between. A strong decrease in subnational spending in 2005, 2010 and in 2014 resulted both from recentralisation trends (e.g. water services and some other tasks in 2014), from *Better Local Government* reforms, including the 2014 Local Government Reform Act which merged 114 local councils into 31 local governments and abolished the previous 8 regional authorities, and from the 2008 recession. The crisis significantly reduced local income and necessitated spending and staffing cuts imposed by central government (Quinn, 2015^[7]).

In the Netherlands, the decline in subnational expenditure was observed only in 1995-96 (subnational spending dropped from 40% of public spending to 33%, and from 21% of GDP to 15%). Since that date, subnational government expenditure is quite stable, the transfer of spending responsibilities in the social sector in 2007 and 2015 being counterbalanced by public finance consolidation measures and management reforms (OECD, 2014^[8]).

Figure 3.1. Decentralising or recentralising trends in the OECD over 1995-2016

Changes in subnational government expenditure as a percentage of GDP and subnational government between 1995 and 2016



Note: Iceland 1998-2016; Japan: 2005-16, Mexico: 2003-16. No data for Australia, Chile and Turkey due to lack of time-series. OECD30 average is unweighted and does not include Australia, Chile, Japan, Iceland, Mexico and Turkey. Information on data for Israel: <http://dx.doi.org/10.1787/888932315602>.

Source: OECD calculations based on OECD national accounts (accessed on 9 October 2018).

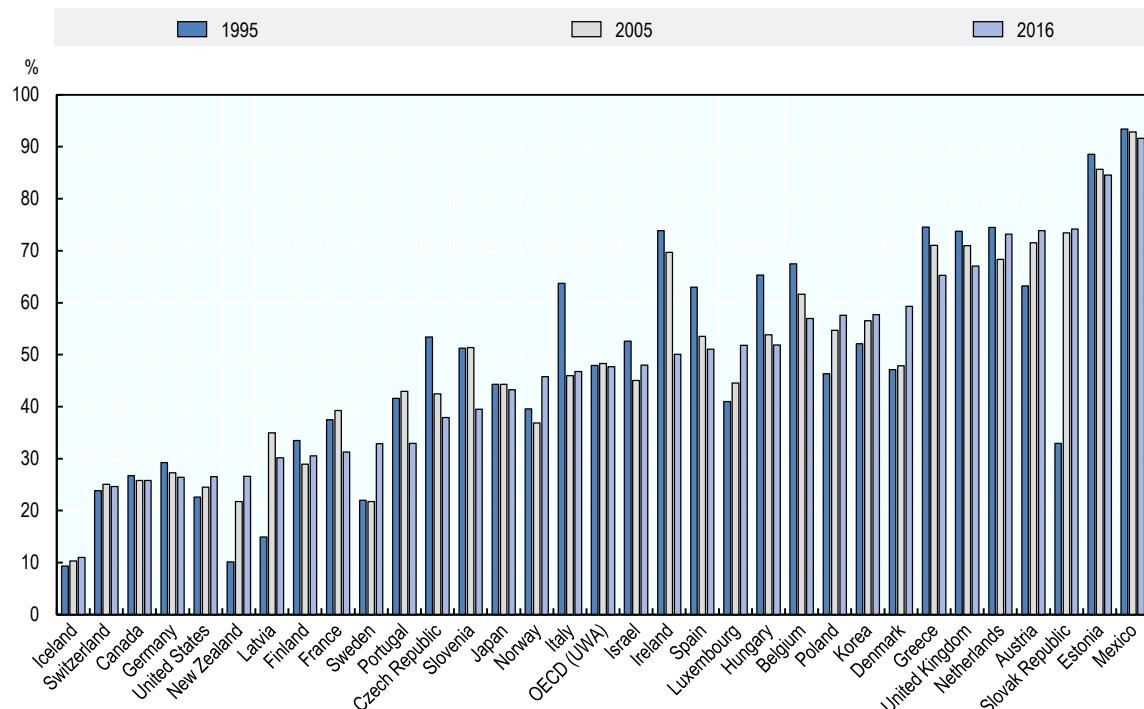
An increase in revenue decentralisation

At the OECD level, the share of grants in total revenue was relatively stable on average between 1995 and 2016. There have, however, been two main stages during this period, before and after the crisis (OECD/KIPF, 2016^[9]). In the 1990s until about 2008, a widespread policy of decentralisation of responsibilities in areas such as education, social protection, transport infrastructure, utilities, etc., was funded mainly by central government transfers, while subnational tax revenues remained largely stable. This resulted in an increase in vertical fiscal imbalance (the difference between subnational government own revenues and their spending obligations). An ever-growing grant system became the mechanism used to respond to higher subnational spending. Increased use of transfers was also employed to prevent regional disparities, correct horizontal imbalances across jurisdictions and meet central government requirements in service delivery (Bergvall et al., 2006^[10]).

At the country level, from 1995 to 2005, the share of transfers grew mainly as a response to the widespread policy of decentralising expenditures. During the economic and fiscal crisis, grants increased considerably in some countries as a means to support recovery plans, but this did not last. After the crisis, public finance consolidation plans in many countries resulted in freezes and cuts in central government transfers. The highest decrease of grants as a share of subnational revenues between 2005 and 2016 was

observed in France, Greece, Ireland, Portugal and Slovenia. As a result, despite the up and down swings of the last 21 years, today the composition of subnational government revenue is close to where it stood in 1995, on average in the OECD. At the country level, over the entire 1995-2016 period, the share of grants in total subnational revenues increased the most in the Denmark, Latvia, New Zealand and the Slovak Republic. The highest decreases were registered in the Czech Republic, Hungary, Ireland and Italy.

Figure 3.2. Grants as a share of subnational revenues in 1995, 2000 and 2016



Note: Ireland: 1998-2016; Japan: 2005-16; Mexico: 2003-16. No data for Australia, Chile, Turkey. OECD average is unweighted.

UWA: unweighted average for all countries

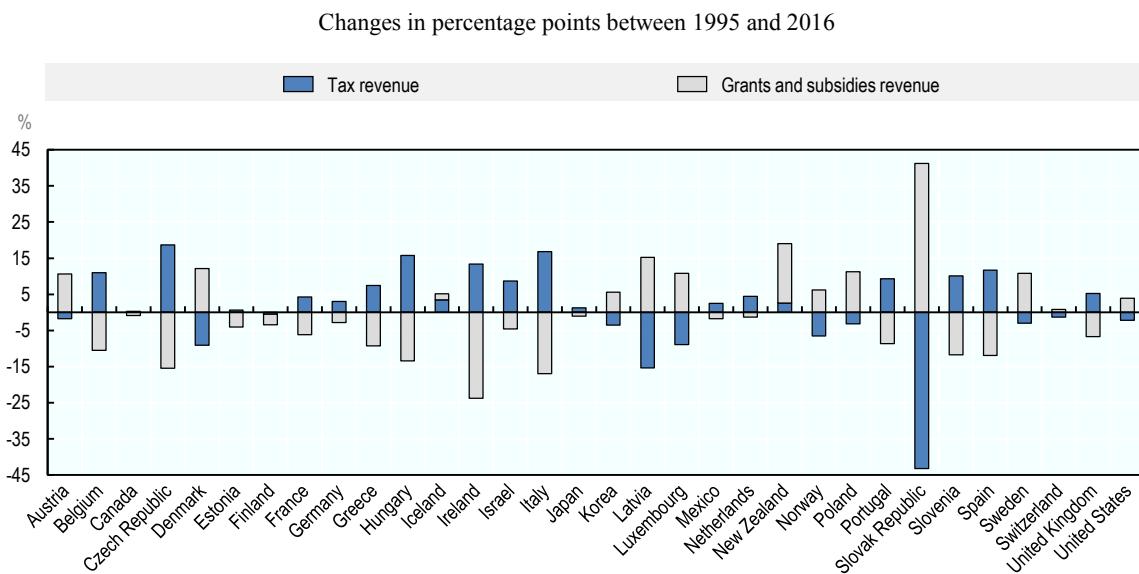
Source: OECD own elaboration based on OECD national accounts (data extracted in October 2018).

On the tax revenue side, tax revenues have increased slightly both in GDP and in total public tax revenues. Tax revenues encompass shared and own-source taxes, which does not allow for assessing progress in tax autonomy. Between 1995 and 2016, subnational tax revenues increased – or decreased – significantly in several countries as a percentage of total public tax revenue and GDP. These changes typically reflect economic performance since taxes such as personal income (PIT), corporate income (CIT), VAT, property transaction, consumption, construction activity, etc., are sensitive to economic fluctuations. The changes also reflect tax reforms indirectly affecting subnational governments (e.g. changes in national shared PIT or CIT) or directly related to subnational governments.

Several tax reforms took place over the past 21 years that aimed at increasing the importance of taxes in subnational funding, either by allocating larger shares of national taxes to subnational governments and/or by giving more taxing powers to subnational governments (ability to create local taxes, to determine rates and bases and to grant tax

allowances or reliefs). These tax reforms resulted in significant increases in subnational tax revenues in Belgium (2002 and 2014), the Czech Republic (2005), Poland (2004), Slovenia (2009) and Spain (in 2002, 2009 and 2012) and. In Italy, after the 1998 Bassanini Reform, tax revenue increased vastly from 25% in 1997 to 41% of subnational revenue after the 2009 reform.

Figure 3.3. Changes in grants and tax revenue as a share of subnational government revenue



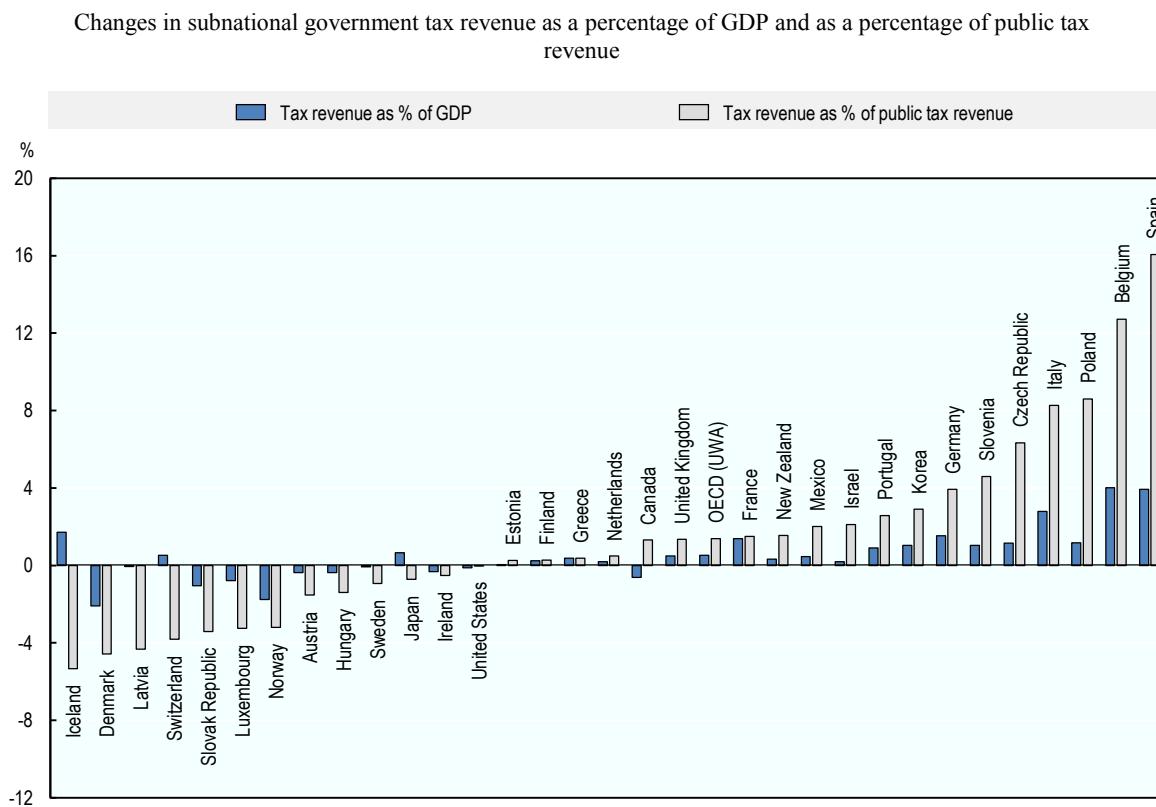
Note: Ireland: 1998-2016; Japan: 2005-16; Mexico: 2003-16. No data for Australia, Chile, Turkey. OECD average is unweighted.

Source: OECD own elaboration based on OECD national accounts (data extracted in October 2018).

In contrast, the share of subnational tax revenue contracted in Denmark (especially since the 2007 local government reform and the abolition of counties, which previously benefited from tax revenues), Hungary (fiscal recentralisation reform, Latvia, Norway (abolition of the national corporate income tax as a local tax in 1999), the Slovak Republic (2005 reform) and Switzerland.

However, these figures do not offer a fair view of the changes as tax revenue figures distinguish between shared taxes and own-source taxes, for which subnational governments have a certain leeway over rates and bases. In France for example, the 2010 local finance reform did not affect the share of tax revenue in local revenue or GDP, but significantly diminished the share of own-source taxes, leading to less tax autonomy. In other countries, the reverse is also true: stability in terms of tax revenue may have been observed over the years although there was an increase in tax autonomy resulting from the introduction of new own-source local taxes and the broadening of local decision-making power for setting rates or based on existing local taxes (e.g. property tax).

To provide a complete picture, it is worth looking at the tax autonomy indicators developed by the OECD Fiscal Network. They show that from 1995 to 2011, tax autonomy increased, at the expense of tax-sharing systems (OECD/KIPF, 2016^[9]). In Denmark and France, fiscal reforms led to a decrease in subnational revenue autonomy, while in Finland, Italy, Japan, Korea, Portugal and Turkey local revenue autonomy increased (OECD, 2017^[11]).

Figure 3.4. Decentralising or recentralising trends in the OECD over 1995-2016

Note: Iceland 1998-2016; Japan: 2005-16; Mexico: 2003-16. No data for Australia, Chile and Turkey due to lack of time-series. OECD30 average is unweighted and does not include Australia, Chile, Japan, Mexico and Turkey. Information on data for Israel: <http://dx.doi.org/10.1787/888932315602>.

Source: OECD calculations based on OECD national accounts (data extracted in October 2018).

A modest increase in subnational spending power from 1995 to 2014

Financial expenditure shares often do not accurately reflect subnational spending power, as subnational spending is generally highly regulated or otherwise influenced by the central government. Using results from the recent spending power questionnaire sent to member countries of the OECD Fiscal Federalism Network, the OECD constructed institutional indicators that compare subnational spending power across countries and policy sectors (OECD, forthcoming^[12]).

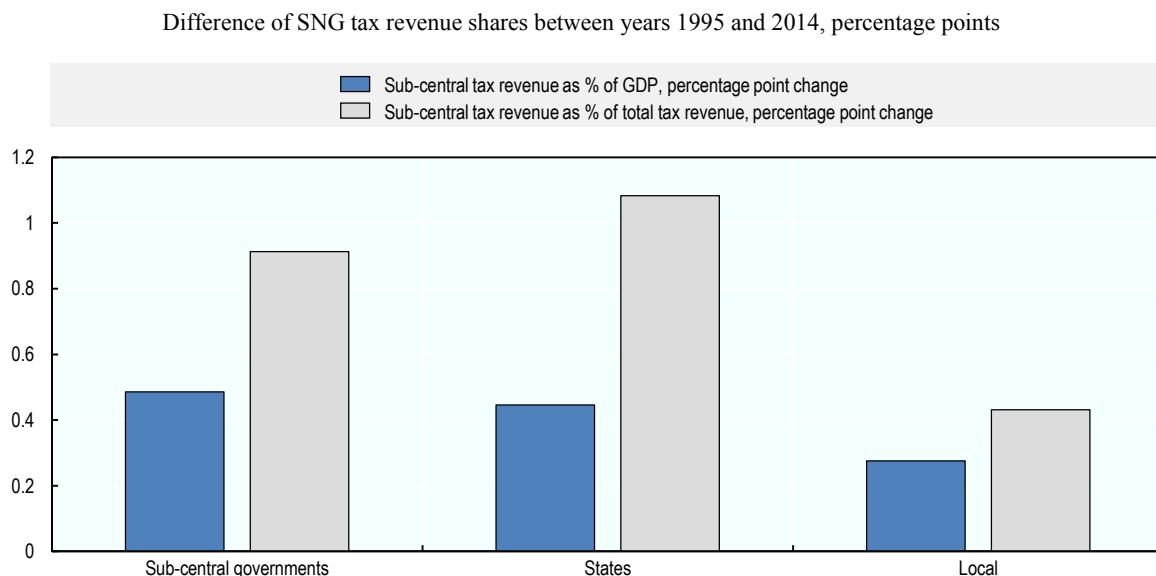
According to the results, subnational spending authority is relatively low, on average. Spending power is quite balanced across sectors but is lower in health and long-term care, and higher in social housing, transport and primary and secondary education (referred to as education).

While the data collected from single questionnaires do not enable comparisons over time, the OECD Fiscal Federalism Database includes useful information for descriptive purposes. For instance, the evolution of taxing power from 1995 to 2014 can be described using data on subnational tax revenue as a percentage of GDP and subnational tax revenue as a percentage of total tax revenue.

The average share of subnational tax revenue increased slightly from 1995 to 2014 (Figure 3.5). The pattern of taxing power changes was more complex, including ups and

downs depending on years and types of subnational government in question (the database has separate figures for states and local governments). On average, the tax revenue share of subnational governments in all tax revenue rose by 0.9 percentage points, by 1.1 percentage points for the state level and by 0.43 percentage points for local governments.

Figure 3.5. A slight increase in SNG tax autonomy indicators during 1995-2014



Note: Author's calculations. Information on data for Israel: <http://dx.doi.org/10.1787/888932315602>. Local governments in the United States have a wide variety of taxing powers but it is not possible to identify the share of each. The unweighted average for 1995 and 2014 applies to the subnational revenue shares in the 35 OECD countries. The unweighted average for States applies only to the ten countries reporting state or regional data. Italy and Spain are considered as regional countries for the purpose of the tax autonomy indicators.

Source: OECD (n.d.^[13]), *OECD Fiscal Decentralisation Database*, <http://www.oecd.org/tax/federalism/fiscal-decentralisation-database.htm>.

Enhanced local autonomy as measured by the LAI

As highlighted in Chapter 2, financial data are not sufficient to assess local autonomy. There are other elements, such as the extent to which municipalities are able to decide on the kind or type of services they wish to provide, how they want to organise themselves, and whether they have an influence on decisions taken at a higher government level. The following section looks at the trends in the different dimensions of local autonomy in 39 European countries (Keuffer and Ladner, 2018^[14]).

The Local Autonomy Index consists of seven dimensions:

1. *Legal autonomy* measures the extent to which the existence of municipalities is constitutionally guaranteed and whether or not municipalities can, for example, be amalgamated against their will.
2. *Policy scope* describes the range of services for which municipalities are responsible.
3. *Political discretion* additionally asks whether municipalities also have some decisional power while fulfilling these tasks.

4. *Financial autonomy* means that municipalities have their own financial resources, can collect tax and decide on their base and their rate and are able to borrow money.
5. *Organisational autonomy* describes the possibility to organise and staff their administration and to decide on features of their political system.
6. *Non-interference* is related to the vertical relations with the higher levels of state and consists in the way supervision is organised and whether financial transfers are unconditionally granted.
7. *Access* captures whether municipalities can influence higher-level decisions.

The LAI concerning the *legal dimension* suggests that lawmakers in Europe gradually seem to be strengthening the level of autonomy granted to local authorities (Table 3.1). With respect to policy scope, there is still substantial variation across European countries, with the Nordic countries and some Central European states at the top end of the scale, and some Black Sea countries as well as Ireland and the United Kingdom at the other end. Policy scope also varies across the policy fields considered (i.e. education, social assistance, health, land-use, public transport, housing, police and caring functions). Policy responsibility is most extensive in the fields of land-use (zoning, building permits), school buildings, housing, caring functions and public transport. In many European countries, it is municipalities that are mostly in charge of these functions. It is more unusual for municipalities to have responsibility for the police, what actually goes on inside school buildings (e.g. educational programmes, the hiring and paying of teachers) or in health services.

Financial autonomy witnesses a huge variation, both across time and among countries. For most of the 1990-2014 period, the dominant trend was an increase in financial autonomy. This was especially true for post-communist countries in Central and Eastern Europe, which started out with a very low level of financial autonomy. There was also an increase in some countries from other parts of the continent (e.g. Italy and Malta). With the 2008 financial crisis, the overall trend was partially reversed, most visibly in changes related to borrowing regulations and in countries that were most severely hit by the crisis. It is interesting to note that the LAI shows no evidence that a large scope of functions allocated to local governments generates demands to tighten control over municipal finance. Rather the opposite seems to be the case: taxation and borrowing autonomy are often higher in countries with more functional decentralisation.

According to the LAI, most European local government enjoy quite high levels of *organisational autonomy*. Municipalities are usually able to elect their local executive directly and have some leeway when it comes to organising their local administration. In some countries, municipalities can decide on elements of their electoral system, such as the number and size of their electoral districts, whether they prefer majority elections or proportional representation, and the form or the size of their local executive (e.g. in the Czech Republic, Denmark, Estonia, Iceland, Norway, Sweden, Switzerland). In most countries, however, these parameters are set by national legislation. As for local administration, in most countries, local government has the freedom to hire its own staff, fix the salaries of employees, choose their organisational structure and establish legal entities and municipal enterprises. There are, however, also countries where the local administration is more directly organised and administered by the central state (e.g. France). If there have been changes in the degree of organisational autonomy, most of them took place in the 1990s. For many countries, particularly for those in Eastern and

Central Europe, active democratic reforms and a transformation of the prevailing political culture were consolidated in this period.

The results of the LAI point out a general increase in autonomy between 1990 and 2009. A similar pattern is shown by the OECD Fiscal Federalism Database indicators. This increase has taken place especially in the new democracies of Central and Eastern Europe, such as Albania, Bulgaria and Romania. However, there are also countries, such as Hungary, that have pursued centralisation policies over the last few years. The LAI shows that in 2014, Switzerland and the Nordic countries (Denmark, Finland, Iceland, Norway and Sweden) rank among the countries with the highest degree of autonomy, together with Germany, Liechtenstein and Poland (Table 3.1 and Box 3.1).

Table 3.1. Local Autonomy Index (LAI), country ranking 2014, 1990 and changes

Countries	LAI_2014	LAI_1990	Changes	Countries (next)	LAI_2014	LAI_1990	Changes
Switzerland	79.6	78.4	1.2	Netherlands	59.6	53.6	6
Finland	79.4	75.2	4.2	Macedonia	59.3	33.4	25.9
Iceland	78.1	68.4	9.7	Romania	58.1	29.3	28.9
Sweden	75.1	73.7	1.4	Croatia	56.7	41	15.8
Denmark	74.7	75.8	-1.1	Luxembourg	55.9	62.6	-6.7
Poland	74.1	68.5	5.6	Spain	55	60.6	-5.6
Germany	73.9	73.5	0.4	Latvia	54.2	51.3	3
Norway	73.9	65.1	8.8	Hungary	50.8	62.8	-12.1
Liechtenstein	69.4	72.7	-3.3	Albania	50.6	13.5	37.2
Italy	68.2	51.1	17.1	Slovenia	48.9	23.6	25.4
Serbia	67	48.4	18.6	Greece	47.9	41.5	6.4
France	66.8	64.2	2.6	Ukraine	47.7	42.4	5.3
Bulgaria	66.2	25.3	40.9	United Kingdom	45.7	46.8	-1.2
Lithuania	65.1	47.3	17.8	Cyprus	42.3	37.1	5.2
Czech Republic	64.9	43.7	21.2	Turkey	39.7	40.2	-0.5
Austria	64.8	63.5	1.4	Malta	39.2	30.1	9.1
Estonia	63.7	64.5	-0.8	Georgia	38.4	23	15.4
Portugal	61.6	51.8	9.7	Moldova	35.9	16.5	19.4
Belgium	61.3	51.9	9.4	Ireland	34.9	30.4	4.5
Slovak Republic	60.9	44	16.8				

Note: Countries sorted by 2014. For Albania, Latvia, Malta, Romania and Ukraine, there is no data for 1990; the first years of measurement for these countries are: 1992, 1991, 1993, 1992 and 1991 respectively.

Note by Turkey: The information in this document with reference to “Cyprus” relates to the southern part of the Island. There is no single authority representing both Turkish and Greek Cypriot people on the Island. Turkey recognises the Turkish Republic of Northern Cyprus (TRNC). Until a lasting and equitable solution is found within the context of the United Nations, Turkey shall preserve its position concerning the “Cyprus issue”.

Note by all the European Union Member States of the OECD and the European Union: The Republic of Cyprus is recognised by all members of the United Nations with the exception of Turkey. The information in this document relates to the area under the effective control of the Government of the Republic of Cyprus.

Source: (Keuffer and Ladner, 2018^[14]).

Box 3.1. Country-specific patterns of local autonomy

More revealing than a simple overall ranking are country-specific patterns of local autonomy. Finland, for example, has a “full” profile, reaching high levels of autonomy in all seven dimensions, whereas the opposite is the case for Ireland. By contrast, high legal autonomy with less autonomy in the other dimensions is characteristic among the newer Eastern democracies such as Bulgaria, the Czech Republic, Estonia and Romania. The latter two distinguish themselves from the other countries by their high degree of organisational autonomy.

France, after its increased decentralisation efforts in the 1980s, demonstrates a substantial degree of autonomy in almost all dimensions, with the exception of features of the local political system and administrative organisation. In Switzerland, municipalities are autonomous in financial and organisational affairs and enjoy legal protection, but they are more limited in their ability to decide on their policies. This is related to their small size and the Swiss form of federalism, which allocates political discretion to the cantons. The much larger German municipalities – despite the federalist structure of the country – are more autonomous with respect to policy scope and political discretion.

Hungary, Slovenia and Ukraine share a similar pattern: a lack of financial autonomy and deficits with respect to access and non-interference. They score average on autonomy on the other four dimensions. Interesting to note are also the similarities between Spain and the United Kingdom. In the former, however, organisational autonomy is low and financial autonomy is high whereas in latter the opposite is the case. The patterns for Ireland finally show very low levels of autonomy in virtually all dimensions.

Source: Keuffer, N. and A. Ladner (2018[14]), *The Local Autonomy Index Project – Extent, Patterns and Effects of Local Autonomy in Europe*.

Preliminary analysis suggests that the LAI is positively related to trust in local and regional government, even when other variables are controlled (Keuffer and Ladner, 2018[14]). On the output side, the analyses show two significant correlations when observing the average size of the municipalities and post-communist countries: between local autonomy and a low degree of corruption plus a high degree of happiness. The LAI analyses also show that financial autonomy is the dimension that almost consistently correlates most strongly with the different performance measures. Quite often, there are also positive links with the policy scope of local government and political discretion on the one hand, and performance indicators on the other hand. These results indicate a need for additional analysis. Developing these indicators further is an essential step to facilitate high-quality empirical analysis of the effects and effectiveness of decentralisation.

Upscaling governance: The rising role of regions and metropolitan areas

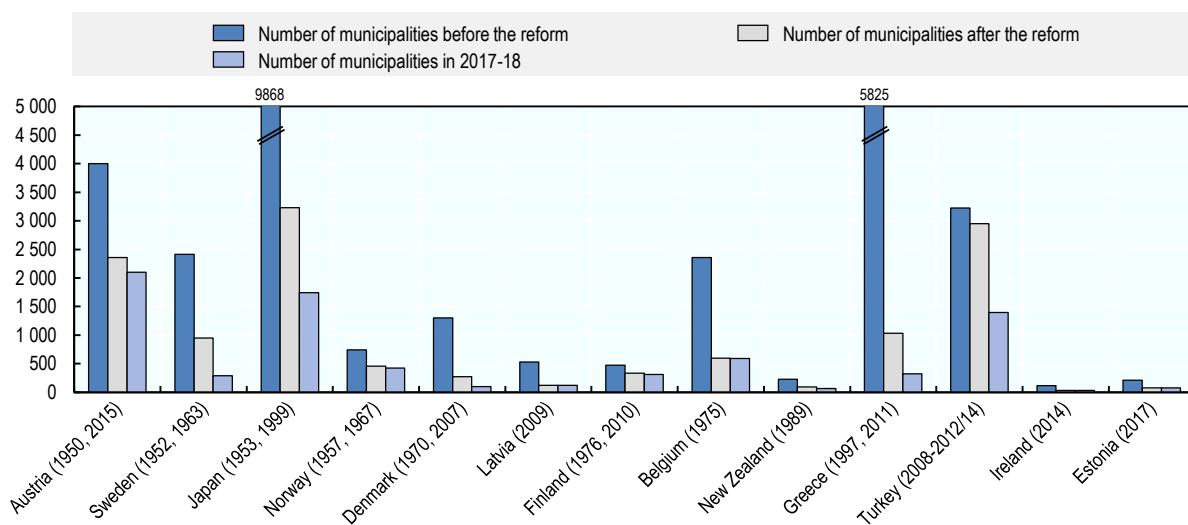
If decentralisation implies a strengthening of local autonomy, it also goes hand in hand with an upscale in subnational governance through municipal co-operation, metropolitan governance and the strengthening of regions. This section provides evidence behind these trends at the inter-municipal, metropolitan and regional levels, and highlights some policy implications.

Municipal consolidation and co-operation

Municipal fragmentation, which can result in an inefficient provision of local services and raises issues of equity in access to services generally and of equivalent quality, has been the driver of policies that encourage or impose amalgamation. It has also engendered policies that foster inter-municipal co-operation (OECD, 2017^[11]) as a way to generate economies of scale, efficiency gains and cost savings.

Municipal mergers have taken place in most OECD countries over the last decades. In some countries, there have been successive waves of reform. In others, it has been a gradual process over a long period, which may still be underway. The global crisis acted as a catalyst to reactivate or introduce municipal amalgamation policies. Recent reforms took place in Greece (2011), Turkey (2012-2014), Ireland (2014) and Estonia (2017) where the number of municipalities decreased from 213 to 79 (14 of which are urban and 65 rural) following the administrative reform completed in October 2017 (OECD, 2018^[15]). Municipal mergers are still ongoing as a piecemeal process in several countries such as in Finland, France, Italy, Luxembourg, the Netherlands and Norway. Some federal countries also introduced mergers under the leadership of federated states e.g. Thurgovie, Fribourg, Vaud, Tessin, Grisons in Switzerland, New South Wales and South Australia in Australia, Styria in Austria, Manitoba or New Brunswick in Canada, and Brandenburg and Saxony-Anhalt in Germany.

Figure 3.6. Municipal mergers in selected OECD countries from 1950 to 2017



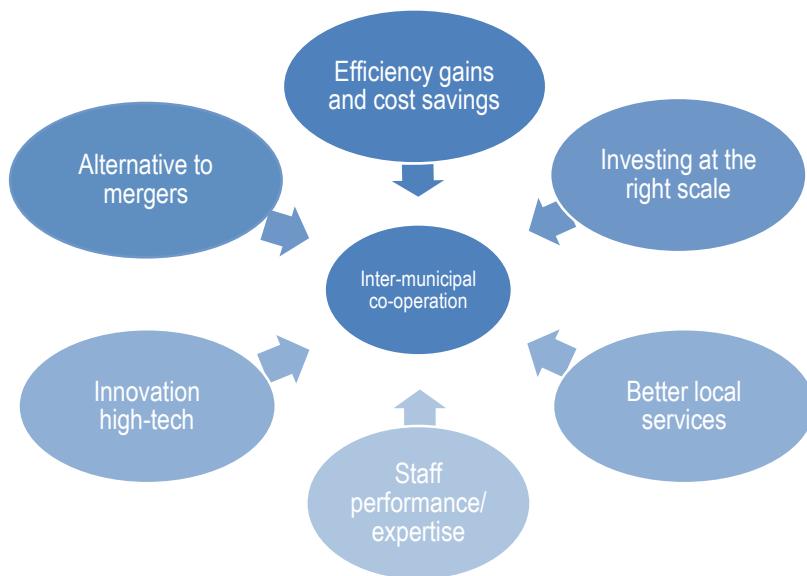
Source: OECD (2017^[11]), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, <https://doi.org/10.1787/9789264272866-en>, updated.

Reasons for mergers are numerous, including the need to adapt to demographic change (e.g. ageing, migration, shrinking or expanding populations) and to reduce the mismatch between obsolete municipal administrative boundaries and socio-economic functional areas. Reasons are also linked to the need to implement economies of scale and scope, generate cost savings and internalise spillovers in the provision of local public services, to increase municipal administrative capacities, to improve the quality and quantity of municipal infrastructure and services and more generally, to improve the governance, professionalism and efficiency of municipal management (OECD, 2017^[11]). However,

despite incentives to merge, the implementation of merger policies has often faced resistance, leading some countries either to impose municipal amalgamations in a compulsory way, to temper initial ambitions or to abandon the project altogether.

Today, inter-municipal co-operation (IMC) is widespread in the OECD, and firmly rooted in European and OECD municipal management practices. It is relevant in all countries regardless of municipal size, offering benefits to rural and metropolitan areas alike (Chapter 4). There have been different drivers for this progress in inter-municipal co-operation, especially since the global crisis (Figure 3.7).

Figure 3.7. Drivers for inter-municipal co-operation in the OECD



Legal frameworks and policies supporting inter-municipal co-operation have been significantly enhanced over the last 15 years (Table 3.2). Inter-municipal arrangements are now extremely diverse and reflect varying degrees of co-operation. There are different formats for inter-municipal co-operation in the OECD, ranging from the softest – single or multi-purpose co-operative agreements/contracts (e.g. shared services arrangements or shared programmes in Australia, England [United Kingdom], Ireland, New Zealand) – to the strongest forms of integration (e.g. supra-municipal authorities with delegated functions in France, Portugal and Spain). Between the two, co-operation covers a range of forms and areas, from co-operation focused on technical issues to strategic co-operation for economic and social development (OECD, 2017^[11]).

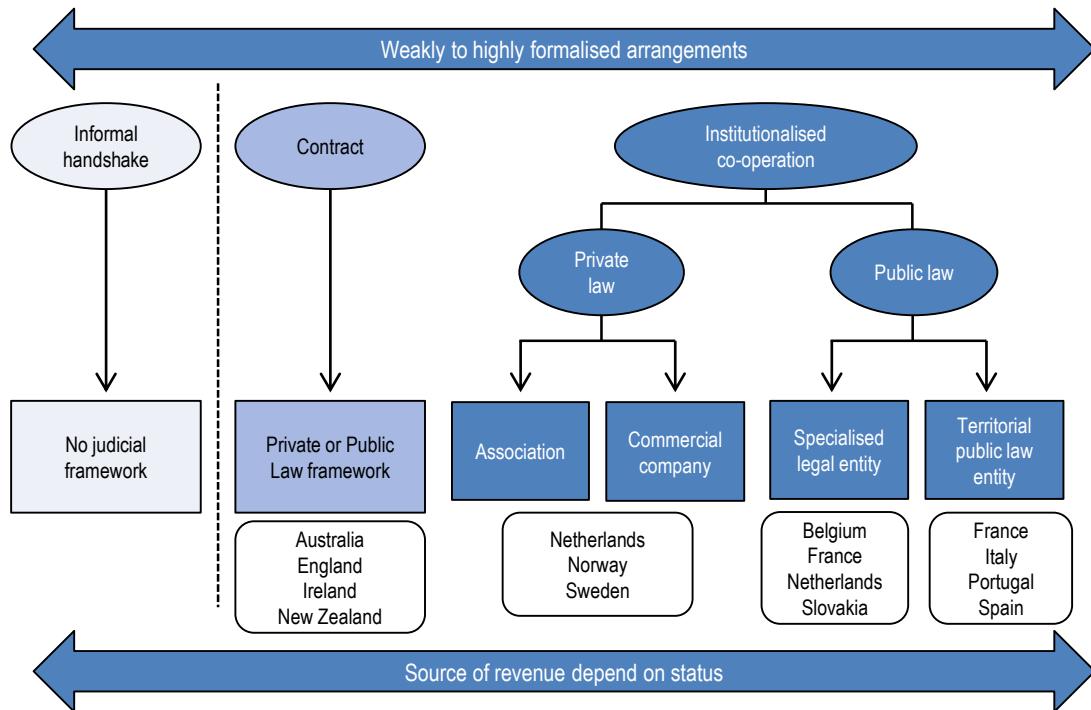
OECD countries generally have chosen to start first with a private law model. This is usually based on the freedom of local authorities to opt for certain formulas, such as contracts, associations and commercial enterprises. The next step is often a move to a public law model. The public model means that co-operation is regulated in some detail by public laws, including the contractual and financing arrangements, the type of delegated functions, the governance structure, the supervision and control, etc.

Table 3.2. Progress of inter-municipal co-operation in the OECD

Country	Legal frameworks and policies
Australia	Regional Organisations of Councils (ROCs), a major type of multi-purpose co-operation arrangement among councils for over 70 years, have been substantially restructured, reformed or have disappeared entirely in some states. Other types of IMC exist: Regional Local governments (Western Australia); Regional Subsidiaries (South Australia); County Councils (NSW), etc. Shared services arrangements promoted in both state and local government throughout Australia.
Austria	IMC designed and implemented by individual states but the Constitution states that municipalities may join forces by agreement or by law to form inter-municipal organisations (<i>Gemeindeverbände</i>). A 2011 federal constitutional amendment further reinforced the ability of municipalities to engage in inter-municipal associations.
Belgium	Flemish and Walloon Regions are currently encouraging “supra-municipalities”. In Flanders, the existence of five legal forms of IMC: “interlocal” association, project association, service providing association, association with a clear assignment, association with a clear assignment and private sector participation.
Canada	Special agencies, joint boards and commissions are popular to provide specific services to groups of municipalities. Some provinces can have specific policies promotion IMC such as New Brunswick.
Chile	A 2009 law allowed municipal associations to obtain legal personality under private law. In 2011, a new law provided the impetus to create municipal associations.
Czech Republic	IMC promoted by the 2000 Act on Municipalities under the form of voluntary municipal association and micro-regions (around 790 IMC structures active in the field of education, social care, health, culture, environment, tourism).
Denmark	Voluntary IMC for example in “Business Regions”.
Estonia	Existing framework for voluntary IMC to perform non-mandatory tasks on behalf of local authorities defined in the 1993 Local Government Organisation Act (non-governmental organisations, municipal enterprises, etc.). Enhanced IMC promoted by the recent territorial reform.
Finland	Special purpose joint authorities (184 currently) producing joint services several municipalities, mostly in healthcare and education will be touched by the ongoing local government reform, creating regions and transferring some municipal functions to them.
France	Different categories of IMC structure with own-source tax (<i>EPCI à fiscalité propre</i>), including since the changes introduced by the 2014 MAPTAM law: “communities of municipalities” in rural areas, “town communities”, 11 “urban communities” for urban areas and metropolis (more than 400 000 inhabitants). Recent 2015 Law NOTRE set up a minimum threshold for inter-municipal groupings.
Germany	IMC is strongly encouraged by <i>Länder</i> , in particular for some standard local services such as waste management, sewage, water or transport (<i>Zweckverbände</i> and municipal associations).
Greece	IMC structures with single or multiple tasks authorised by the municipal code but many of them are inactive.
Hungary	IMC is encouraged through the 1997 Act on the Associations and Co-operation of Local Government. The 2011 Cardinal Law on Local Governments stated compulsory pooling of administrative services for municipalities under 2 000 inhabitants in joint offices or districts or micro-regions.
Iceland	IMC takes place on a regional basis through regional boards, regional federations and economic development agencies co-owned by the municipalities (Local Government Act n°45/1998). IMC mandatory for small municipalities (less than 8 000 inhabitants) following the decentralisation of social services for disabled people.
Ireland	Shared services programme for waste management regulation and shared services currently being developed.
Israel	Existence of municipal associations
Italy	IMC promoted since 1990 in particular through municipal unions, mountain communities. 2014 Law no. 56 encouraged IMC by strengthening the municipal unions, establishing a minimum threshold is established and extending their scope of tasks. IMC compulsory for small municipalities (less than 5 000 inhabitants). This law also transformed the provinces into IMC bodies, including the 14 metropolitan cities.
Japan	IMC takes place through voluntary Partnership Agreement established under the Local Autonomy Act to be implemented in 2014.

Korea	Local government may establish intergovernmental corporate authorities but little use.
Luxembourg	Around 75 Intercommunal associations with quite a wide range of activities.
Mexico	Since 1999, municipalities can create an inter-municipal association and formalise inter-municipal agreements for the joint supply of public services such as water and sewage, public security and public transport.
Netherlands	Around 700 IMC structures in 2010 concluded under the Joint Regulations Act (<i>Wet Gemeenschappelijke Regelingen</i> or WGR Act) and since 2004 with the Work and Social Security Act (creation of shared services centres e.g. for social services) and functional regions for safety and healthcare.
New Zealand	IMC and shared services between local authorities encouraged by the 2013 Local Government Act 2002 Amendment Bill.
Norway	Since the 1992 Local Government Act and Intermunicipal Companies Act of 29 January 1999, IMC agreements and inter-municipal bodies are widespread. In 2006, an amendment to the Local Government Act widened the range of delegated tasks to IMC bodies to a "host municipality" through an agreement.
Poland	Introduction of the "territorial contracts" in 2014 which are intended to strengthen partnership and improve co-ordination of territorially oriented activities of various stakeholders.
Portugal	IMC encouraged since 2003 laws creating intermunicipal communities (<i>comunidades intermunicipais</i>). In 2013, a new law created 23 compulsory intermunicipal communities regrouping previous urban communities, intermunicipal communities for general purpose and some metropolitan areas created in 2003 and abolished in 2008. Development of multi-level contracts: the Partnership Agreements with the European Commission are used to promote IMC.
Slovak Republic	Municipalities co-operate in the framework of voluntary "joint municipal office" which are multi-purpose and implementing co-ordination arrangements covering 21 different domains. The 2012-203 ESO Programme reinforced the role of joint municipal office for the purposes of managing functions delegated from the state.
Slovenia	2005 amendments to the Financing of Municipalities Act provided financial incentives for voluntary joint municipal administration.
Spain	<i>Mancomunidades</i> are voluntarily established entities to carry out joint projects and provide common services. Law 27/2013 promotes the integration or co-ordination of municipal services through financial incentives.
Sweden	IMC rules defined by the Local Government Act establishing contracts, "common committee" to run joint services in healthcare or education and "municipal federation" (<i>kommunalförbund</i>).
Switzerland	IMC framework and policies are designed and implemented by cantonal constitutions and laws
Turkey	Municipalities can provide jointly some services, especially in rural areas, through municipality unions and unions for irrigation.
United Kingdom	In England, development of "shared Service Agreements" involving collaboration between two or more local authorities and promotion of combined authorities in urban areas. In Scotland, councils are able to set up joint board or joint committee organisations with other councils to provide a service across a combined area of the participating local authorities.
United States	IMC designed and implemented by individual states; 51 146 formal entities in 2012 (schools districts, transport districts, water management, fire services) undergoing a consolidation process. Formal shared services arrangements commonly directed by state government have a 20- to 30-year history of development.

In terms of financing, inter-municipal bodies' structures are most often financed through contributions from municipality members but they usually complement these subsidies with other revenue sources related to the services they provide (user charges and fees). They can also receive grants from the central government. This is a way for the central government to favour co-operation, and has been the practice in several OECD countries (e.g. Estonia, France, Norway and Spain). France is the only OECD country that has systematically set up public institutions for inter-communal co-operation with taxing powers, i.e. able to raise their own sources of tax revenue (*EPCI à fiscalité propre*).

Figure 3.8. From soft agreements to more formalised forms of co-operation in the OECD

Source: Adapted and completed by the OECD based on <http://www.municipal-cooperation.org>.

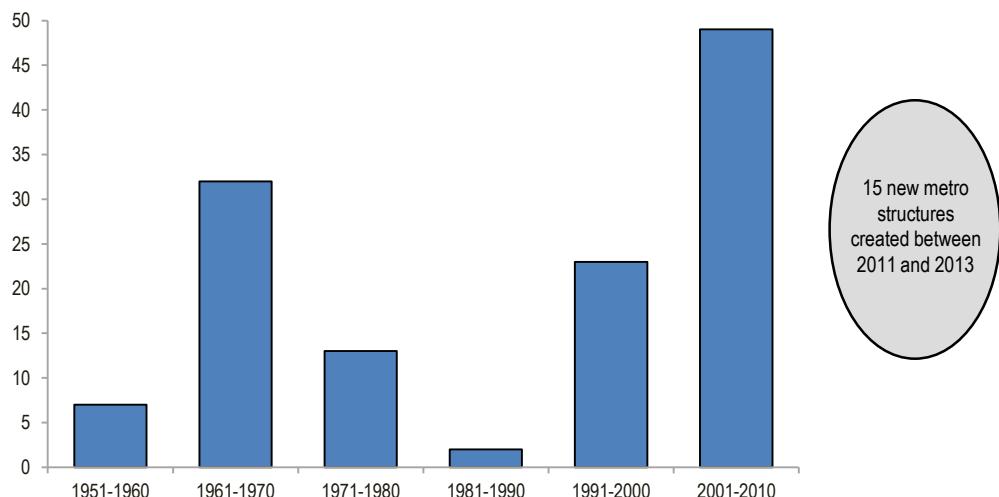
Metropolitan governance

Metropolitan governance reforms aim at addressing the issue of municipal fragmentation in large urban areas. Efficient metropolitan governance has become a hot topic in many countries. Administrative borders in metropolitan areas, based on historical settlement patterns, no longer reflect current human activities or economic and social functional relations (OECD, 2015^[16]). Enhancing co-operation and the co-ordination of public policies on a metropolitan-wide basis, in particular with regard to the provision of public infrastructure and services, aims to improve the quality of life and international competitiveness in large cities.

The number of metropolitan governance authorities has increased considerably and there has been renewed momentum in the number of metropolitan governance bodies created or reformed since the 1990s, against the backdrop of the early 1990s recession and the 2008 financial crisis. Currently, around two-thirds of the metropolitan areas in the OECD have a metropolitan governance body (Ahrend, Gamper and Schumann, 2014^[17]). The additional responsibilities given to metropolitan areas are often linked with infrastructure and planning tasks, such as public transport, environment, and spatial planning, as well as services targeted at local business.

Recent years have seen more and more OECD countries adopting differentiated municipal governance for metropolitan areas. Capital districts with special autonomy often started out in the mid-20th century with lower levels of authority because of restrictions on representation or other elements of self-rule.

Figure 3.9. Number of metropolitan governance structures created or reformed in the OECD, by decade



Source: OECD update based on Ahrend, R., C. Gamper and A. Schumann (2014_[17]), “The OECD Metropolitan Governance Survey: A Quantitative Description of Governance Structures in large Urban Agglomerations”, <http://dx.doi.org/10.1787/5jz43zldh08p-en>.

The latest update of the Regional Authority Index (RAI) (2010-16) included a focus on metropolitan and urban governance (see Box 3.2). Metropolitan and urban government in 45 countries that fulfil the criteria for regional government all contribute to differentiation in subnational governance, but they do so in different ways. Although metropolitan and urban government constitute an additional tier of subnational government in only part of the country, they often exercise authority over a large part of the population. For example, in France, the *communautés urbaine* (urban communities) and *métropoles* (metropolises) involve 1 485 out of a total of more than 36 000 (4.1%) municipalities and exercise authority over about 27.7 million inhabitants which constitutes 43% of the total population. Italian metropolitan cities (*città metropolitana*) are home to almost 22 million out of a total of 59 million people (37% of the total population). Seven combined authorities in the United Kingdom involve 44 constituent local authorities and about 13.5 million inhabitants, which is around 21% of the total population. In some countries, metropolitan and urban government affect almost the whole population. In Portugal Continental (mainland), inter-municipal communities and the metropolitan areas of Lisbon and Porto (*Área Metropolitana de Lisboa/do Porto*) involve all 278 municipalities (out of a total of 308 municipalities including Autonomous Regions of Azores and Madeira), 90% of the total municipalities, and comprise almost 9.8 million out of a total of 10.3 million citizens (95%).

A second way that metropolitan governments may contribute to differentiation in subnational governance is when they have additional competencies when compared to their “peers” within the same government tier. For example, metropolitan cities in Italy (*città metropolitana*) take over the competencies of provinces and are given additional responsibilities for local police services, roads, transport, and spatial and urban planning. The metropolitan city mayor is directly elected. In comparison to provinces, metropolitan cities score higher score on the RAI- policy scope and executive indicators but they have similar scores for institutional depth, fiscal autonomy, and borrowing autonomy. In

Hungary, cities with county rights are allowed to borrow with prior approval by the central government whereas counties have no borrowing autonomy.

Box 3.2. Metropolitan governance as measured by the Regional Authority Index

The Regional Authority Index (RAI) defines metropolitan and urban government in the same way as a regional government, which means that:

1. It is an intermediate tier of government in between local, municipal tier and national government. A sub-metropolitan or sub-urban tier can consist of councils or assemblies established in city districts or in the member municipalities.
2. It is a multi-purpose and not single- or specific-purpose government.
3. It legally exercises competencies and is not a collaboration purely based on a voluntary basis. This means that the competencies of metropolitan and city government are laid down in legislation, either in a specific law or a chapter in a local/regional government law.
4. It has an average population size of 150 000 people or more across units.

Source: Schakel, A. et al. (2018[18]), Final Report on Updating the Regional Authority Index (RAI) for Forty-Five Countries (2010–2016).

A third way in which metropolitan and urbanised governments contribute to differentiation in subnational governance is through special autonomy arrangements that only apply to the capital. Seven capital cities with their own law and which fulfil the criteria of regional government have been identified: Barcelona, Brussels, Bucharest, Copenhagen, Helsinki, Paris and Prague. What sets these capitals apart from other capitals with special laws is that they are a general-purpose government that exercises significant additional authority when compared to other regional government units. For example, Prague is both a municipality and a region and, in contrast to other regions which are completely reliant on intergovernmental grants, Prague can set the property tax rate in its capacity as a municipality. Similarly, Bucharest is a municipality with county rights that, before 1999, had more fiscal and borrowing autonomy when compared to other counties thanks to its legal status as a municipality.

There are 26 metropolitan and urban governments, showing that this type of subnational governance is a relatively recent phenomenon. The general trend in regional authority shows a significant increase from the 1970s onwards. Most subnational and urban governments were established in the 1990s and 2000s. Out of the 11 metropolitan and urban governments that were created before 1990 all but 2 concern one particular area or territory. Out of the 16 metropolitan and urban governments that were set up in or after 1990, 8 concern a singular entity and 8 involve multiple government units.

All metropolitan and urban governments have responsibilities relating to industrial promotion, environmental planning, garbage disposal, public transport, regional spatial planning, regional economic development, recreation, regional parks, tourist promotion, traffic planning, traffic regulation and water supply. Nine out of 24 metropolitan and urban governments score 2 on policy scope because they have (limited) competencies in cultural-education policy (e.g. cultural, sport and recreational facilities, inter-municipal libraries, museums and school buildings) and/or in welfare policy (i.e. hospitals, public health, social housing or social services).

Another notable feature of metropolitan and urban government is their limited fiscal and borrowing autonomy. Nine metropolitan and urban governments rely completely on municipal transfers and user fees whereas 15 can set the rate of a property tax.¹ In addition, 6 metropolitan and urban governments cannot borrow and 15 can only borrow under strict rules and with *ex ante* approval from the central (or higher regional) government. In general, the fiscal capacity and budgetary autonomy of metropolitan and urban government is particularly limited, which makes them more reliant on intergovernmental transfers from the participating municipalities and cities and from higher regional and national governments. This may not only be detrimental for their autonomy but also complicates budgetary negotiations.

Rising role of regions

The Regional Authority Index (RAI) presents a useful way to explore trends in decentralisation across a large number of countries. This index is a comprehensive attempt to measure the real degree of power of intermediate governments, going beyond fiscal indicators. The RAI specifically focuses on regional government, which is defined as an intermediate tier of government between the lowest, local tier and national government, with at least 150 000 inhabitants per regional unit on average. This indicator traces regional authority across 10 dimensions in 81 countries between 1950 and 2010 (Hooghe et al., 2016_[2]; Hooghe, Marks and Schakel, 2010_[19]). The RAI's ten dimensions include fiscal autonomy and borrowing autonomy, but also lawmaking and executive control (Box 3.3; Annex A).

The RAI consists of two components, self-rule and shared rule, each of which has five dimensions. Table 3.4 displays the number of reforms for self-rule and shared rule for each of the 10 dimensions in 81 countries between 1950 and 2010. Two observations are particularly important: i) the total number of reforms affecting self-rule is more than three times larger than the total number of reforms affecting shared rule; ii) a closer look reveals that fiscal indicators have been least subject to reform. Reforms are three times less likely to involve fiscal autonomy and control, and borrowing autonomy and control, rather than other dimensions of authority, policy scope or representation (Figure 3.10).

Box 3.3. Self-rule and shared rule in the RAI

Self-rule is the authority exercised by a regional government over those who live in the region. Self-rule taps into the extent to which a regional government is autonomous rather than deconcentrated (institutional depth), the range of policies for which a regional government is responsible (policy scope), the extent to which a regional government can independently tax its population (tax autonomy), the extent to which a regional government can borrow (borrowing autonomy), and the extent to which a region has an independent legislature and executive (representation).

Shared rule is the authority exercised by a regional government or its representatives in the country as a whole. Shared rule can be exercised through regional representatives in an upper chamber of the national parliament and through intergovernmental meetings with national and other regional governments. Similar to self-rule, regions can have shared rule across a range of dimensions:

- the extent to which regional representatives co-determine national legislation (law making)

- the extent to which regional executives co-determine national legislation (executive control)
- the extent to which regional representatives co-determine the distribution of national tax revenue (fiscal control)
- the extent to which a regional government co-determines subnational and national borrowing constraints (borrowing control)
- and the extent to which regional representation co-determines constitutional change.

Annex A provides further detail on the scores for each of the ten dimensions.

Source: Hooghe, L. et al. (2016^[2]), *Measuring Regional Authority: A Postfunctionalist Theory of Governance*, Oxford University Press, Oxford.

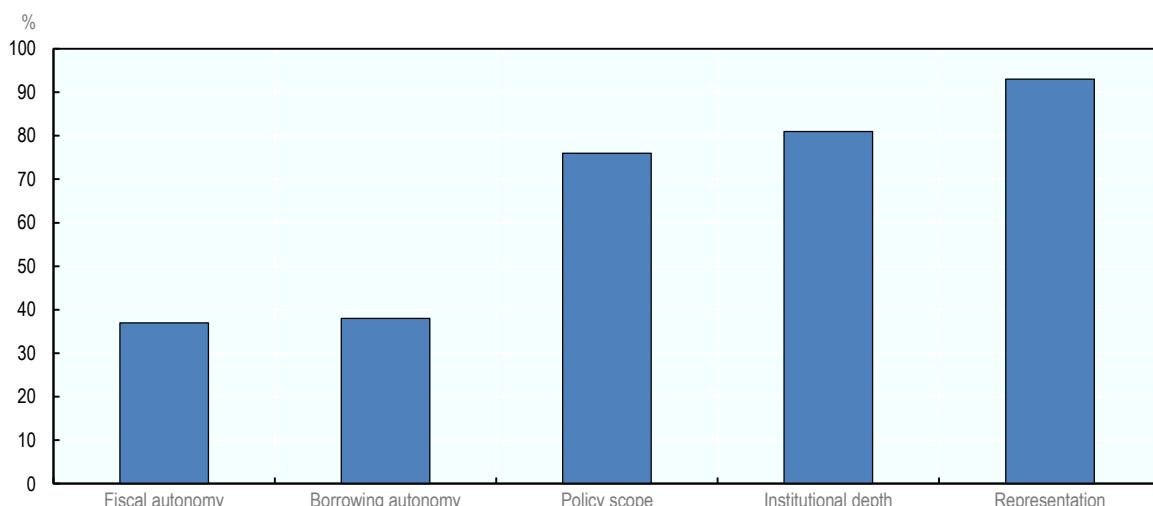
Table 3.3. Number of reforms broken down into ten dimensions of regional authority

Dimension	Positive	Negative	Dimension	Positive	Negative
Institutional depth	81	27	Law making	21	15
Policy scope	76	20	Executive control	21	1
Fiscal autonomy	37	11	Fiscal control	17	7
Borrowing autonomy	38	16	Borrowing control	11	1
Representation	93	29	Constitutional reform	27	17
Self-rule	325	103	Shared rule	97	41

Note: Shown are the number of positive and negative reforms for 5 dimensions of self-rule and 5 dimensions of shared rule for 81 countries for 1950-2010. A reform is included when there is at least a 0.1 change in the magnitude of a country RAI-score in a particular year.

Source: Schakel, A. et al. (2018^[18]), *Final Report on Updating the Regional Authority Index (RAI) for Forty-Five Countries (2010-2016)*.

Figure 3.10. Type of reforms strengthening self-rule in regions



Source: Schakel, A. et al. (2018^[18]), *Final Report on Updating the Regional Authority Index (RAI) for Forty-Five Countries (2010-2016)*.

All regions are concerned about the increase in the RAI (Box 3.3). Figure 3.11 displays average RAI-scores for American, Asian and European countries since 1950. A striking observation is a clear trend of increasing regional authority across the three groups of countries and this trend is especially noticeable from 1970 onwards. Average regional authority was 55% higher in 2010 than in 1950. Of the 81 countries covered by the RAI, 52 experienced a net increase in the degree of regional authority and only nine experienced a net decline.²

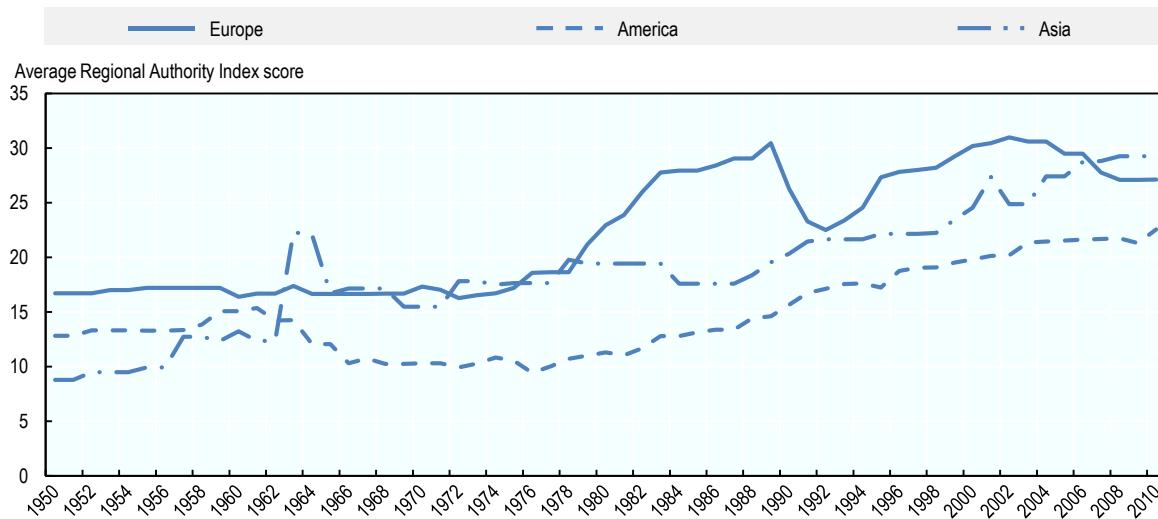
Box 3.4. RAI score in Latin America, Asia and Europe

The average RAI-score in 1970 was 10.3 for America, 15.5 for Asia, and 17.3 for Europe. In 2010 the average RAI-score increased to 22.6 in America, to 29.3 in Asia, and to 27.1 in Europe. An increase of 10 to 14 points indicates that, on average, each country included in the RAI has introduced a fully equipped intermediate tier of government. A 12-point increase in the RAI is equal to establishing a general purpose regional tier subject to central government veto (+2 points), which has authoritative competency in economic and cultural-educational policy (+2 points), which can set the base and rate of a minor tax (+2 points), which can borrow without prior authorisation by central government (+2 points), and which has a directly elected assembly (+2 points) and a regional executive appointed by the regional assembly or directly elected (+2 points).

Source: Schakel, A. et al. (2018_[18]), *Final Report on Updating the Regional Authority Index (RAI) for Forty-Five Countries (2010-2016)*.

The motivation for regionalisation reforms varies across countries. The size of the country matters: large countries tend to have more layers of subnational governments (OECD-UCLG, 2016_[20]). However, many countries of a relatively modest size have also introduced or strengthened a regional level in recent decades. The main objectives behind regionalisation reforms are an upscale in governance to generate economies of scale for public service provision, for example in the health or public transport sectors. Regions may also better respond to widening functional labour markets. Other objectives are to improve co-ordination between municipalities and intermediate levels of government in such areas as infrastructure delivery, spatial planning and land-use, for example. Larger regions are also expected to be more competitive: they have higher critical mass, more resources to implement effective regional development strategies, and the ability to foster intra-regional co-ordination and to implement more integrated territorial planning. They may better target regional comparative advantages through access to local knowledge, compared to the national government or to fragmented local governments.

Several countries have created new regions, notably in East European countries in the context of EU enlargement. Others have strengthened existing regions: this is the case in recent or current reforms in Nordic countries, France or Italy. In several Nordic and Central and East European countries, responsibilities such as higher education, specialised healthcare and regional public transport were reassigned from the municipal and the central government levels to a newly created regional level. However, in recent years some European countries have also gone in the opposite direction and have reduced the role of regions. This is the case in Denmark with a reduction in the responsibilities assigned to regions, for example, or in Hungary through recentralisation reforms.

Figure 3.11. Regionalisation in America, Asia and Europe since 1950

Note: Shown are average Regional Authority Index scores for 29 American, 11 Asian and 41 European countries. *America*: Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Cuba, the Dominican Republic, Ecuador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, El Salvador, Suriname, Trinidad and Tobago, Uruguay, the United States, and Venezuela. *Asia*: Australia, Brunei, Indonesia, Japan, Malaysia, New Zealand, the Philippines, Singapore, South Korea, Thailand, and Timor Leste. *Europe*: Albania, Austria, Belgium, Bulgaria, Bosnia and Herzegovina, Croatia, Cyprus,³ the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Kosovo,⁴ Latvia, Lithuania, Luxembourg, Malta, Montenegro, the Netherlands, Norway, Poland, Portugal, Romania, Russia, Serbia and Montenegro (until 2006), Serbia, the Slovak Republic, Slovenia, Spain, Sweden, Switzerland, the United Kingdom and Turkey.

Source: Schakel, A. et al. (2018[18]), *Final Report on Updating the Regional Authority Index (RAI) for Forty-Five Countries (2010-2016)*.

Table 3.4. Main objectives of regionalisation reforms

Broad policy objective	Governance and management objectives	Solve current challenges	Counterarguments
Make economies of scale in public service provision	<ul style="list-style-type: none"> ● Improved efficiency of health system provision ● Economies of scale in labour market services, public transport, infrastructure ● Internalisation of spillovers, better quality public service provision ● Improved co-ordination between local governments 	<ul style="list-style-type: none"> ● Fragmentation of responsibilities for public service delivery in many policy areas (infrastructure, transport, healthcare, housing, etc.) 	<ul style="list-style-type: none"> ● Risk of creating clumsy constructions ● Optimal size debate: very hard to identify an optimal size for efficient public service delivery ● Efficiency-related counterarguments, presented by those who believe that smaller units may be more efficient and less bureaucratic since they have better local knowledge, can choose measures more adapted to the needs of their clients and are better able to adjust service provision to variations in local demand
Enhance competitiveness and regional growth	<ul style="list-style-type: none"> ● Bigger regions would have higher critical mass, more resources to implement effective regional development strategies, the ability to foster intra-regional co-ordination and to implement more integrated territorial planning ● Better access to local knowledge, remedy to asymmetries of information ● For public goods with strong local/regional externalities – related to regional development such as innovation, labour market policy as spatial planning and public transports – it makes sense for the regional government to have more responsibility for reasons of proximity or local knowledge and a better match of policies with functional areas. For others, national governments may be in the best position for reasons of scale or capacity, to provide services efficiently⁵ 	<ul style="list-style-type: none"> ● Lack of regional development strategies – strategies are either too fragmented or only top-down from the national government ● Need for improved spatial planning at the regional scale ● Need for improved synergies across sectoral policies (e.g. infrastructure, innovation, higher education, housing, labour market) ● Need for increased co-operation: to respond to the widening functional labour market region trend 	<ul style="list-style-type: none"> ● Local labour markets are sometimes smaller than individual municipalities, co-ordination challenges could be addressed by inter-municipal co-ordination arrangements in some cases ● Risk of insufficient transfer of resources and lack of regional capacities to conduct appropriate strategic planning in remote regions
Enhance local democracy	<ul style="list-style-type: none"> ● Enhanced local democracy and transparency in decision making through direct election of regional bodies 	<ul style="list-style-type: none"> ● Limits of inter-municipal co-operation: horizontal co-operation comes at the cost of a less transparent decision-making process, as regional co-operation councils are indirectly elected, thus reducing voter control and transparency of the decision-making process 	<ul style="list-style-type: none"> ● No evidence of citizen support to regionalisation reforms due to the lack of consultation and the fact that counties are very old territorial units, with a strong identity ● More authority for regional government hence regional government becomes more important, yet turnout in regional elections is low. This challenge is more important for metropolitan and urban government which often have indirectly elected assemblies, making the “chain of accountability” between voters and representatives more indirect

Responsibilities assigned to regions

Compared to regions in unitary countries, those in federal countries tend to have greater policy scope and some authority to implement or shape major social policy areas, such as health, education, and social spending. In federal countries, regional tiers are generally in charge of borrowing, while in unitary countries there is greater variation. In contrast to local governments, which are often general-purpose, it is not uncommon for regions to be deconcentrated, possess dual executives, or have more limited autonomy, particularly in unitary countries.

Almost all regions that have general-purpose government play a role in the co-ordination and administration of education (often secondary), healthcare (specialised and hospital), social services, infrastructure and economic development, yet levels of authority vary widely. Some self-governing regions have very little policy scope, such as the Danish *Regioner* or Spanish *Provincias*. At the opposite end of the spectrum are the Australian States, Quebec in Canada, and the Swiss Cantons, which have full policy autonomy and also authority over immigration⁶, citizenship and residency.

Some regional governments depend completely on the centre and/or their municipalities for funding, while others have greater tax autonomy and thus extensive own resources, as well as constitutionally protected shares of central government transfers or taxes (tax sharing). Those with full control of major taxes include for example Canada, the Swiss cantons and the United States.

In the two-tier system of subnational governments, the regional level between the municipalities and the central government, because it operates on a larger scale usually provides services of regional interest, which benefit from economies of scale, generate spillovers, involve redistribution and are required to meet the same standards across the jurisdiction (OECD, 2017_[21]). The regional tier may also facilitate co-operation and strategic planning.

In a three-tier system, as in France, Italy, Poland and Spain, the breakdown can be complex, sometimes resulting in duplication, overlap and co-ordination challenges. However, in recent decades, the intermediate level in a majority of these countries has lost many of its powers and responsibilities in favour of regions, which have gained more importance. Intermediate governments are now mainly responsible for administrative and delegated tasks, and have small budgets and in general no, or only limited, taxing powers.

Policy and governance implications of increasing regional authority

Regionalisation trends are clear in OECD countries and around the world, and they raise several policy and governance implications. They increase the need for co-ordination across government tiers and the need for clarification in the assignment of responsibilities, in order to avoid overlap. The fact that fiscal autonomy and control have not been strengthened at the same pace as other dimensions (like policy scope) implies that regions depend quite heavily on the national government for financing. This may curb the autonomy of regional government to the extent that central government transfers come with strings attached. It is quite likely that regionalisation trends will continue to progress in the coming decades, to generate economies of scale in public service delivery and provide more effective regional development policies, given persistent territorial disparities. However, in the current context of crisis of democracies, there is also a call for stronger municipalities, which is the government tier closest to citizens. Scale issues thus need to be balanced with accountability and democratic issues. One trend that might

increase as well is the differentiation of responsibilities assigned to different regions. The following section will explore this trend in depth.

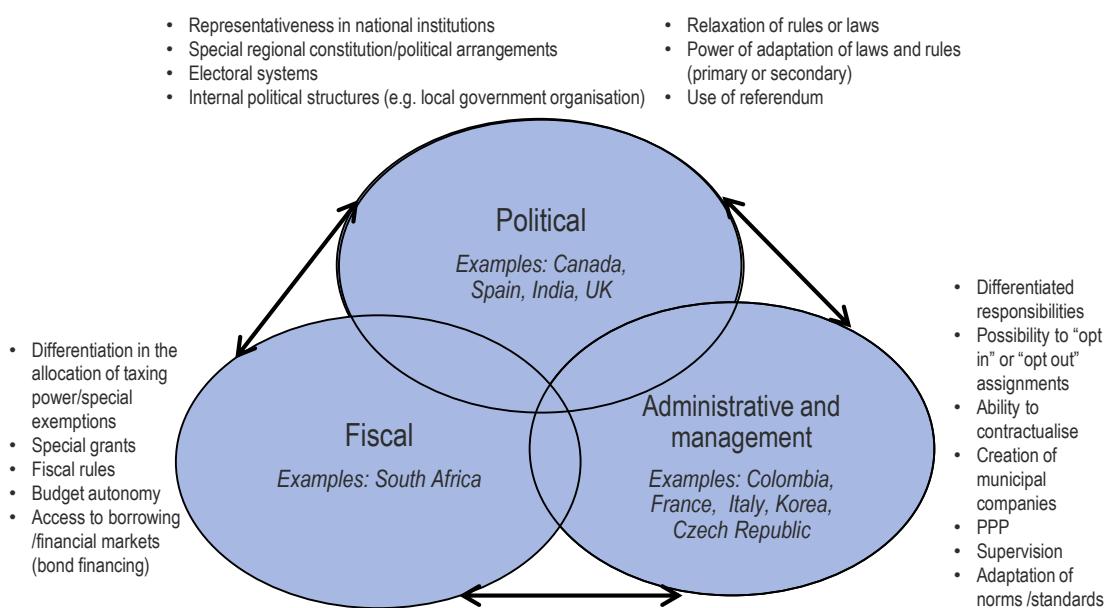
Growing asymmetric decentralisation

Asymmetric arrangements have been common since at least the 1950s and are still growing in popularity. In 1950, around half of the countries covered by the Regional Authority Index (RAI) had some kind of differentiated governance at the regional level. In 2010, almost two-thirds of the countries in the RAI had implemented asymmetric arrangements in some form. Asymmetric decentralisation, however, is in transition: between the 1950s and the 1970s asymmetric arrangements occurred mostly at a regional level, whereas the present trend seems to apply asymmetric decentralisation to major urban areas. There can be political, economic or administrative motives for asymmetric decentralisation (Bird and Ebel, 2006^[22]). This section will review recent trends in asymmetric decentralisation in OECD countries.

What is asymmetric decentralisation?

Asymmetric decentralisation occurs when governments at the same subnational government level have different political, administrative or fiscal powers (Congleton, 2015^[23]) (Figure 3.12). Political asymmetric decentralisation refers to situations where some regions or subnational governments have been given political self-rule that deviates from the norm or average assignment.

Figure 3.12. Three main types of asymmetric decentralisation



One common way to categorise asymmetric decentralisation is to divide the policies into *de jure* and *de facto* arrangements (Martinez-Vazquez, 2007^[24]; Bird and Ebel, 2006^[22]). *De jure* asymmetric decentralisation is based on the special legal status of a certain region. In some cases, the status is outlined in the constitution, but more often asymmetric treatment is established in the ordinary law (sometimes both).⁷ The regions with special *de jure* status often enjoy considerably broader political autonomy than other regions.

Politically motivated asymmetry usually leads to administrative and fiscal asymmetry as well.

Even if subnational governments belonging to the same government tier are treated symmetrically in terms of the politico-legal system, there might still be *de facto* asymmetry in implementation. This administrative asymmetry often aims to take the different capacities of subnational governments into account. Administrative asymmetry may, for example, include sequencing a national policy so that the subnational governments that fulfil certain predetermined standards are given greater autonomy in spending and revenue. The rest of the subnational governments could then “grow into this role” over time.

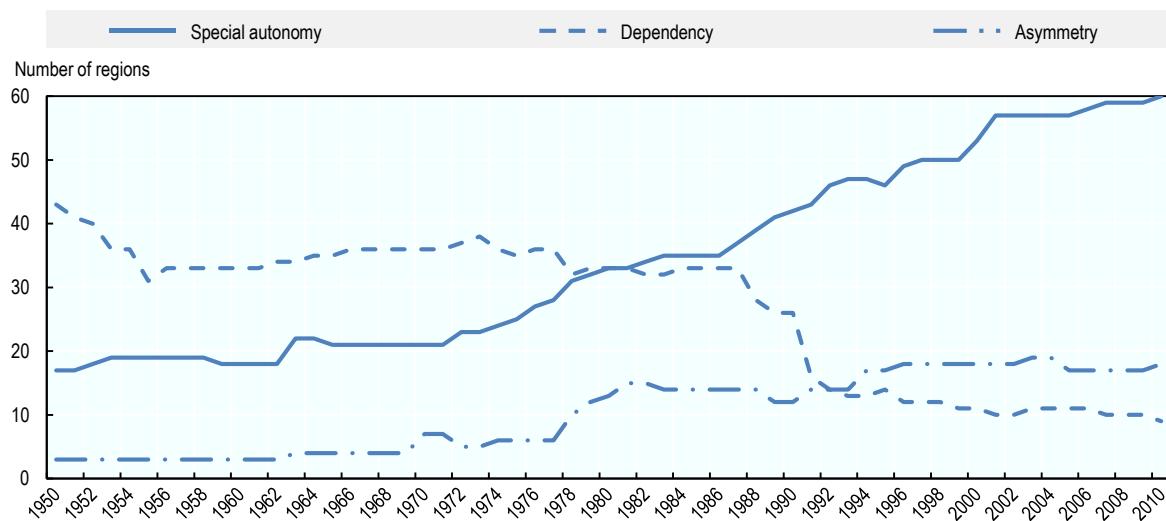
Asymmetric fiscal arrangements consist of a wide variety of measures including special spending responsibilities, revenue bases or taxation rights and additional transfers. The main forms of asymmetric fiscal decentralisation can be summarised as follows:

- *Differential spending assignments.* For example, some regions or subnational governments may be assigned tasks in specific services, which are otherwise provided by the central government or a higher level of subnational government.
- *Differential revenue autonomies.* The subnational governments with more capacity may be given more tax autonomy than others. Asymmetric autonomy could also be used for collecting user fees or selling property.
- *Differential treatment in the transfer system.* In this case, the regions with unique service needs or an exceptional operating environment may justify the use of special purpose grants or use of certain criteria in formula-based grants. Specific transfers may be used as an alternative to differential revenue autonomies.
- *Differential fiscal rules.* Some subnational governments may be given more room for manoeuvre in borrowing for example. This could be the case if the subnational government has special needs for public investments and if it is capable of fulfilling its obligations.

An increasing trend in asymmetric decentralisation

During the last seven decades or so, asymmetric arrangements have become more common especially among unitary countries. In 1950, some 45% of the countries covered by the RAI and with regions had some kind of differentiated governance (autonomy, asymmetry or dependence). By 2010, this figure had increased to 62% (Hooghe et al., 2016[2]) (Figure 3.13).

Figure 3.13. Number of special autonomous regions, dependencies and asymmetric regions in 81 countries since 1950



Note: Asymmetric and special autonomous regions and dependencies are subject to a different kind of autonomy regime than standard regions. Dependencies are directly ruled by central government and have very limited autonomy. The decline in the number of dependencies is largely based on the change of dependencies into standard regions in South America.

Source: Hooghe, L. et al. (2016[2]), *Measuring Regional Authority: A Postfunctionalist Theory of Governance*, Oxford University Press, Oxford.

Asymmetric arrangements are increasing in metropolitan areas

Asymmetric decentralisation is often applied at three different scales: regional (state/province), metropolitan and local (Table 3.5). Asymmetric decentralisation trends are, however, changing: whereas during the past decades the asymmetric arrangements occurred mostly at the regional level, the present trend seems to apply asymmetric decentralisation to large cities or for selected local governments. One reason for this shift may be linked to a better understanding and acceptance of the benefits of urbanisation and agglomeration economies.

Table 3.5. Different scales of asymmetric decentralisation

Regional	Metropolitan	Local
<ul style="list-style-type: none"> The most common form In 1950, around half of the countries covered by the Regional Authority Index (RAI) had some kind of differentiated governance at the regional level In 2010, almost two-thirds of countries in RAI had implemented asymmetric arrangements in some form Rising trend Long-term trend 	<ul style="list-style-type: none"> Since the 1950s: specific status for capital cities Since 1990s: increase in metropolitan governance to address specific challenges and capacities of metro regions 87 new metro structures created since 1991 compared to 14 between 1971 and 1991 	<ul style="list-style-type: none"> Different sets of responsibilities for different municipalities, depending on their capacities Municipal classifications, based on population, access to public services, budget, performance Urban/rural municipalities: classification may just statistical or lead to differentiation in funding or responsibilities

Asymmetric arrangements are increasing especially in unitary countries

Asymmetry is often a basic characteristic in federal countries. There are however different gradients of asymmetry: some federal countries are highly asymmetric, such as Canada, India, Russia and Spain. Some federations tend to favour symmetry, like Australia, Austria, Germany, Switzerland and the United States. However, even the most “symmetric federations” (e.g. Switzerland and the US) have elements of asymmetry (Bird, 2003^[25]; Dafflon, 2006^[26]).

In unitary states, symmetry is often one of the basic principles of the state, motivated by equity and integration of different parts of the country, such as in Chile and France. However, some unitary states have strong elements of asymmetry, in particular recognising a different status in territories with a strong history/identity (e.g. in Italy and the United Kingdom), as well as peripheral territories such as outermost regions, islands and outlying regions (e.g. Finland, France and Portugal).

Asymmetric decentralisation is increasing in unitary countries, based on new motives, including metropolitan governance arrangements, asymmetric administrative decentralisation and to give more responsibilities to regions with greater capacities. This is revealing a convergence between unitary and federal countries in the trend toward greater differentiated governance at the subnational level (Table 3.6).

Table 3.6. Asymmetric decentralisation/federalism

Federal countries	Unitary countries
<ul style="list-style-type: none"> Asymmetry is often a basic characteristic of federations. There are however different degrees of asymmetry: <ul style="list-style-type: none"> - Asymmetric: Belgium, Canada, India, Russia, Spain. - More symmetric federations: Australia, Austria, Germany, Switzerland, United States. However, even the most “symmetric federations” have elements of asymmetry, e.g. United States. 	<ul style="list-style-type: none"> Symmetry is often one of the leading principles of a unitary state (with unity and integration). <ul style="list-style-type: none"> However, some unitary states have strong elements of asymmetry, in particular to recognising a different status in territories with a strong history/identity (Italy, United Kingdom) as well as peripheral territories such as outermost regions, islands, outlying regions (Finland, France, Portugal). Asymmetric decentralisation is increasing, based on new motivations.
Greater convergence in recent years	

Examples of asymmetric decentralisation

Political asymmetric decentralisation

Political asymmetric decentralisation is commonly practised among OECD countries and elsewhere. This type of decentralisation generally takes place at the regional (state/province) level. In Italy, there are currently 5 regions (out of 20) with a special constitutional status, approved by the Italian parliament. Defined by the Italian constitution in 1948, the islands of Sardinia and Sicily and the Alpine regions of Friuli-Venezia Giulia,⁸ Trentino Alto Adige and Valle d’Aosta have been given special statute with the aim of avoiding separatist movements and to protect linguistic minorities. Asymmetric decentralisation means that these regions have broad legislative powers and considerable financial autonomy. For example, the Valle d’Aosta retains 90% of all its

taxes, and Sicily at times 100%. While the 2001 reform of the Italian constitution gave all the Italian regions significant powers in the legislative field, the latest developments in Italy (especially since 2009) indicate that the decentralisation trend has reversed and that recentralisation seems to be a current trend (memorandum of Council of Europe 2015). If the centralisation trend prevails in all the regions except those with asymmetric treatment, the differences in self-government between the five special regions and the 15 ordinary regions are expected to increase. Moreover, some recent developments indicate that differentiation is still planned in some cases. The regions of Emilia Romagna, Lombardy and Veneto have recently signed a tentative deal with the Italian government for more autonomy, though this arrangement still needs to be accepted in Italy's parliament before taking effect.⁹

The French territory of Corsica, previously one of the French departments, gained a special regional status in 1991. Corsica has its own institutions (the Corsican Assembly and the Executive Council of Corsica, each with a president) and more powers than other French regions. However, in general, the legislation governing the French regions applies also to Corsica if not defined otherwise in legislation. The regional reform implemented in 2015 reduced the number of French regions from 22 to 13, not including Corsica, however (Congress of Local and Regional Authorities 2016).

In Canada, while the Canadian constitution is based on a unified approach, it does enable asymmetric arrangements for Canadian provinces. More specifically, asymmetric decentralisation in Canada is mostly based on "menu federalism", where the "opt in" or "opt out" choices are made available to all provinces. The province of Quebec has been using this option more frequently than other provinces (Smith 2005; Milne 2005). In general, Quebec is an example of *de jure* political asymmetric decentralisation that is based on historical, cultural and linguistic reasons. Being the largest province and second most populous of Canada's ten provinces, French-speaking Quebec is an influential member of Canada's federal government. This is in contrast to a situation in many other countries, where the asymmetric arrangements are applied mostly to regions of small economic importance. Quebec has had and used specific powers for example in healthcare provision, the pension system, with the position of the French language in government, and immigration screening. Although the secessionist movement in Quebec has gained more support since the 1980s, the majority of voters in referendums (in 1980 and 1995) for independence, voted against secession. As for the effectiveness of Canada's asymmetric decentralisation model, while there seems to be continuous discussion about equal treatment of provinces in the federation, the main goal to keep the Canadian federation united has been reached (Bird and Vaillancourt, 2007^[27]).

In the United Kingdom, since the devolution in 1998-99 of certain powers and responsibilities to regional elected bodies, local government organisation and functions are defined and reformed by the UK government (and parliament) for England, and by devolved nations for Northern Ireland, Scotland and Wales.

In Portugal, there is also an asymmetric organisation with two autonomous regions – Azores and Madeira – having legislative responsibilities as overseas territories (there is no self-governing region on the mainland). These autonomous regions are responsible for the financing and general supervision of local authorities within their territory, and also have the legislative power to create, dissolve and alter local government boundaries in accordance with the national laws.

Administrative asymmetric decentralisation

Sweden is an example of a highly decentralised country where the subnational government levels have important tasks and a strong autonomous position, and where an asymmetric and innovative approach to decentralisation has prevailed. In Sweden, there is a long history of asymmetric decentralisation. The geographic, demographic and socio-economic differences between counties are significant, and this has motivated the central government to permit bottom-up initiatives and reforms that aim to adjust governance structures and competencies according to territorial capacity. While an “across the board” regional reform is politically difficult, counties themselves have gradually and voluntarily implemented regional reform themselves.

In Finland, the government is currently planning a major regional reform to be launched in 2020.¹⁰ The reform would transfer health and social services, as well as regional development and labour services, from municipalities (healthcare and social services) and the central government (regional development and labour services) to the 18 new counties. Healthcare would be organised in an asymmetric fashion, as the most demanding hospital services, including emergency services, would be provided by only 12 regions. The remaining six regions were considered too weak to be able to arrange the most challenging specialised healthcare services. In addition, the Helsinki Metropolitan Area in the Uusimaa region would have a special arrangement in regional development and labour services.

In France, in December 2017, several French deputies presented a bill aimed at implementing a differentiation and simplification of standards/norms applicable in the territories. The purpose of the bill is to replace regulatory standards with measures adapted to a diversity of local situations. The proposed law is based on the observation that there is a proliferation of standards applicable to territories. The bill in question also proposes the creation of a principle of subsidiarity by entrusting the local authorities with the adaptation of the norms of application of the law. The bill proposes to allow differentiation of norms and standards (e.g. building, public works, environment, etc.) according to spatial or local government particularities.

In the United Kingdom, the “Cities and Local Government Devolution Act 2016” is considered an important step towards decentralisation. It makes various amendments to the 2009 Act to allow greater devolution of powers to combined authorities (housing, transport, planning and policing powers) and to introduce directly-elected mayors, thanks to “Devolution Deals”, which built on previous “city deals” (OECD, 2017^[11]). The New Devolution Deals also include fiscal policies, which are discussed below in the section describing fiscal asymmetric decentralisation.

Another interesting but perhaps somewhat less common motivation for asymmetric decentralisation has been to deregulate and simplify government guidance of local governments. Over time, the accumulating normative regulation has become an obstacle for efficient public service provision and reforms. Deregulation of subnational government services is a difficult task, however. Therefore, many governments have often decided to proceed carefully, for example by experimenting. An example of this is Denmark, where between 2012 and 2015, nine local municipalities in Denmark were granted exemptions from government rules and documentation requirements in order to test new ways of carrying out their tasks, in a policy experiment known as the “Free Municipality” initiative.^[11]

Fiscal asymmetric decentralisation

Over the past decades, the central government in Spain has devolved competencies asymmetrically to subnational governments. The so-called Foral Regime, autonomous communities (i.e. the Basque Country and Navarra), have a special constitutional status and an autonomous taxing authority, whereas other regions have limited local taxing authority. The Foral Regime regions are responsible for tax administration and have autonomy to set rates and bases (albeit with some limitations). The main tax bases such as income, corporate, wealth, inheritance and wealth transfers are fully administered by these regional governments. To compensate for the services that the central government provides these regions, the regions pay an amount to the central government. In terms of spending responsibilities, the Foral Regime does not differ from other Spanish regions (Garcia-Milà and McGuire, 2007^[28]).

In the United Kingdom, the capital financing of local governments provides an example of asymmetric fiscal decentralisation. While borrowing from the Public Works Loan Board has been the most common form of capital financing of local governments in the United Kingdom, new ways to access capital finance for local infrastructure investment have also been developed. For instance, in 2013-14, the UK government has introduced tax increment financing schemes, which allow local authorities to borrow against future growth in business rate receipts. Another example is the “New Development Deal”, which benefits particularly cities with special status as defined by central government. The 2012 Budget set a limit of GBP 150 million that could be borrowed via New Development Deals: the funding would only be available to “core cities” (House of Commons, 2016).

In South Africa, the 278 municipalities have different fiscal and administrative capacities. The South African government has adopted a differentiated decentralisation approach, particularly with respect to municipal funding. In order to accomplish this, several classifications are used to group municipalities. The 1996 constitution provides for three categories: A (metropolitan municipalities), B (local municipalities) and C (district municipalities). Other classifications exist in other areas, such as the Municipal Infrastructure Investment Framework Investment that defines seven categories based on spatial characteristics, size of institution and budget, and population variables, among others. The National Treasury also classifies municipalities into six “performance groups” using economic, demographic and performance variables such as access to basic services, poverty rate, municipal viability, staff vacancy, municipal debt, population density and size of the municipality’s economy. As underlined by the Financial and Fiscal Commission, the different classification methodologies highlighted above recognise that municipalities need differentiated approaches that take into consideration their different characteristics and needs. However, the South African Financial and Fiscal Commission has argued that a differentiation approach is not always clear, and some classifications are not always useful for making decisions or allocating resources. This is because categorisation often depends on the policy purpose and often detracts from looking at the links between rural and urban municipalities. In addition, the large volume of classification methodologies may undermine co-ordinated decision-making and intervention strategies (OECD, 2017^[21]).

In Colombia, the country’s 1 101 municipalities are responsible for providing electricity, urban transport, cadastre (land registry), local planning and municipal police. Municipalities are grouped into “certified” or “non-certified” units: only certified municipalities are allowed to provide important services such as health, education, water

and sanitation. If the municipality is considered too weak or it is otherwise ineligible for service provision, the service is provided by the upper (department) government level (OECD-UCLG, 2016_[20]; OECD, 2014_[29]).

In Norway, the small rural local governments with substantial tax revenue from hydropower plants provide another example of asymmetric fiscal decentralisation. The municipalities where the power plants are located receive taxes and other revenues from the power company. These revenues are considered compensation for environmental damages and have been important for generating local support for projects that are profitable for society as a whole. The average total revenue per capita among local governments with hydropower revenue was NOK 32 600 (USD 6 520) in 2007. In comparison, the revenues for all other local governments were NOK 28 300 (USD 5 430) (Borge, Parmer and Torvik, 2015_[30]).

In Sweden, the intergovernmental grant system is an example of “Robin Hood” equalisation, which evens out a considerable share of differences in subnational government revenue bases and service costs. A rather detailed formula is used to define the grants for subnational governments. While the transfer system is primarily based on general grants, also some discretionary and earmarked grants have been used. The so-called “structural grants” are related to regional policy and their aim is to strengthen municipalities with a small population, with decreased population and/or with a problematic labour market. Structural grants mainly benefit the more remote municipalities, for example in Norrland County (OECD, 2017_[31]).

Table 3.7. Asymmetric decentralisation by type and scale, some examples of practices

	Political	Administrative	Fiscal
Regional	<ul style="list-style-type: none"> • Italy: Five regions with special constitutional status. • France: The French territory of Corsica has a special regional status. • Portugal: The autonomous regions of Madeira and Azores have special legislative responsibilities • Canada: Province of Quebec has used actively the “opt in, opt out” choices available to all provinces. 	<ul style="list-style-type: none"> • Sweden: A voluntary regionalisation reform from 1990s until 2018 in terms of political representation and responsibilities in different regions and in different phases. Since the beginning of 2019 all Swedish counties have been responsible (by law) for regional development. 	<ul style="list-style-type: none"> • Spain: The autonomous taxing authority of “Foral Regime” autonomous communities.
Metropolitan	-	<ul style="list-style-type: none"> • France: 14 metropolises will be granted greater responsibilities than “standard” municipalities • Italy: 14 metropolitan cities created to administer large urban areas. 	<ul style="list-style-type: none"> • UK: Special investment funding for core cities. • US: Some states assign a portion of state tax revenues to municipalities with a substantial share of the state population (New York City, St. Louis, Kansas City). • Germany: The “City-States” like Berlin have both state and local government responsibilities and revenues.
Local	-	<ul style="list-style-type: none"> • Denmark: Free municipality experiment in order to simplify regulation. • Czech Republic: Limited number of municipalities perform central government delegated functions on behalf of smaller surrounding municipalities. 	<ul style="list-style-type: none"> • Colombia: Royalty revenues for municipalities in certain mining/oil regions. • Norway: Hydropower revenues for specific municipalities. • Sweden: Special grants for the most rural/remote municipalities.

Source: Allain-Dupré, D., I. Chatry and A. Moisio (forthcoming^[32]), “Asymmetric decentralisation: Trends, challenges and policy implications”, OECD, Paris.

Policy implications

There are clear trends showing greater use of asymmetric decentralisation arrangements in the OECD and around the world. The trends also indicate that once adopted, asymmetric arrangements are maintained in the long term. Of the countries with differentiated decentralisation arrangements in 1950, every one still had differentiated regions in 2010, while 10 of the 24 countries without differentiation in 1950 included differentiated regions by 2010 (Hooghe et al., 2016^[2]).

There is no blueprint or optimal strategy for choosing between an asymmetric or symmetric approach because the optimal strategy is usually case specific and depends on local circumstances. Nonetheless, some observations and conclusions can be made based on the economics literature and experiences from practical implementation. This section aims to shed light on the pros and cons of asymmetric arrangements based on key policy considerations. There are benefits and challenges associated with asymmetric decentralisation. Benefits are linked to the fact that institutional and fiscal frameworks are

better targeted to local capacities, and may allow a better response to local needs. In general, asymmetric decentralisation favours experimentation, learning-by-doing and innovation in policymaking. Ultimately, it represents an advanced form of place-based policy. The challenges of asymmetric decentralisation are associated with the cost of co-ordinating a complex system that may be unclear for citizens and lead to accountability challenges, notably at the metropolitan level. Other potential challenges include the increasing disparities in capacity across regions, which would call for adequate equalisation systems.

Sequencing decentralisation reforms may help central and subnational governments learn from successes and mistakes and take steps to revise the reform if needed. In this way asymmetric decentralisation can be seen as a form of experimentation and “menu federalism”, where subnational governments voluntarily choose the tasks that best serve their own interests (Congleton, 2015^[23]). Asymmetric decentralisation also helps implement tailored governance frameworks and place-based regional policies. For example, the effects of major exogenous shocks such as natural disasters or climate change usually affect different regions differently. Accommodating diverse preferences for political and fiscal autonomy across regions may also mitigate separatist movements and help maintain political stability.

Perhaps the most significant risk of asymmetric decentralisation relates to the fact that, by definition, asymmetric arrangements do not directly promote equal treatment of subnational governments and citizens. In some cases, asymmetric decentralisation may result in a perception that asymmetry means deviation from an overall objective of equality. Spending assignments with a clear redistributive function such as education, health and social services could be examples of such services. In addition, there may be a risk that asymmetric decentralisation is perceived as support for the wealthiest regions or subnational governments. The “favoured” governments may be able to attract citizens and business from other subnational governments, which could accelerate the differentiated economic and social development between regions (Congleton, 2006^[33]). If widely applied, asymmetric arrangements may reduce the transparency and accountability of governance and result in complex administrative systems (Bahl and Martinez-Vazquez, 2005^[34]). As in with decentralisation in general, the effects and outcomes of asymmetric decentralisation depend on implementation.

Shared responsibilities, mutual dependence and a renewed role for central governments

Decentralisation policies affect subnational governments, certainly, but also national governments. They imply a renewed role for central governments, one that is more strategic but also more focused on setting the conditions for proper co-ordination and alignment of policy objectives, monitoring the performance of regions and cities, and ensuring the balanced development of all parts of the national territory. Given that most responsibilities are shared, decentralisation policies imply managing mutual dependence to achieve common objectives.

Most responsibilities are being shared between the central and subnational governments

As highlighted in Chapter 2, most responsibilities – apart from defence and monetary policy – are shared among levels of government. The extent of responsibility sharing also depends on the service in question. For example, responsibilities tend to be more

frequently shared in public transport than in childcare or elderly care (OECD, 2016^[35]). Some examples of commonly shared responsibilities include:

- *Physical infrastructure* and its related public investment are among the most commonly shared responsibilities (OECD, 2014^[36]). Subnational governments are generally responsible for local roads and local transport infrastructure. Higher levels of government generally manage investments with high externalities.
- *Education* is the most common major public service to be shared substantively across multiple tiers of government (OECD, 2016^[35]; OECD, 2016^[37]). In most OECD countries, lower levels of government are responsible for managing and funding lower levels of schooling (mainly pre-elementary, primary and sometimes lower secondary education) whereas responsibility for secondary, and in particular upper secondary, schooling rests more often with provincial/regional or central levels. In addition, central governments establish framework legislation while local governments are usually responsible for maintaining and constructing physical infrastructure and the paying staff, though in many cases without actual authority over hiring or salary.
- *Healthcare* is usually more centralised than education because of high system complexity, with specific roles for different levels of government but often less autonomy (OECD, 2016^[37]).
- *Social assistance or welfare* is much more varied and is more likely to be jointly provided because of the strongly redistributive character of the service.
- *Land use planning* is predominantly a local task, even though several countries use guiding land use plans prepared at the inter-municipal or regional levels. National and regional governments both focus primarily on strategic planning and the provision of policy guidelines. Most countries do not prepare land use plans for their entire territory but are more likely to focus on land use plans for areas of particular importance (OECD, 2017^[38]).

Table 3.8. Shared responsibilities across levels of government in federal and unitary countries

Proportion of decisions where more than one government level is involved (%)

	Education	Long-term care	Transport services	Social housing	Healthcare
Austria					13
Australia					78
Argentina					100
Russian Federation	34	38	44	26	
South Africa	2	34	74	61	
Belgium	59	42	16	23	39
Germany		35	82	45	20
Italy	11	58	44	59	29
Canada	11	23	92	73	13
Switzerland	28	21	54	48	65
Spain	21	68	76	93	19

Brazil	69	68	62	80	
Mexico	83	78	76	33	77
Average across federal countries	35	46	62	54	45
Chile	10	25	28	35	2
New Zealand	0	12	5	56	36
Luxembourg	6	38	13	28	32
Denmark	23	11	33	25	67
Latvia	19	36	42	15	16
Netherlands	0	60	45	40	26
Norway	37	35	37	31	26
Finland	31	31	42	22	44
South Korea	67	14	48	73	
Indonesia	67	67	31	60	
Poland	43	44	61	48	41
Estonia	38	58	51	78	20
Average across unitary countries	30	36	36	43	28

Note: The above calculations account for any “not applicable” or unanswered responses for each country.

Source: OECD (forthcoming^[12]), *The Spending Power of Subnational Governments across Five Policy Sectors*, OECD Publishing, Paris.

Decentralisation implies a renewed role for central governments

The impact of decentralisation on the central government is often underestimated. Decentralisation represents substantial challenges for central governments as it requires profound changes of organisation, practices, culture and skills within the central government itself (Devas and Delay, 2006^[39]).

Not only do decentralisation reforms affect central governments in the capital, but they also affect central government representation at the territorial level as well.

Failing to take the full measure of this may be detrimental to reform success, slowing down or modifying the reform process (OECD, 2017^[11]). The fiercest opponent to decentralisation efforts is often the central government itself, as decentralisation may be perceived as a threat (Box 3.5).

Decentralisation reforms imply a more strategic role for national governments, which focus on putting in place the strategies, framework conditions and regulations, incentives – rather than in the implementation of policies. It involves a shift from a direct role in service delivery to one of enabling, advising and assisting, ensuring consistency, facilitating the work of local governments and sometimes helping share good practices across local governments. This requires building new capacity at the central government level, able to cope with these new functions, which cover a large area of sectors.

Box 3.5. Resistance from central government to decentralisation reforms

Resistance to decentralisation reform is often strong from central government itself, even if it is the main promoter of the reform and in charge of its design and implementation. Departments in charge of leading decentralisation processes may be unsuccessful at persuading other departments or ministers to relinquish powers.

There are different reasons for this. First, national government tends to have limited trust in subnational government competency and accountability for failure (Gash, Randall and Sims, 2014^[40]). Second, decentralisation may represent a loss in terms of public employees and control on public affairs. Third, decentralisation requires profound changes in organisation, practices, culture and skills within the central government itself.

Decentralisation implies a reduction in central government employees. It may also directly affect civil servant jobs, particularly if they are transferred to subnational governments, which could involve a less advantageous shift in status, wages, pensions and other benefits. In Ukraine for example, it is expected that the decentralisation reform will reduce the number of central government civil servants by about 30% as numerous functions will be transferred to subnational levels (OECD, 2018^[41]). In Chile, the creation of self-governing regions, with the democratic and direct election of regional governors will also have a strong impact on the regional representation offices of national ministries (SEREMI) and central government regional agencies (OECD, 2017^[21]).

In France, this issue has only recently been addressed. Decentralisation initiatives have not been accompanied by a reform of central government structure, especially at the local level. This situation has generated duplications in responsibilities, services and staff between the central and deconcentrated, subnational units (OECD, 2017^[11]).

Sources: Gash, T., J. Randall and S. Sims (2014^[40]), *Achieving Political Decentralisation: Lessons from 30 years of Attempting to Devolve Political Power in the UK*, Institute for Government; OECD (2018^[41]), *Maintaining the Momentum of Decentralisation in Ukraine*, <https://doi.org/10.1787/9789264301436-en>; OECD (2017), *Making Decentralisation Work in Chile: Towards Stronger Municipalities*, <https://doi.org/10.1787/9789264279049-en>; OECD (2017), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, <https://doi.org/10.1787/9789264272866-en>.

National/federal governments play a crucial role in ensuring that decentralisation does not widen disparities in terms of access and quality to the public services provided by subnational governments in their new functions. There is a risk exists of significant heterogeneity in financial and human capacities given differences in local capacities and performance among subnational governments. In a context of reinforced decentralisation, central governments must address this challenge with appropriate instruments aimed at monitoring, diagnosing and improving the performance of local services. This could include such instruments as management and certification models based on minimum quality standards and performance indicators for basic local services. In Chile, for example, a key factor in the reform of the municipal management system is setting minimum standards for municipal services (*Servicios Municipales Garantizados*, SEMUG) to reduce horizontal disparities among municipalities. Initially, the SEMUG is composed of seven municipal services called “the first generation of guaranteed minimum services”. These services represent a high impact on the community, or high costs or income for the municipality. The minimum standards encompassed a basic level of quantity and quality for a common set of services to be guaranteed by all Chilean

municipalities, and accessible to all citizens regardless of where in the country they choose to live. The 7 selected services include 22 standards and 47 indicators (OECD, 2017^[21]). In Norway, the KOSTRA performance measurement system electronically publishes result within a month of receipt from the municipalities, in this way supporting municipal public service provision and capacity. Some other OECD countries such as Italy, the Netherlands and the United States have gone beyond the definition of minimum standards by developing service charters to promote the continuous improvement of public services and to make clear commitments to the quality standards that citizens can expect.

Another challenge for the central government is linked to human resources management, to make sure that decentralisation does not generate a two-speed civil service. In Chile, for example, although municipal governments now have the same public sector employment arrangements as the central government, they do not have the same employment conditions. Consequently, municipal capacity remains weak as attracting and retaining a highly-skilled workforce is challenging. Low salaries, limited career opportunities and politics are just some of the factors that hinder the attractiveness of municipal public administrations as employers, and thus represent a challenge for the success of decentralisation (OECD, 2017^[21]). Decentralisation should involve a convergence of civil service status, salaries and advantages at central and subnational levels. Disparities between the central government and subnational sector may be significant. Central governments have a crucial regulatory and co-ordination role to play in ensuring that subnational governments have the necessary autonomy and flexibility in this area. This can include the ability: to define the general framework for public employment (i.e. the legal, financial and social conditions of the employees, procedures of recruitment, staff categories and salary scales, retirement conditions, ethics rules, workforce planning, performance systems, etc.); to develop training and learning programmes to bridge capacity gaps; to favour staff mobility across levels of government, etc.

Box 3.6. OECD country experience in central-local co-ordination for pay-setting at the subnational government level

The OECD has identified several reasons why a national government may seek to influence or control remuneration and other employment conditions for staff in subnational administrations. Differences in employment conditions might: i) hamper mobility across public administrations and government levels; ii) as a means to limit or cap the growth of public expenditure; or iii) in order to ensure coherence in public employment conditions. Countries are using a number of instruments to oversee municipal payrolls while at the same time granting subnational governments flexibility to set their own wages.

- In Spain, the law that regulates the civil service also regulates the structure of the pay system for civil servants at the national and subnational levels. The annual remuneration increase is contained in the general state budget. Contracted employees are employed under normal labour market conditions.
- In France, each local government can determine remuneration and other employment conditions for its employees, but their actions are regulated by law and by the fairly complex regulations for the French corps (or career) system.

- Subnational governments in Denmark set their own wages. However, the State Employers Authority maintains an informal, ongoing dialogue with municipal and regional associations that function as central employers for the subnational administration. The State Employers Authority is also represented on the municipal and regional Boards of Wages and Tariffs that function as employer representatives in negotiations with the unions in these sectors and has veto power on the regional board.

Sources: OECD (2008_[42]), *Challenges of Human Resource Management for Multi-level Government*; OECD (2017_[21]), *Making Decentralisation Work in Chile: Towards Stronger Municipalities*, <https://doi.org/10.1787/9789264279049-en>.

The central government also needs to renew its supervisory and monitoring role vis-à-vis subnational governments, especially in legal and fiscal matters. Control should be based on *posteriori* rather than *a priori* control. As far as budget and financial supervision and control are concerned, *a posteriori* controls are essential in a context of increased fiscal decentralisation and greater autonomy. The central government also has a role to play in accordance with the principle of local autonomy. Financial audits are necessary to assess the quality of financial reporting and the reliability and accuracy of financial information and management provided by subnational governments. But with respect to external audits, state financial supervision and the control system over subnational governments should be adapted to the new decentralisation context, for example in liaison with an external and independent audit institution. In several OECD countries, the supreme audit institution can audit both state and local government budgets on the expenditure and revenue side. This is the case in France (*Cour des Comptes*), Germany, Italy (*Corte dei Conti*), Poland (NIK) and Portugal, for example. Some national supreme audit chambers have a network of regional chambers as well (e.g. the *Chambres régionales des comptes* in France) (OECD, 2018_[41]; 2017_[21]).

Box 3.7. Central government's evolving role in the context of decentralisation

France has started to take into account this need through the 2010 reform of the state (REATE) which aimed at streamlining the territorial administration and at improving the old and complex relationships between deconcentration and decentralisation. In 2015, the French regional reform was also an opportunity to think about the modernisation of the functioning of government services at the regional level and to redefine their role and missions (Charter for Deconcentration). More recently, a new impulse has been given in this direction by the new French government, based on the recommendations of the “Public Action Committee 2022” (CAP 22), concerned with the need to draw all the consequences of decentralisation, eliminate the duplication of competencies between the central and subnational governments, and rethink the role and the areas and methods of intervention of the state at regional and local levels.

Finally, the role of national governments to establish adequate co-ordination mechanisms – ones that support aligning objectives and policies across and among levels of government is fundamental in this changing context. The same is true for their ability to

design instruments for effective intergovernmental relations, co-operation and dialogue, as these can also build trust in a reform process (Box 3.8).

This is particularly important for regional development policies. Responsibilities for regional development are now more fragmented among national, regional and local actors, which have various resources, agendas, and legal or political standing. In this context, the role of the central government is increasingly important for providing an overarching framework and guidelines for regional development policies. It also needs overseeing co-ordination mechanisms within which regional policy can be formulated and implemented.

Ensuring that objectives and priorities are aligned, particularly in areas that support regional development but where responsibilities and/or interests overlap (e.g. economic development, transport, health and education) requires vertical co-ordination mechanisms that foster a partnership-based relationship among levels of government.

Some OECD countries have addressed these concerns early on in their decentralisation processes, improving governance structures between levels of government as well as across sectors (see Chapter 5). In Denmark, the Regional Growth Forum integrates local, regional, national and EU development activities within a single, programme-based policy structure. Sweden's Regional Growth Policy aims to improve local and regional competitiveness across all regions through regional programmes and enhanced regional and sectoral co-ordination (OECD, 2010^[43]).

Box 3.8. The renewed role of the central government for managing regional development policies

The following central government roles have emerged under the new paradigm of regional development policies:

- Facilitate consensus-building and coherence between regions and sectors including defining objectives, time frames and spatial horizons.
- Gather and analyse appropriate data and information and co-ordinate discussions and databases concerning needs and opportunities: facilitating dialogue among policymakers.
- Develop legal, fiscal and administrative frameworks: frameworks or “grand rules” which manage the complexity, plurality and tangled hierarchy characteristic of most modes of co-ordination.
- Serve as a “court of appeal” for disputes among sectors and regions: including taking political responsibility for the final decision, especially in the event of a governance failure.
- Seek to re-balance power differentials among sectors, regions and levels of governments: for the proper functioning of the overall governance system, the national government can and should help weaker entities establish capacity building strategies (including training provided by the central government).
- Evaluate and monitor policy results: closing information gaps and improving the quality of decision-making by actors at all levels of government.

Source: OECD (2010^[43]), *Regional Development Policies in OECD Countries*, <https://doi.org/10.1787/9789264087255-en>.

Ensuring balanced development in all parts of the national territory

In decentralised settings, national governments have a key role in ensuring a balanced development in all parts of the national territory and in minimising the potential risk of increased disparities (see Chapter 4). This can be achieved through active regional development policies at the national level and well-designed equalisation policies, which promote development efforts of subnational governments. Fiscal equalisation aims to correct imbalances between subnational governments, thus fostering equity between territories, be they regions or localities.

Fiscal disparities can be one of two kinds: differences in revenue-raising capacity and differences in public service expenditure needs. In the first category, unequal tax-raising capacities come from differences in per capita GDP across jurisdictions. In the second, they are related to specific geographical factors (mountains, islands, isolated or low-density areas, etc.) or special groups such as children, the elderly, the disabled, etc. that explain a higher cost per service unit, raising the overall cost of public services.

Equalisation mechanisms are widely used in OECD federal and unitary countries, either through vertical transfers (from the central/federal government to subnational governments that are financially weak) or through horizontal transfers (from the wealthiest subnational governments to the poorest), or both (see Chapter 5). Equalisation schemes also aim to develop national standards to ensure equal access to local services and a minimum level of quality in the provision of local public services.

Most OECD countries apply various equalisation arrangements, combining horizontal and vertical equalisation with tax revenue and cost equalisation. Vertical equalisation tends to prevail, though both systems have their advantages and disadvantages (OECD, 2013^[44]). Tax revenue equalisation and cost equalisation systems are roughly the same size, although tax revenue disparities are between four and six times larger than cost disparities (Kim and Lotz, 2008^[45]). One of the main difficulties in establishing an equalisation system is the way tax-raising capacity and/or the cost of services is measured (see Chapter 5).

- In Germany, the principle of uniformity of living conditions for Germans throughout the Federation and equalisation is enshrined in the constitution. In Switzerland, the equalisation system was established in 1958 by the Federal Law on Financial Equalisation and thoroughly reformed in 2008.
- In Australia, fiscal equalisation is not mentioned in the constitution but the objective of equalisation is strong. The country aims to ensure that all states have the same fiscal capacity per capita to provide the same services and infrastructure to all residents.
- In Italy, the horizontal equalisation mechanism between the regions created in 2001 was reformed in the framework of Law 42/2009, strengthening vertical equalisation through a state-run fund. It aims to ensure the coverage of essential public services (e.g. health, education and social assistance) in regions with low tax revenues.
- In Sweden, the vertical and horizontal equalisation system is based on five allocations, including income equalisation and cost equalisation. The system is regularly reviewed with an eye on assessing any counterproductive and dissuasive effects the equalisation system may have and correcting any drift, in one direction or the other.

In most instances, the effect of equalisation on the reduction of fiscal disparities between subnational governments is substantial across the OECD (Box 3.9). However, equalisation is frequently the subject of technical and political debate, and is often contested for its complexity, lack of transparency and its potentially negative incentive effects on tax base development and spending levels (OECD, 2013^[44]; 2018^[46]).

Box 3.9. Equalisation in the OECD countries: Some key facts

For a set of 15 OECD countries, equalisation amounts to around 2.3% of GDP, 4.8% of total government expenditure and around half of all intergovernmental grant fiscal equalisation transfers, confirming that there is ample room for improving equalisation.

Across OECD countries, equalisation has a strong redistributive effect: on average, fiscal equalisation diminishes disparities in revenue-raising capacity – as measured by the Gini coefficient or variation coefficient – by almost two-thirds, from 29% to 10%. In some countries – such as Australia, Germany and Sweden – revenue-raising disparities are virtually eliminated. After equalisation, fiscal disparities are clearly narrower than economic disparities, as measured by regional GDP. In other words, the ability to provide public services is more evenly distributed than economic output.

Source: OECD (2013^[44]), *Fiscal Federalism 2014: Making Decentralisation Work*, <http://dx.doi.org/10.1787/9789264204577-en>.

Notes

¹ An important exception is combined authorities in the United Kingdom. A reform in 2016 made it possible to establish direct elections for a mayor and combined authorities with directly elected mayors can increase business rates by two pence in the pound. This reform went into effect in six combined authorities when their mayors were elected on 4 May 2017. This falls outside the scope of the RAI update for 2010-16.

² For the 48 countries in the RAI dataset for the full 60 years, regional authority increased from an average of 8.1 to 12.6.

³ See Table 3.1 for notes regarding Cyprus.

⁴ This designation is without prejudice to positions on status, and is in line with United Nations Security Council Resolution 1244/99 and the Advisory Opinion of the International Court of Justice on Kosovo's declaration of independence.

⁵ In particular, there is a recent trend in OECD countries such as Denmark, Germany and Norway to recentralise healthcare provision. This option was also discussed in Sweden. The proposal was that healthcare might be reorganised, with primary care entrusted to municipalities and specialised care brought closer to research facilities. This would mean the recentralisation of specialised healthcare. However, Swedish regional reform is not moving in that direction, although some options have been discussed.

⁶ While Quebec does have substantial authorities over immigrant selection, the final decision to issue a visa remains a federal matter. Also, the Quebec government does not have authorities over Citizenship or Residency – these are both federal jurisdictions.

⁷ The division of asymmetric arrangements (with legal basis) into ones that are based on constitutional status and others that are based on ordinary law is of course a simplified description of reality. In many cases, such as Spain for example, the regions may have special status both by constitution and ordinary law.

⁸ The region of Friuli-Venezia Giulia has had a special status since 1963.

⁹ Source: <http://www.italianinsider.it/?q=node/6454> (accessed on 16 May 2018).

¹⁰ Finnish Ministry of Health and Social Affairs Internet pages: http://alueuudistus.fi/en/artikkeli/-asset_publisher/10616/sote-ja-maakuntaudistus-voimaan-1-1-2020-maakuntavaalit-lokakuussa-2018?p_p_auth=opMDJ79x (accessed in February 2018).

¹¹ In fact, the tradition of experimenting using the “free municipality” initiatives had already begun in several Nordic countries in the 1980s. The first free municipality trials were implemented in Sweden in 1984, Denmark in 1985, Norway in 1987 and Finland in 1989 (Swedish Government, 1991). In Norway, there has been a law for continuous experimenting since 1993. The law allows voluntary experimenting in municipalities, counties and central government.

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Chapter 4. Decentralisation: Its benefits and challenges

Decentralisation is often subject to heated debate. The proponents of decentralisation tend to emphasize the pros and the critics often highlight the cons. Fortunately, after several decades of practical policy implementation, a considerable amount of information has accumulated on the effects of decentralisation. This chapter discusses the benefits and challenges of decentralisation using the best available information on research results and practical policies pursued in various OECD countries. After brief introduction, the chapter begins by describing the benefits and opportunities and then continues to examine the risks and challenges of decentralisation. Both sides of decentralisation are discussed from economic, administrative and political aspects. In the end of the chapter, a conclusion and a short summary table of the main effects are presented.

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

As highlighted in Chapters 1 and 2, the trend in decentralisation continues worldwide (Hooghe et al., 2016^[1]). Moreover, practices in various countries show that the implementation of decentralisation has evolved as new challenges have emerged. Some examples of this are the urbanisation and regionalisation trends. Also, the economic crisis that began in 2008 and the austerity and consolidation measures that followed have affected fiscal decentralisation in many significant ways. This chapter provides a brief discussion of the benefits and challenges of decentralisation, as well as the results of recent empirical research on the topic.

Practical experiences of decentralisation reforms in various countries have accumulated over several decades, with researchers and practitioners debating their effects. One major aspect of this discussion has been the effect of decentralisation on economic growth and well-being. While country statistics do not enable strictly causal conclusions, in recent years it has been found that subnational fiscal power can be positively associated with economic activity (Blöchliger, 2013^[2]). Although correlation does not mean causality, it is interesting to note that especially measures such as gross domestic product (GDP), public investments made in physical and human capital, and education outcomes show a positive correlation with decentralisation. Revenue decentralisation appears to be more strongly associated with income gains than spending decentralisation (Blöchliger, 2013^[2]). In addition, examples and research results from several countries show that decentralisation can be conducive to public sector efficiency, democratisation and political stability (Faguet, 2014^[3]; Ivanyna and Shah, 2014^[4]). These effects, however, depend largely on the way decentralisation is designed and implemented. It should be emphasised that decentralisation reform is always ultimately a political choice. Such reforms should always be implemented as part of a larger political reform process, making sure that the judiciary, civil service and regulatory frameworks are capable of dealing with any associated change.

There is an extensive economic theory and empirical research on multilevel governance. The so-called “first generation” economic literature of fiscal federalism, developed in the 1950s and 1960s, emphasised the benefits of decentralisation. The optimistic view of decentralisation was based on the theoretical assumption of the benevolence of public decision-making, or perhaps more realistically, the positive outcomes resulting from electoral pressures in a democratic government system (Ahmad and Brosio, 2006^[5]; Oates, 2005^[6]). Many decentralisation reforms implemented during the 1970s, 1980s and 1990s were founded on the early fiscal federalism principles. Another important motivation for decentralisation was the desire to advance democratisation processes. The “second generation” fiscal federalism literature, which began to emerge in the late 1990s, mostly relaxes the assumptions of previous research. A more critical and nuanced view of decentralisation is now offered by public choice and political economy research, for instance by allowing for self-interested motives of public decision-making (Weingast, 2014^[7]; Lockwood, 2002^[8]). The second-generation literature argues that the first generation literature must be complemented by political economy aspects to give a rigorous account of the preference-matching and accountability benefits of decentralisation (Oates, 2008^[9]). Another important strand of second-generation fiscal federalism literature has been motivated by the fiscal crises caused by intergovernmental fiscal behaviour in some Latin American and European countries. This line of research emphasises the dangers of impartial or unbalanced decentralisation reforms and discusses conditions under which decentralised countries could ensure fiscal discipline (Rodden, Eskeland and Litvack, 2003^[10]). Moreover, the research focusing on regional development has studied the links between decentralisation and regional development and

effects on regional disparities (Ezcurra and Rodríguez-Pose, 2013^[11]; Tselios et al., 2012^[12]).

Many countries claim that they are decentralised but the reality may be very different. Different measures of decentralisation can lead to very different conclusions regarding degrees of decentralisation (Hatfield, 2015^[13]). The way decentralisation is designed and implemented has a major impact on its outcomes. For example, many researchers stress that implementing “partial decentralisation” may lead to unexpected effects and loss of potential benefits. A typical example of partial decentralisation is a policy where spending tasks are widely delegated to subnational governments, but where subnational own-revenues remain highly limited. It should also be noted that spending or revenue decentralisation alone cannot secure or guarantee all the benefits associated with decentralisation. At the same time, adequate capacity of subnational governments, accountability of local public decision-making and good overall governance are required to support positive outcomes of fiscal decentralisation (OECD, 2013^[14]; 2017^[15]; Allain-Dupré, 2018^[16]; Kim and Dougherty, 2018^[17]).

The benefits and challenges of decentralisation can be direct or indirect. Direct effects include changes in service levels, plus the quality and efficiency of public services. Indirect effects of decentralisation, such as effects on economic growth or societal stability, result from direct outcomes of decentralisation, such as better education or higher participation in political decision-making. Since the indirect effects of decentralisation are affected by a variety of factors, the role of decentralisation is, of course, harder to separate from other trends and policies.

Opportunities and benefits

There are various economic, political and other reasons behind the upsurge of decentralisation reforms, and the reasons vary considerably across countries (see Chapter 2). For instance, in some countries, decentralisation can be seen as a counter-reaction to previous strong centralisation and even autocratic trends (Hooghe et al., 2016^[11]). In these countries, decentralisation has been a way to ensure that democratisation will not be reversed. In other countries, decentralisation has been a method to reform the public sector, for example in order to improve the efficiency of public services, thereby curbing the growth of government spending. As for other motives, decentralisation is often thought to deliver positive effects, such as more accountable and transparent public governance, lower corruption, higher political participation and policy innovation. These benefits are discussed below.

Economic benefits

Decentralisation may facilitate tailoring services to local needs

Perhaps the most important direct benefit of decentralisation is the allocative efficiency resulting from local public service provision. Subnational governments often hold valuable information on local demands and conditions, which enables them to tailor public service provision to meet residents’ needs. Decentralised choice, therefore, gives an opportunity to increase economic welfare by adapting public service provision to the heterogeneous preferences of smaller population groups (Wallis and Oates, 1988^[18]). It would be costly for the central government to obtain such information and therefore the central level is often likely to provide a uniform level of public output in all jurisdictions. In the case of heterogeneous preferences and local public goods, subnational governments

clearly outperform central government in allocating public sector resources (Oates, 2005^[6]).

It is important to note that the highest allocative advance from subnational service provision is usually obtained in the case of “local public services”, which consist of public tasks that have a spatially limited area of benefits.¹ Ideally, the benefit areas should match with administrative boundaries of local jurisdictions. Public services with major externalities or services with important economies of scale are less suitable for local provision, although in these cases allocative benefits may also be obtained. In the case of redistributive services, such as education or healthcare, the co-ordination responsibility is usually maintained with a higher level of government (Box 4.1).

Box 4.1. Assigning allocation, redistribution and stabilisation tasks: Fiscal federalism principles

The traditional fiscal federalism literature divides public tasks into three branches: allocation, redistribution and stabilisation functions (Musgrave and Musgrave, 1980^[19]). According to this categorisation the allocation function – i.e. public services provision – can be the responsibility of both the central and subnational levels of government. In allocation, the central level of responsibility is best applied when the services have no specific local interest. Subnational responsibility is justified when the benefits of the goods or services are spatially limited. Moreover, according to the “Decentralisation Theorem” (Oates, 1972^[20]), the subnational level is the most suitable level to provide the services and goods, unless the central government has a clear advantage in provision. This could, for example, be where there are considerable economies of scale in the provision.

According to the Musgravean distinction, redistribution and stabilisation functions are mostly central government responsibilities. In particular, the central government is considered best suited to deal with monetary or fiscal policy (Musgrave and Musgrave, 1980^[19]). It is also widely accepted that the redistribution function should be mostly central level responsibility: the central government is more capable of carrying out income redistribution from the wealthy to the poor and in establishing minimum standards of public services across regions (King, 1984^[21]).

“Pure local goods”, such as local infrastructure (street lights, local roads), sewage, land use planning or basic education, are usually considered best suited for subnational government provision. It is nevertheless quite common that subnational governments are also involved in the provision of services with redistributive features, at least in some way. In some countries, such as the Nordic countries, even health, education and welfare services have been delegated from the centre to subnational governments. In the case of a decentralised redistribution, the central government usually retains responsibility for co-ordination and ensuring equity of citizens in different parts of the country. This can be achieved for example by using transfers from central to subnational governments, or with normative regulation (minimum standards), or both.

Sources: Broadway, R. and J. Tremblay (2012^[22]), “Reassessment of the Tiebout model”, <http://dx.doi.org/10.1016/j.ipubeco.2011.01.002>; Musgrave, R. and P. Musgrave (1980^[19]), *Public Finance in Theory and Practice*, McGraw Hill Kogahusha; Tiebout, C. (1956^[23]), *A Pure Theory of Local Expenditures*, <http://www.jstor.org/stable/1826343> Accessed:28/07/200805:58; Oates, W. (1972^[20]), *Fiscal Federalism*, Harcourt Brace Jovanovich, New York; King, D. (1984^[21]), *Fiscal Tiers: The Economics of Multi-level Government*, Allen and Unwin; Allain-Dupré, D. (2018^[16]), *Assigning Responsibilities across Levels of Government: Trends, Challenges and Guiding Principles for Policy-makers*, OECD, Paris.

Decentralisation may improve the efficiency of public service delivery

Compared with centralisation, decentralisation contributes to better accountability because it alters the incentives of the authorities who serve local populations. In a decentralised model, the elected local authorities are accountable to residents who finance and consume the services. In a centralised public service provision system, the administrators are not accountable to local residents but instead, they report to their superiors in the central government. Decentralisation reverses the accountability chain from a “top-down” to a “bottom-up” relationship and therefore affects the motives of all stakeholders.

Decentralisation allows for many types of political and fiscal competition, which can be efficiency enhancing. From a political perspective, decentralisation increases the number of political arenas and therefore lowers the entry cost for new political candidates. These enlarged political fora give citizen-voters more choice in elections. As a result, voters are better able to express their preferences on service delivery and to inform politicians about problems at the local level.

While local and national elections provide the main channels for citizens to influence policies and express their “voice”, it is important to make sure that there are also other forms of citizen participation (Inman and Rubinfeld, 1997^[24]). Such alternative ways include participation in surveys, town meetings, local referenda and direct involvement in service delivery (Azfar et al., 1999^[25]).

Increased participation and engagement can contribute to local ownership of public policy programmes. In addition, higher overall citizen participation can lead to tighter political competition not only at the local level but also in national elections. Increased political competition can lead to better overall policies and more efficient implementation of government programmes.

Decentralisation may enhance competition not only within local jurisdictions but also between jurisdictions. The underlying mechanism is the “exit” (or threat of exit) of taxpayers from their current jurisdictions. The more the subnational governments rely on revenues based on mobile resources, the more likely there is to be competition between jurisdictions. This is reflected in the traditional “voting with the feet” model of decentralised government (Tiebout, 1956^[23]). Although in reality, the mobility of households and companies is far from perfect, the threat of losing taxpayers creates additional pressure for elected local authorities to ensure that the services match the local demands with a competitive tax burden (Oates, 2005^[6]). Such competition is usually assumed to result in a better match between service provision and local preferences, generating a more efficient allocation of resources (Box 4.2).

“Yardstick competition” is a form of competition that does not involve mobility. It occurs when voters can compare the taxes and service quality in their own jurisdiction with those in neighbouring jurisdictions. If voters observe that the service-tax mix is better in the neighbouring jurisdictions (or other similar communities), they punish the elected representatives in their community by voting against them in the next local elections. Yardstick competition can be efficiency improving if voters can truly identify and re-elect politicians whose “type” is “good” rather than those whose type is “bad” (Ahmad and Brosio, 2006^[5]). Openly available information on outcomes can foster such benchmarking (Weingast, 2014^[7]; Faguet, 2014^[3]).

These basic accountability mechanisms work best if local residents have a strong incentive to evaluate the efficiency of their local administration. Such motivation depends

primarily on the financing system of locally provided public services and on information available on the service outcomes. If local residents finance a considerable share of local services by paying local taxes, they will have a strong incentive to monitor their local administration.

Box 4.2. Tiebout model and mobility

Charles Tiebout's famous 1956 paper, *A Pure Theory of Local Expenditures* is one of the earliest contributions to the modern theory of fiscal federalism and decentralisation. The model was not intended as a complete theoretical description of decentralised government. Instead, the purpose was to demonstrate a mechanism by which voters' preferences for public services could be revealed by "exit" rather than "voice". Nevertheless, the concept of "voting with one's feet" of his model has been later used widely as a theoretical assumption when modelling decentralisation.

In Tiebout's model, the perfect mobility of households will lead to an optimal allocation of households among local communities. Musgrave and Musgrave described the Tieboutian competing communities as follows: "Those who like sports will want to reside with others who are willing to contribute to playgrounds. Those who like music will join the others who will participate in building a concert hall, and so forth. Each community will do its own thing, and everybody will be happy".

The assumptions behind Tiebout's model are strict. In addition to the perfect mobility of households, the assumptions of the model include local public goods, endogenous number of communities and benefit taxation. The model has only one level of government and there is no transfer system.

Since the times of Tiebout's paper, fiscal federalism theory has been further developed, and many of the strict assumptions made by Tiebout have been relaxed. As Broadway and Tremblay note, fiscal federalism is really about outcomes in a world with more than one level of autonomous government. In reality, the mobility of households is far from perfect, which weakens the effect of competition between communities. The tasks provided by subnational governments may vary less than assumed by Tiebout, because state, regional and municipal levels of governments often provide services that have been delegated from the central level.

Oates argues that the gains from fiscal decentralisation do not depend on the mobility of households. Potential welfare gains from decentralisation would exist even without mobility due to a subnational government's ability to tailor services to local demands and circumstances. Mobility, if it happens, would, however, strengthen the benefits expected from decentralisation.

Sources: Tiebout, C. (1956^[23]), *A Pure Theory of Local Expenditures*, <http://www.jstor.org/http://www.jstor.org/stable/1826343>; Broadway, R. and J. Tremblay (2012^[22]), "Reassessment of the Tiebout model", <http://dx.doi.org/10.1016/j.jpubeco.2011.01.002>; Musgrave, R. and P. Musgrave (1980^[19]), *Public Finance in Theory and Practice*, McGraw Hill Kogahusha; Oates, W. (2008^[19]), "On the evolution of fiscal federalism: Theory and institutions", *National Tax Journal*, Vol. 61/2.

Decentralisation may enhance economic growth

Several theoretical and empirical studies have been carried out to test the link between growth and decentralisation. Theoretical research on this topic can be grouped roughly

into three aspects: increased competition, better preference matching and enhanced accountability (Hatfield, 2015_[13]). While the results of theoretical work are somewhat mixed, the general conclusion is that decentralisation can be conducive to growth when it is properly designed and implemented (OECD, 2016_[26]), and especially if competition between jurisdictions is allowed to work in a way that promotes efficiency, accountability and preference matching at the subnational level.

There is extensive empirical research on the effects of decentralisation on growth (Hatfield, 2015_[13]). The largest group of empirical work consists of studies that use cross-country data to regress a measure of economic growth on measures of decentralisation, such as local revenue share or local expenditure share. For instance, recent studies analysing data from OECD countries find that subnational fiscal power is positively associated with economic activity (Blöchliger, 2013_[2]; OECD, 2016_[26]). According to the study, the positive impulse seems to stem both from productivity and human capital improvements. Decentralisation can, for instance, improve the efficiency and productivity of the public sector, which in turn may contribute to higher productivity in the private sector. Decentralisation could also result in more educational investment and enhanced human capital, both of which are important factors behind economic growth (Blöchliger, Égert and Fredriksen, 2013_[27]).

Investment in physical and human capital as a share of general government spending is significantly higher in more decentralised countries. It has been estimated that on average, a 10 percentage point increase in decentralisation is associated with 3% to 4% higher share of investment in total government spending (Blöchliger, Égert and Fredriksen, 2013_[27]). The relationship is stronger for investment in human than physical capital and stronger for revenue than for spending decentralisation.

Recent research results suggest that revenue decentralisation, in particular, is related to growth (Blöchliger, 2013_[2]; OECD, 2016_[26]). The link with spending decentralisation and economic growth seems to be less clear, however. This empirical finding may reflect that “true” fiscal autonomy is better captured by the subnational revenue share (instead of the spending share), as a large part of subnational spending may be mandated or regulated by central government (Blöchliger, 2013_[2]).

The second group of studies focuses on how variation in the local share of government revenues and expenditures across provinces or states affects outcomes within a single country. The third group of empirical research examines the effect of inter-jurisdictional competition by using the number of jurisdictions within a geographic unit as a measure of competition. The results of the second and third groups of empirical research are mixed. Moreover, because of the endogenous relationship between growth and decentralisation, it is not possible to draw causal conclusions. That said, one general result of the empirical studies seems to rise above others: it is important that a certain level of taxes be levied at the local level for fiscal decentralisation to contribute to economic growth (Weingast, 2014_[7]; Hatfield, 2015_[13]; Ivanya and Shah, 2014_[4]; Blöchliger, 2013_[2]). While a general rule for the optimal degree of tax autonomy is obviously difficult to define, it is usually argued that local authorities should rely on their own revenues for financing their services at the margin. Such a principle would help ensure that decisions to expand public programmes are made keeping in mind the additional costs (Oates, 2008_[9]).

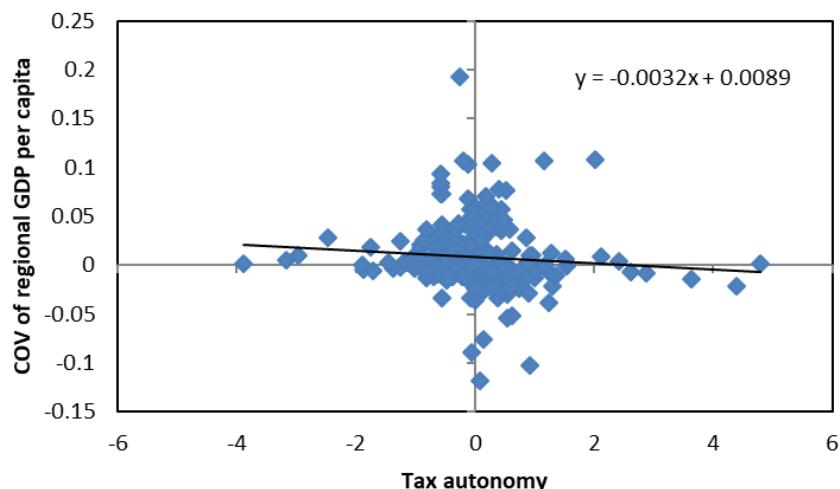
Decentralisation may contribute to lower regional disparities

Recent empirical evidence indicates that revenue decentralisation could be associated with smaller regional economic disparities (Bartolini, Stossberg and Blöchliger, 2016_[28]).

Although correlation does not imply causality, a possible explanation is that own-source revenue may spur growth especially in poorer regions and enhance the convergence process towards the best performing regions (Blöchliger, Bartolini and Stossberg, 2016_[29]) (Figure 4.1). In some countries such as Mexico, decentralisation is motivated by the fight against poverty and territorial disparities (Faguet, 2014_[3]).

Figure 4.1. Subnational government tax autonomy tends to be associated with lower regional GDP disparities

Coefficient of the variance of GDP per capita (vertical axis) and tax autonomy (horizontal axis)



Note: The sample covers 20 OECD countries (19 for tax autonomy) and the years 1995 to 2011. Each point reflects the coefficient of variation of regional GDP per capita in one country in one year. The lines indicate the results of a bivariate ordinary least squares (OLS) regression. Variables are normalised using the respective country means to net out differences between countries that are persistent over time.

Source: Blöchliger, H., D. Bartolini and S. Stossberg (2016_[29]), *Does Fiscal Decentralisation Foster Regional Convergence?*.

High share in intergovernmental transfers of total subnational government revenues has been found to correlate with disparities in regional GDP per capita. Fiscal autonomy and reliance on own-source revenues, therefore, appear to help the catching-up regions more than those above the national average (Blöchliger, Bartolini and Stossberg, 2016_[29]). This result is supported by a recent study by Tselios et al., who observed that decentralisation is positively associated with smaller interpersonal inequities at the regional level. The relationship seems to weaken as overall income rises (2012_[12]). These results do not necessarily mean that a causal relationship exists between decentralisation and regional disparities (Box 4.3). More research is certainly needed on this topic.

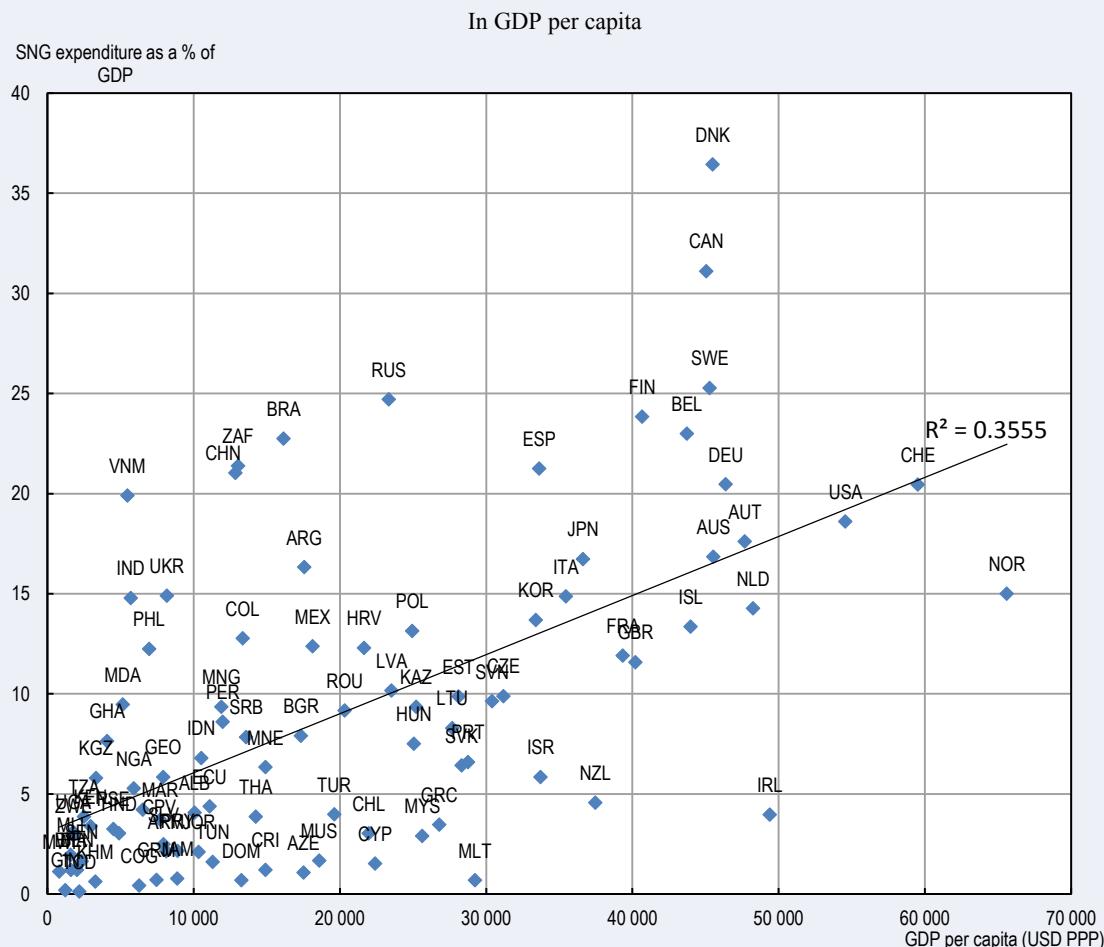
While incentives for developing own source revenues at the subnational government level contribute to regional growth policies, many subnational governments nevertheless need substantial central government financing to provide the services they are assigned (Shah, 2017_[30]). Transfer systems are, therefore, often designed to equalise both cost differences and differences in revenue base. Well-designed equalisation systems can help ensure reasonably comparable levels of public services at comparable burdens of taxation. At best, equalisation can contribute to economic growth by creating a level playing field, which facilitates inter-regional movement of labour and business in response to economic stimuli, but slows down their movements in response to fiscal considerations alone.

Equalisation transfers support national/state objectives in creating a common economic and social union.

Box 4.3. Linking decentralisation and development: Some evidence at world level

At the world level, the 2016 OECD-UCLG study shows that the wealthiest countries tend to be more decentralised. The correlation between the GDP per capita (measured in USD PPP) and the level of spending decentralisation (measured by the share in GDP) is again positive (Figure 4.2).

Figure 4.2. Decentralisation of spending responsibilities is a feature of development at world level, 2014



Note: Luxembourg is not represented on the graph as it is an extreme case due to its high GDP per capita.

Note by Turkey: The information in this document with reference to “Cyprus” relates to the southern part of the Island. There is no single authority representing both Turkish and Greek Cypriot people on the Island. Turkey recognises the Turkish Republic of Northern Cyprus (TRNC). Until a lasting and equitable solution is found within the context of the United Nations, Turkey shall preserve its position concerning the “Cyprus issue”.

Note by all the European Union Member States of the OECD and the European Union: The Republic of Cyprus is recognised by all members of the United Nations with the exception of Turkey. The information in this document relates to the area under the effective control of the Government of the Republic of Cyprus.

Source: OECD-UCLG (2016_[31]), *Subnational Governments Around the World: Structure and Finance*, <http://www.oecd.org/regional/regional-policy/sngs-around-the-world.htm>.

Decentralisation can be a lever for regional development

Another potential benefit of decentralisation is the ability to carry out better regional development policies (Morgan, 2006^[32]). To mobilise the regional productivity catch-up potential as well as to ensure that growth and productivity will be more balanced and inclusive across the territory, an efficient multi-level governance system is therefore required – one that is based on an enhanced role for subnational governments, especially regions, capable of designing and implementing context-sensitive interventions (OECD, 2017^[33]).

The links between decentralisation and regional development may at least partly explain why the regionalisation process was so strong in the Central and East European countries that were planning to join the European Union. Even if the EU did not promote a particular model of decentralised governance, the prospect of entering the EU led several countries to create self-governing regions to access and manage EU funds for regional development.

Regional development was also a strong motivation of the first decentralisation reforms in Japan, in particular, to correct the excessive population concentration in Tokyo. In the creation of new regions, many saw the need to correct interregional disparities, to give regional and local actors the means to implement regional development policies adapted to the new economic realities (functional areas of prefectures were outdated), and to and realise economies of scale in terms of infrastructure facilities and services (OECD, 2016^[34]; 2017^[15]). In Chile, the regionalisation process that created self-governing regions with directly elected governors was linked to the need to correct high regional disparities (OECD, 2017^[33]). In Chile, “hyper-centralisation” has gone hand in hand with a “hyper-concentration” of population, resources and powers in the metropolitan region of Santiago. In Korea, addressing the regional imbalance between Seoul and surrounding regions is also at the core of the decentralisation programme launched in 2017-18 (Annex C).

Political benefits

Decentralisation may strengthen citizen participation in government

Decentralisation has the potential to support and expand citizen participation by bringing government closer to citizens and by making government more accessible. Citizen participation is an essential part of successful decentralisation. High voter turnout in local elections helps to ensure that spending reflects the preferences of residents. Active citizen engagement also supports the accountability of local public decision-making.

Political participation has traditionally been an important justification for decentralisation reform. This was the case in many former communist countries such as Poland (OECD, 2008^[35]; Regulski and Drozda, 2015^[36]), and many developing countries (e.g. Bolivia, Cambodia, Peru and Uganda) (Faguet, 2014^[3]). Recent empirical evidence from both developed and developing countries has shown that there is a positive association with decentralisation and political participation (Stoyan and Niedzwiecki, 2018^[37]; Michelsen, Boenisch and Geys, 2014^[38]). Moreover, an earlier study using data from 80 counties also found a positive relationship between fiscal decentralisation and citizen participation (Huther and Shah, 1998^[39]).

Decentralisation may improve political stability

Decentralisation can be a “glue” that holds countries together (Bird, 2003^[40]). By decentralising powers to regions and subnational governments, the tensions arising due to various cultural, historical or political reasons may be mitigated. This can also happen because decentralisation might be asymmetric, thus making it easier to take into account certain territorial specificities.

Since decentralised governments are well positioned to offer services suited to the local needs and preferences, the destabilising demands promoted by separatist movements may be alleviated. It has also been argued that a decentralised system may promote the rise of types of political leaders who are willing to work co-operatively within the state (Faguet, 2014^[3]).

Since decentralisation generates a larger number of political arenas and government layers (compared with a centralised model), pressure on candidates to win elections at the national level at any cost may be diminished. This can reduce the overall political tensions. In addition, decentralised systems usually result in a higher number of independent actors in government. This can create stability because rules, laws and policies cannot be easily and frequently changed (Faguet, Fox and Pöschl, 2014^[41]).

Administrative benefits

Decentralisation may constrain rent-seeking and corruption

Decentralisation may diminish the opportunities for rent-seeking and corruption in public administration (Boadway and Tremblay, 2012^[22]). There are alternative and complementary explanations for why this might happen. One explanation is simply that in a decentralised setting the scale of government is smaller. This reduces the size of rents available and makes rent-seeking less interesting. An alternative explanation is that the enhanced competition fostered by decentralisation reduces opportunities for rent-seeking and corruption. In other words, decentralisation brings a local aspect to lobbying, and this reduces the “monopoly power” of national level rent-seeking (Bordignon, Colombo and Galmarini, 2008^[42]).

Empirical research provides some support to these theoretical arguments. For instance, a larger subnational share of public expenditures has been found to correlate with lower corruption (De Mello and Barenstein, 2001^[43]). Using cross-country data on governance and fiscal indicators from 78 countries, the study found that in particular, a higher local government share of public revenue² was associated with lower corruption. These results may depend on the decentralisation model that was chosen and on its implementation. For example, very complicated multi-level governance models with several government tiers and unclear assignments of responsibilities have been found to be more prone to corruption (Fan, Lin and Treisman, 2009^[44]). Using data on a survey of business managers conducted in 80 countries³ and data on several fiscal indicators including the number of tiers of government, the study found that in countries with a larger number of government tiers, reported bribery was both more frequent and costlier to firms. According to the study, the degree of a country’s development affects the relationship between governance and corruption. In developed countries, the association was weaker than in developing countries (Fan, Lin and Treisman, 2009^[44]).

Decentralisation enables experimenting and policy innovation

Decentralisation provides a useful platform for experimenting with public policies. At best, such a “learning by doing” process of decentralised policy innovation can result in important information spillovers from good practices. The “information externalities” created by decentralisation can benefit not just subnational governments themselves but also central government.

Subnational innovation activities are best motivated if local jurisdictions are responsible not only for spending but also for raising financing. Innovation activities at the subnational government level can be further enhanced if systematic frameworks are created to support and encourage subnational governments to introduce their own programmes (Oates, 2008^[49]). Yardstick competition between subnational governments can foster the adoption of the most effective methods.

In many countries, central governments have adopted practices that were first implemented in the best performing subnational governments. Oates describes several examples of such cases from the United States (Oates, 2008^[49]). For instance, unemployment insurance, gasoline taxation and environmental regulation were state-level policies before the federal government introduced similar measures or standards for the whole country. There are numerous such examples from all over the world, including Participatory Budgeting which was first implemented in the city of Porto Alegre, Brazil, and is now practised in several countries (Campbell and Fuhr, 2004^[45]). Such “laboratory federalism” may enhance the efficiency and quality of public policy in general.

Some countries have adopted bottom-up models of experimental governance, i.e. state-sponsored experimentalism. For example, governments are increasingly receptive to and supportive of public sector innovation hubs to promote territorial development and public service reform. The UK innovation foundation, NESTA, is one of the most prominent pioneers of public and social labs dedicated to addressing societal challenges through evidence-based local experiments (Morgan, forthcoming^[46]).

Risks and challenges

Despite the numerous potential benefits of decentralisation, there are also potential risks in such reforms that need to be properly addressed. Some of these challenges relate to decentralisation in general but problems may also arise because of partial or unbalanced implementation of decentralisation processes. The question is not whether decentralisation is good or bad in itself – it is rather under which conditions decentralisation can be conducive to regional development and citizen engagement. The outcomes of decentralisation reforms depend extensively on the way decentralisation is conceived and put in place.

Decentralisation presents a challenge for subnational governments because it requires certain economic, political and administrative capacities. Unless the capacity challenge is addressed, there is a risk that decentralisation intensifies differences between jurisdictions in a way that could jeopardise equal access and service quality. Partial decentralisation, such as high subnational government spending responsibilities combined with strong normative regulation and low revenue-raising autonomy, could put at risk the subnational government ability to adjust public-good levels to suit local demands. A high reliance on central government transfers may reduce a subnational government’s incentives for responsible fiscal behaviour. Unbalanced decentralisation, i.e. situations where tasks that are closely linked or complementary are decentralised to varying degrees, can weaken

multi-level governance. These aspects and other challenges of decentralisation are briefly discussed below.

Economic challenges

Lack of resources and underfunded mandates

One of the most frequent challenges is the misalignment between responsibilities allocated to subnational governments and the resources available to them. The most extreme cases, unfunded mandates, where subnational governments have the responsibility to provide services or manage policies but without the requisite resources, are common.

The fiscal dimension is very often the weak, or even missing, link of decentralisation. The transfer of spending responsibilities should normally involve transferring equivalent resources to subnational governments in order to allow them to perform their new tasks correctly. This can be done through central government transfers (general or earmarked), or through the allocation of a share of national taxes such as the personal income task (tax sharing arrangements). It can also be accomplished through the right to levy own-source revenues, such as local taxes and user charges and fees, and to raise revenues from subnational financial and physical assets (e.g. natural resources, dividends from local companies, sales of property assets, etc.). This is the “finance follow functions” principle, also called the “connection” or “matching principle”.

In practice, there are often imbalances between the assignment of spending responsibilities and the assignment of revenues, resulting in unfunded or under-funded mandates.

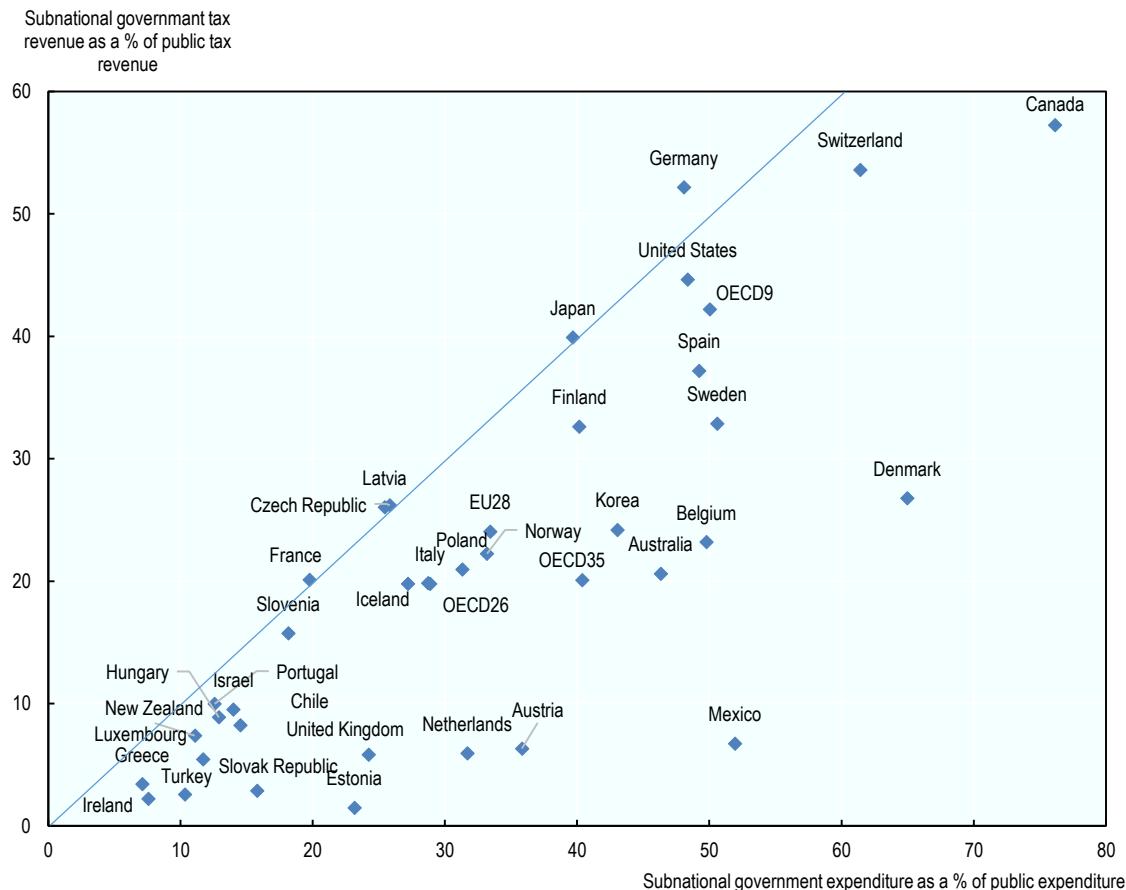
Risks of partial decentralisation: Lack of fiscal autonomy

Lack of fiscal autonomy for subnational governments to exert their responsibilities forms a major challenge to decentralisation. However, a minimum degree of fiscal autonomy is required to allow subnational governments to make better use of public resources, targeted to local needs. Fiscal decentralisation is not only about assigning tasks to subnational governments, but also about granting some autonomy to the subnational government to raise and manage resources.

While in a strict sense decentralisation means devolving true spending and taxing powers from central to subnational governments, in reality, decentralisation is often implemented in a way that satisfies only part of that definition. For instance, seen from the fiscal decentralisation perspective, spending is usually much more decentralised than revenues (OECD, 2018^[47]). This is the case in all OECD countries (Figure 4.3). If subnational governments have little freedom to choose the levels of local public goods, especially when transfers are accompanied by mandates that specify how the money is to be allocated across spending categories, or if service provision is tightly regulated with norms and laws, the decentralisation is only partial (Brueckner, 2009^[48]; Borge, Brueckner and Rattsø, 2014^[49]). This is especially the case in developing countries but it is also the case also in many developed countries. In particular, own revenue-raising capability by subnational governments is often limited, for instance, because central government has reserved the most valuable tax bases for central taxing only. Central governments also commonly regulate subnational government tax bases and tax rates. Furthermore, if subnational service provision is strongly steered by normative regulation,

also the spending autonomy is limited. Implementing such “partial decentralisation” could lead to unwanted effects and loss of potential benefits of decentralisation.

Figure 4.3. Vertical fiscal imbalances in the OECD, 2016



Note: Australia and Chile: estimates from IMF Government Finance Statistics. 2015 data for Mexico, New Zealand and Turkey.

Source: OECD elaboration based on OECD (2018^[47]), *Subnational Governments in OECD Countries: Key Data (brochure and database)*, <http://dx.doi.org/10.1787/region-data-en>.

Partial decentralisation can have a variety of undesirable effects on subnational government incentives and decision-making. The main disadvantage resulting from highly restricted subnational spending and revenue autonomy is the weakened ability of subnational governments to allocate public resources according to local demands and local conditions. According to recent theoretical research, policies that limit subnational government taxing power weaken allocative efficiency (Brueckner, 2009^[48]).⁴ In addition, a carefully implemented empirical study using data from Norway found that dropping central regulations on subnational spending resulted almost immediately in important changes in local service provision. This suggests that there was a clear demand for local discretion (Borge, Brueckner and Rattsø, 2014^[49]).

A high reliance on central transfers can incentivise subnational governments to overspend and to incur debt especially if subnational governments operate under soft budget constraints. Soft budget constraints may develop if subnational governments expect that

central government will bail them out in the case of economic troubles or insolvency (Bordignon, Giglio and Turati, 2015^[50]). The soft budget constraint problem is exacerbated if subnational governments are responsible for services that are of national importance, like healthcare. This is because in these cases central governments may find it politically difficult to commit to a no-bailout policy. In addition, some subnational governments, such as the largest cities, can be too important for the central authorities to allow bankruptcy (the “too big to fail” argument). At worst, subnational government fiscal problems coupled with soft budget constraints can destabilise the entire economy (Rodden, Eskeland and Litvack, 2003^[10]). In this respect, the experience of some Latin American countries (especially Argentina and Brazil) is usually mentioned. In these countries, powerful provincial authorities were able to run major fiscal deficits and accumulate large debts up to a point that led to the bailout of provinces by the central government, and eventually to a national financial crisis (Oates, 2008^[9]).

The importance of grants and shared taxes in subnational funding results in a significant vertical fiscal imbalance, i.e. the difference between subnational governments own revenues (own-source tax, user charges and property income) and spending obligations. To measure vertical fiscal imbalances, a proxy comparing the level of tax revenues and that of spending can be used.

Benefit spillovers and inadequate scale

While the traditional theoretical assumption is that a jurisdiction’s administrative boundaries coincide with the service benefit areas (the so-called “fiscal equivalence principle”), in practice benefit spillovers across jurisdiction borders form a common problem of decentralised service delivery. Benefit spillovers can lead to under-provision of public services if subnational governments do not take into account the benefits received by residents in other jurisdictions. Central government may intervene in these situations by paying matching grants to subnational governments to encourage extended service delivery. Other solutions to under-provision and spillovers include mergers of the smallest subnational governments and enhanced co-operation between local jurisdictions. These reforms can be voluntary, “bottom-up” reforms or centrally-led, “top-down” restructurings. The issue of benefit spillovers is not an easy challenge to solve, however, not least because each public service has a different optimal benefit area and internalising externalities in an existing structure is often difficult.

Decentralisation may result in loss of certain economies of scale (Oates, 1985^[51]). This could happen if subnational governments are unable to co-operate with each other or to outsource production to larger, neighbouring subnational governments or private companies. The risk of inefficient outcomes is smaller if subnational governments are responsible for both the spending on and financing of services because subnational self-financing provides a strong incentive to select the most efficient service production technology. In countries with small subnational government units, such as the Nordic countries, France, the Slovak Republic and Spain, subnational partnerships, joint authorities and outsourcing are frequently used to utilise scale economies. Municipal merger reforms are also often on the political agenda, especially in decentralised countries, to respond to economies of scale and benefit spillover problems.

Determining optimal subnational unit size is a context-specific task; it varies not only by region or country but by policy area, as well. The efficient size differs between waste disposal, schools or hospitals. In Finland, research on scale benefits of expanding the size of local governments found that large municipalities were less efficient at service delivery

and the optimal size was between 20 000 and 40 000 inhabitants (OECD, 2017_[15]; Moisio, Loikkanen and Oulasvirta, 2010_[52]). Yet in Japan, unit costs of public services bottomed out at about 120 000 inhabitants and increased at both higher and lower municipal sizes (OECD, 2017_[15]).

Municipal mergers may be considered effective in larger conurbations with a high degree of municipal fragmentation, but ineffective when the size of municipalities is already large or in remote areas where service delivery is largely determined by geography. Often, efficiency gains can be made without abolishing tiers or merging municipalities (OECD, 2017_[15]).

Decentralisation may increase disparities between subnational governments

Without specific measures that strengthen the capacity of poor regions, the benefits of decentralisation may accrue only to the most developed and prosperous regions, hence contributing to increased regional disparities. There can be important differences between subnational governments in a financial capacity and administrative skills, which can endanger the ability of lagging regions to catch up. It has also been argued that decentralisation may foster agglomeration effects, which could increase disparities (Bartolini, Stossberg and Blöchliger, 2016_[28]). These results may depend on the type of country, and its level of economic development. According to some studies, decentralisation may reduce regional disparities in high-income countries, while increasing them in low-income countries (Ezcurra and Rodríguez-Pose, 2013_[11]). On the other hand, these results also show that when the inefficiencies within a system are properly addressed by decentralisation processes, interpersonal inequality could decrease faster in less developed than in more developed areas. This would be despite the large capacity constraints (Ezcurra and Rodríguez-Pose, 2013_[11]).

In this context, it is also interesting to note the results from Albouy (Albouy, 2012_[53]), who argues that fiscal equalisation systems which are currently designed to support poorer areas, may, in fact, slow down much wanted economic growth both in lagging and in more prosperous regions. This could be because transfers could constrain inter-regional migration, which is an important component of economic growth, and because these transfers usually do not take into account the costs that accrue to major urban areas. Blöchliger and Pinero-Campos argue that equalisation transfers reduce fiscal disparities in the short term, but may reduce development incentives in the long run (Blöchliger and Pinero-Campos, 2011_[54]).

Decentralisation may risk uncoordinated public investment

Recent research results suggest that there is a positive association between decentralisation and total regional public investment. In particular, decentralisation in terms of revenue autonomy increases public investment in infrastructure (Kappeler et al., 2013_[55]). Public investment is nevertheless a shared responsibility among levels of government (OECD, 2013_[14]). Yet these are not all and not always equipped with the same level of capacity to ensure successful investment planning and implementation. Due to the long-term effects of investment decisions, errors made in the decision-making process are difficult and costly to correct. Without effective vertical and horizontal co-ordination, decentralisation may lead to inadequate scale and loss in public investment opportunities (OECD, 2013_[14]).

Finding the right balance between own-source revenues and transfers

How can we determine the level of own-source revenues, in particular of own-source taxes? There is no ideal model or rule for thresholds to determine a good level of revenue autonomy. It depends on the overall system, including the type of responsibilities managed by subnational governments and the overall institutional, economic, fiscal and social conditions framework. For example, one major difficulty of developing own-revenues is a country's level of development. It is difficult to solicit the taxpayer or the users of local services in poor countries where there is a high level of informality; where potential contributors are partially registered or not registered at all and have a very low level of income; where the land registry or the company register is non-existent or under-developed; where there are few local services or infrastructure that can be priced and generate user fees or charges; where tax administration is weak at the national and local levels; and where subnational governments lack the capacity to raise and manage revenues, etc. These challenges call for careful planning and implementation of decentralisation policies.

In addition, increasing own-source revenues, in particular through greater tax autonomy, may bring many benefits but also difficulties. There are pros and cons in some counter-arguments that can justify limiting tax decentralisation to a certain extent (Ter-Minassian, 2015^[56]) (Table 4.1).

Table 4.1. Increasing own-source revenue of subnational governments: Benefits and drawbacks

Benefits	Drawbacks
<ul style="list-style-type: none"> • Better quality and efficiency of spending to respond to community preferences. • More democratic accountability to citizens. • Better mobilisation of local resources. • Improved budget management efficiency. • Promotion of fiscal responsibility. • More capacity to access credit. • More incentives for growth-oriented economic and fiscal policies. 	<ul style="list-style-type: none"> • Higher mobility of tax bases within the national territory, hence increasing the scope for tax evasion and leading to a detrimental form of tax competition among subnational governments (SNGs) (race to the bottom). • Unequal distribution of tax bases, increasing revenue disparities and undermining SNG ability to provide common standards for basic public services. • Drop in the cost-effectiveness of subnational tax administrations (diseconomies of scale, lack of capacities). • Risk of greater fiscal instability for both subnational governments and the central government.

Sources: OECD (2017^[15]), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, <http://dx.doi.org/10.1787/9789264272866-en>; Ter-Minassian, T. (2015^[56]), “Promoting responsible and sustainable fiscal decentralisation”, in Ahmad, E. and G. Brosio (eds.), *Handbook of Multilevel Finance*, Edward Elgar Publishing.

Political risks

The political dimension behind decentralisation reform – to favour local democracy, improve the quality of governance, promote citizen participation and control, show accountability and transparency – has been somewhat left on the backburner in favour of a more economic approach focused on policy-relevant outcomes, such as education, health or fiscal sustainability (Faguet, 2011^[57]). This is partly explained by the fact that, in some countries, decentralisation has in reality been hijacked by local and national elites, as a strategy for mobilising and maintaining regional power bases (Devas and

Delay, 2006^[58]). This “elite capture” of local power structures has produced counter-productive outcomes, for example in terms of poverty reduction and corruption (Crook, 2003^[59]), but has also damaged the credibility of political arguments.

Local or central elite takeovers and corruption may compromise decentralisation benefits

It has been argued that in some cases the benefits of decentralised service delivery may primarily go to local elites. Particularly in developing countries, local jurisdictions may be vulnerable to capture by predatory pressure groups, who may be able to receive a disproportionate share of spending on public goods (Bardhan, 2002^[60]). Such unhealthy development would also increase opportunities for corruption. This underlines the importance of the institutions of local democracy and mechanisms of overall political accountability.

There is also the possibility of predatory central government, not just local elites. Predatory central government can compromise all or most of the benefits of decentralisation (Weingast, 2014^[7]). For instance, the ruling parties at the national level may try to affect local decision-making to avoid competition from most successful subnational governments. A central government transfer system may be used to affect local decision-making. At worst, predatory governments may even use their powers to reduce the authority of the local government, for example by taking over the local government and reversing its policies.

Administrative challenges

Unclear assignment of responsibilities

An important challenge of decentralisation is formed by overlapping assignments among levels of government. This challenge is repeatedly mentioned as a critical one in OECD Territorial Reviews and Economic Surveys, as well as in the International Monetary Fund (IMF) and World Bank country studies for developing countries. The challenge is true for unitary countries, but also some federal countries, such as Australia or Germany, for example.

A lack of clarity in the assignment of responsibilities makes service provision and policymaking costlier. It also contributes to a democratic deficit by creating confusion among citizens regarding which agency or level of government is responsible for a specific service, activity or policy. Without a clear assignment of responsibilities, it becomes almost impossible to hold leaders accountable for shortcomings or policy failures. It also hinders efforts at transparency and citizen engagement (Allain-Dupré, 2018^[16]).

This problem may arise especially in a multi-level governance system with several government tiers and with a large number of subnational governments. While the challenge can be mitigated with well-planned service assignments and taking into account the varying capacities of subnational governments, it is a very difficult situation to completely avoid in a decentralised environment. Overall, the assignment of functions to the most appropriate government tier plays an important role in minimising both unnecessary spillovers and overlapping responsibilities.

Several countries grapple with unclear assignments. In Brazil, the division of responsibilities is unclear in a number of areas, including healthcare, education, social

security, welfare, agriculture and food distribution, environmental protection, sanitation and housing. In Chile, municipalities have few exclusive competencies, and there are 13 national/municipal shared competencies with unclear or poorly established lines of interventions, which are also subject to change. In France, a 2017 report from the *Cour des Comptes* suggested going further in the clarification of the allocation of competencies between departments and intermediate governments and strengthening efforts to mutualise functions across municipalities (OECD, 2017^[15]).

The unclear allocation of responsibilities and functions is particularly notable for the policy areas which are most frequently “shared” among levels of government, in particular, infrastructure (transport), education, spatial planning, health and labour market policy:

- *Transport*: in Mexico, the competency for road construction and maintenance are divided between the three levels of government, with construction mainly executed by federal and state governments, and maintenance mainly carried out by the states or municipalities. In Ukraine, municipalities are responsible for infrastructure and its maintenance. At the same time, the road agency of the national government is responsible for roads, including their paving and repaving. In the case of a bridge (infrastructure), if its road-surface requires repaving, there is a high risk of inaction as neither level of government is compelled to act (OECD, 2018^[61]).
- *Education*: in most OECD countries, lower levels of government are responsible for managing and funding lower levels of schooling (mainly pre-elementary, primary and sometimes lower secondary education), whereas responsibility for secondary, and in particular upper secondary, schooling is more often retained at provincial/regional or central levels. Such arrangements, where sub-sectors of schooling operate under different political and administrative jurisdictions, may raise significant challenges concerning efficient use of resources (risks of competition, duplication and overlaps) and co-ordination of policies and actors.
- *Health*: healthcare systems seem to suffer greatly from an unclear division of responsibility, duplication, cost shifting and scale inefficiencies .
- *Labour market policy*: is often shared, with frequent overlaps among levels of government. Greater difficulty arises when several levels of government share the same functional responsibilities, within the same responsibility sector.

Unclear allocation of roles between subnational governments and deconcentrated central state administrations

Another type of challenge is linked to the often unclear allocation of roles between subnational governments and deconcentrated central state administrations in territories. Although the prevalence of deconcentrated central state administrations alongside autonomous subnational governments in the same territory has diminished in the past decades, the challenges remain important in some countries, such as Estonia, Finland, France, Hungary, Greece, Italy, Poland, Sweden, Turkey and Ukraine. Reconsidering these complex and often opaque arrangements could help facilitate the clear assignment of responsibilities.

Coordination of service delivery is a challenge especially in the case of redistributive services

In many countries, the provision of redistributive services, such as healthcare and secondary education, has been assigned to subnational governments. In such cases, central government is usually concerned with equity issues and co-ordination of service delivery. Without adequate central steering of subnational governments and with no mechanism that transfers resources to poor jurisdictions, decentralisation may lead to considerable differences in regional disparities in health, education and social service outcomes (Martinez-Vasquez, 2011^[62]). With the intention of securing access to services in all parts of the country and to guarantee a minimum quality of services for all residents, laws and other normative steering mechanisms are frequently used to regulate their provision and financing. The problem is then to strike a balance between co-ordination and local autonomy. With strict regulation, the benefits from decentralised provision may be radically diminished. Moreover, the bureaucracy costs can be high from such steering. On the other hand, with loose regulation, it is possible that differences between subnational governments become politically unacceptable.

It should also be noted that in a multi-level governance setting, the policy-makers are often confronted by a series of policy “gaps” (Charbit and Michalun, 2009^[63]) which can present a considerable challenge to governance.

Lack of subnational government capacity may limit benefits received from decentralisation

The lack of sufficient administrative, technical or strategic capacities is probably one of the bigger challenges in the field of decentralisation. Inadequate capacity may, therefore, be an argument for limiting or delaying decentralisation.

Beyond the fiscal capacity issues, reviews repeatedly report the lack of adequate capacities – in terms of staff, expertise, scale – to address complex issues such as strategic planning, procurement, infrastructure investment, oversight in local public service delivery, performance monitoring, etc. The institutional capacities of subnational governments vary enormously within countries, even the most developed ones (Tselios et al., 2012^[12]; OECD/CoR, 2015^[64])

Sometimes subnational governments may lack adequate human resources to plan, implement and manage public services. The professional quality (e.g. level of education and job experience in particular) of civil servants working in subnational governments is therefore key. If subnational governments were for some reason not able to hire the quality staff needed to provide services that meet the minimum standards, then decentralisation would pose a risk. In these cases, central government could support local capacity building with training and financial incentives. However, local leadership, community participation and local ownership of the service programmes are equally important factors behind successful local capacity building (Fiszbein, 1997^[65]). Without enough local commitment, the resources invested in strengthening subnational capacities may be wasted.

It should be acknowledged that building capacities takes time and therefore needs a long-term commitment from both central and subnational government levels. Even among the developed countries, the capacity differences remain considerable despite efforts to close the gap. For instance, the joint Consultation of Sub-national Governments among the OECD countries by the OECD and EU Council of Regions showed that two-thirds of

subnational governments (65%) reported that the capacity to design adequate infrastructure strategies is lacking in their city/region. More than half of the subnational governments (56%) reported a lack of adequate own expertise on infrastructure. These results were particularly strong in the case of small municipalities and inter-municipal structures (OECD/CoR, 2015^[64]).

Conclusion

While each country must find its own way to utilise the benefits and tackle the challenges of decentralisation, the policy experiences and research results that have accumulated over the past decades can help policy-makers to implement decentralisation reforms in a way that avoids the major pitfalls. For this purpose, the OECD has developed ten Guidelines for implementing decentralisation, which apply both to federal and unitary countries. These are described in the following section of this report. The guidelines are more than just recommendations. Each section covers the rationale of each guideline, key trends, good practices and not-so-good practices. The themes are elaborated with examples from federal and unitary countries.

Table 4.2. Benefits and challenges of decentralisation

Benefits	Challenges
	Economic and administrative effects
<ul style="list-style-type: none"> ● Allocative efficiency: Services are aligned with local demand, provided that SNGs have adequate spending autonomy. ● Efficiency of public service provision: Subnational governments have better information about local circumstances and conditions. This enables cost-efficient service provision. ● Service quality and availability: Yardstick competition incentivises locally elected decision-makers to focus on high-quality service delivery at reasonable cost. ● Innovation and experimentation: A higher number of jurisdictions combined with local autonomy facilitates local experimentation and promotes policy innovation, which benefits all tiers of government. ● Fiscal responsibility: Spending and revenue autonomy of subnational governments limits spending growth, which contributes to lower tax rates. Local taxing rights with a considerable share of spending financed from own revenue sources limits risks for overspending. ● More efficient revenue collection: Mobilisation of local resources in the case of taxing power decentralisation. ● Economic growth: Decentralisation contributes to better public services through competition and accountability. This can have a positive effect on economic growth and well-being of the population. ● Regional convergence: Decentralisation can help lagging regions to catch up. 	<ul style="list-style-type: none"> ● Benefit spillovers: With a large number of small SNGs, the externality problems may intensify. To solve this, extensive equalisation/transfer systems may be needed, which can make the funding system complex. ● Diseconomies of scale: If subnational governments are unable to co-operate with each other and if they are not allowed to outsource service production, inefficient service provision may result due to small scale. ● Overlapping responsibilities: Unless proper assignment of functions is ensured, administrative costs and waste may result from duplication of services. ● Lack of capacities: Adequate human and technical capacity is a prerequisite for successful decentralisation. Without sufficient capacities at the local level, decentralisation can be a risk, especially from the equity aspect. However, decentralisation can also create responsibility and ownership of public programmes, which may help in building capacity. ● Destructive competition: Fierce competition between subnational governments for taxpayers can lead to a “race to bottom” type of competition, which can have a negative effect on services. ● Macroeconomic stability: If central government is weak, it may not be able to resist demands for local bailouts. This can soften subnational government budget constraints. If local debt is allowed to accumulate without limits, the sustainability of public finances may be endangered. ● Disparities: Without policy measures that strengthen the capacity of the poor regions, the benefits of decentralisation may accrue only to the most developed and prosperous regions.
	Political effects
<ul style="list-style-type: none"> ● Accountability: Decentralisation changes the incentives of authorities serving local populations. Residents can express their opinion by voting (voice) or by moving to another jurisdiction (exit). These are powerful forces that strengthen accountability of public decision-making. ● Participation: Decentralisation increases the number of political arenas and provides more opportunities for local politicians. Voters will have more opportunities to express their opinions on local services and problems. This can increase participation in both the local and central decision-making level. ● Minorities: Decentralisation facilitates minorities’ participation, which improves the status and position of minority groups. ● Rent seeking and corruption: Decentralisation reduces the size of government units, which can make rent-seeking less interesting. More importantly, decentralisation increases competition between jurisdictions, reducing opportunities for corruption and rent-seeking. 	<ul style="list-style-type: none"> ● Local elite takeover: Particularly in poor countries, local jurisdictions may be vulnerable to capture by local elites, who may then receive a disproportionate share of spending on public goods. This can also create corruption. ● Central elite takeover: Subnational governments, especially in poor countries with a weak democratic tradition, may be unable to resist suppression and pressure of corrupt central government, for example, if the transfer system is used to strengthen the ruling parties’ position. ● Low political participation: Political participation may be low especially if subnational governments do not have real spending or taxing autonomy. ● Non-solidarity: Unless wide disparities are tackled with an equalising transfer system, decentralisation may increase accusations of favouritism. This can reduce consensus and agreement between regions and eventually increase political tensions in local and national politics. ● Risk of slow development and stagnation: If decentralisation results in increased numbers of veto players in important decisions.
<ul style="list-style-type: none"> ● Political stability: Decentralisation can reduce tensions arising for various historical, ethnic or cultural reasons by accommodating heterogeneity in public policy. Autonomic decision-making can suppress local motives for conflict with central administration. ● Number of political institutions: Decentralisation increases the number of independent political actors, which divides power both vertically and horizontally. This has a stabilising effect on society. 	

Notes

¹ Examples of such services include a wide collection of “neighbourhood services”, such as local infrastructure, parks, kindergartens, elementary schools and water and sewage.

² As measured in the IMF’s Government Finance Statistics.

³ The survey was conducted in 1999 and 2000 by a team from the World Bank. Managers from over 9 000 firms in more than 80 countries were surveyed with a standard questionnaire.

⁴ In the same vein, compared with fully centralised taxation, partial revenue decentralisation is a superior alternative, assuming benevolent decision-makers and provided that subnational governments are able to adjust public-good levels. This is mainly because of the allocation benefits from local discretion (Brueckner, 2009^[48]).

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Chapter 5. Making decentralisation work: A handbook for policy-makers

This chapter is the “handbook” component of this report. This chapter presents ten guidelines on selected key issues of decentralisation to aid the policy-makers to implement decentralisation reforms, as decentralisation outcomes depend very much on the way the process is designed and implemented. Each subsection follows the same structure: in the beginning, the issue in question is described and the key international trends and the rationale of the theme are discussed. The sections then present examples of good practices and pitfalls to avoid. The examples presented cover both unitary and federal countries. Finally, the key recommendations for policymakers are presented. A checklist to help identify the main aspects of the issue linked to the guideline in question is also provided in the end of every section.

Decentralisation is not an end in itself but should be part of a broader strategy of territorial development. Decentralisation outcomes depend very much on the way the process is designed and implemented, on adequate subnational capacity and on the quality of multi-level governance, including efficient co-ordination mechanisms across levels of government. Overall, it should be remembered that decentralisation reforms tend to take time and the assignment of responsibilities needs to be periodically reviewed.

A pragmatic approach to decentralisation should be adopted, based on an in-depth analysis of political, social and economic conditions of the country. The challenge of designing decentralisation has sometimes been compared to a soufflé where all ingredients must be present in the right amounts and prepared in the right way at the right time to achieve success (Sharma, 2018_[1]; Parker, 1995_[2]). But ingredients are not enough. The cooking is essential. Even if a decentralisation reform is well designed, it can face implementation challenges due to its complex and systemic nature. Decentralisation may produce unexpected perverse effects and undesired outcomes, making adjustments and fine-tuning necessary. The best-laid plans can fail due to implementation difficulties. There is a long and difficult path between theory and practice and between plans and experience in the field, made of “potholes, detours and road closures” (Shah and Thompson, 2004_[3]). Decentralisation as *a process* must receive the attention it deserves.

Making the most of decentralisation for regional development is particularly crucial in the current context of the growing “geography of discontent” and the increasing divides between places that have felt left behind by globalisation and technological change and those that have been able to seize the opportunities offered by these. Dysfunctional decentralisation systems are part of the story behind the current crisis of democracies: it is thus critical to find ways to make decentralisation systems work in a more effective way.

Subnational governments are particularly well placed to design and implement relevant regional and local development strategies by identifying local comparative advantages and responding to people’s needs. This implies that they enjoy some capacity and flexibility to act and identify local comparative advantages and relevant development projects, including adequate responsibilities and resources.

Ten guidelines to help make decentralisation work have been identified.¹ They are further broken down into detailed recommendations, with practical guidance, pitfalls to avoid, good practices and a checklist for action, tailored to both federal and unitary countries.

Guideline 1: Clarify the responsibilities assigned to different government levels

Definition

- Transparent division of powers means that the responsibilities of various levels of government have been codified in significant detail in legal and regulatory frameworks, and/or intergovernmental agreements, traditions, etc., and are widely disseminated. Such codification would clarify each sub-function, the role of various levels of government in policy, legislation, standards, oversight, financing, provision/administration, production, distribution, performance monitoring, evaluation, citizen complaints, feedback and redress mechanisms.
- Principled division of powers means that the following well-known assignment principles and related considerations are taken into account:

- *Fiscal equivalency principle.* Political jurisdiction and taxing (revenue) and benefit (spending) areas should overlap, i.e. local services should be self-financed by each local jurisdiction to ensure local autonomy, accountability and fair burden sharing while eliminating free rider problems.
- *Correspondence principle.* The jurisdiction that determines the level of public provision of each public good should include precisely the set of individuals who consume the good.
- *Decentralisation theorem.* Each public service should be provided by the jurisdiction having control over the minimum geographic area that would internalise benefits and costs of such provision.
- *Subsidiarity principle.* Taxing, spending and regulatory authority for any service should be vested in the lowest order of government unless a convincing case can be made for higher order assignment. Developing a convincing case to override subsidiarity would require combining economic, political, administrative, social, cultural and historical considerations to decide on a specific assignment. Note that application of these principles to individual circumstances yields unique country-specific results.
- *Balanced decentralisation principle.* Local and regional economic development requires integrated multi-sectoral, system-wide approaches. Balance in decentralised responsibilities should ensure that subnational governments are not hampered in their pursuit of improving economic and social outcomes by an ill-conceived, unbalanced division of powers.
- *Recognition of economies of scale and scope and inter-jurisdictional spillovers.* The assignment of functions needs to pay due consideration to economies of scale and economies of scope (appropriate bundling of local public services to improve efficiency through information and co-ordination economies, e.g. fire and ambulance services are better provided jointly) and to inter-jurisdictional spillovers to limit the free rider problem.
- *Asymmetric decentralisation principle.* To make decentralisation work, it is desirable that functional responsibilities be tailored to the local preferences and needs, demographic and geographic character (area, population size, topography, urban vs. rural, small towns vs. metropolitan areas, plains vs. mountainous region, agricultural vs. industrial towns, etc.) and fiscal capacity of local jurisdiction.
- *Stable assignments but subject to a review on a need basis.* Globalisation, the information revolution and a changing internal and external environment call for a periodic review of the assignment issues and for adaptation of the division of powers to a changing world and domestic orders. Institutions of executive and legislative federalism must be in place and empowered to address these issues on a need basis.

What are the key trends/data?

- Over the past several decades, there has been a persistent global trend towards decentralisation, at both the regional and municipal levels (with a few exceptions).

- Most responsibilities are shared among levels of government. The extent of responsibility sharing also depends on the service in question. For example, responsibilities tend to be shared more often in public transport than in childcare or elderly care (OECD, 2016_[4]). In most countries, due to the complexity of interactions in shared rule, many ambiguities in the assignment of responsibilities still remain.
- Given the diversity of regional and local governments in a country, a major trend in recent decades has been to tailor responsibilities to be consistent with local capacities, local circumstances, local needs and local preferences. These considerations have contributed to an increasing emphasis on an asymmetric assignment of responsibilities (Allain-Dupré, 2018_[5]).
- Shared responsibilities and division of powers require clarity with stability but an opportunity for a joint review on a need basis. Many OECD countries have continuously strived to improve clarity as well as to adapt to changing circumstances.

Rationale and benefits

- A principled and transparent division of powers is crucial for governments to deliver on their mandates and be held accountable by citizens. This is especially desirable for shared rule, i.e. when a function is the joint responsibility of several levels of government as is often the case in the provision of education, health and social welfare due to their redistributive nature. For preference matching and tailoring of programmes to specific local needs these services are best provided locally, but higher-order legislative frameworks and financing may be required for equitable provision.
- A lack of clarity in the division of powers for concurrent/shared responsibilities contributes to government failures or inefficiency and inequity in public service provision.
- A lack of clarity in responsibilities contributes to critical infrastructure needs not being addressed in a timely manner.
- Balanced decentralisation – i.e. when the various policy functions are decentralised to a similar extent – is conducive to growth. Balanced decentralisation allows subnational governments to better co-ordinate policy and to reap economies of scale and scope across functions (OECD, 2016_[4]).
- Citizen-based government accountability can only work if the citizens are well-informed about who is responsible for what and whom to approach to address their concerns about service quality or service failure.
- Clarity in the division of spending powers is critical for tax assignment and the design of higher order transfers to ensure consistency of revenue means with expenditure needs and other national objectives.
- Clarity in the division of power is critical to building subnational government capacities as well as instituting mechanisms for intergovernmental as well as beyond government partnership and co-ordination.

What are examples of good practices?

Federal countries

- Reasonably clear division of powers exists in the newer federal constitutions of Canada, Germany and Switzerland, backed by appropriate legislative and legal frameworks and intergovernmental agreements.
- In Switzerland, reforms over the 2004-08 period clarified federal and canton competencies and provided incentives and the mechanism for the formalisation of inter-canton co-operation agreements. Since 2008, Switzerland has further clarified federal and cantonal roles in specific policy areas and developed a new framework for inter-cantonal collaboration in order to avoid fragmentation and unproductive competition for schools and higher education, culture, waste management, wastewater treatment and urban transport.
- Following the 2011 intergovernmental agreement, Belgium has devolved additional responsibilities in employment, healthcare, social assistance for the elderly and disabled and family support and justice to the regions and communities.
- During the past decade, Germany transferred responsibilities in staff management, economic functions, and trade and justice to the lander and clarified the division of powers for university education and the environment. It also reformed intergovernmental fiscal relations. The German Bundesrat passed legislation in 2017 to terminate the current inter-state horizontal equalisation programme upon expiry in 2020, and to shift the responsibility for equalisation to federal goods and services tax (GST) revenue sharing and specific purpose programmes (Shah, 2017_[6]).
- In 2013, Austria established a Commission on Tasks and Deregulation to develop further clarity in the respective roles of various orders of government (OECD, 2017_[7]).

Quasi-federal countries

- In 2013, Spain adopted a reform to clarify municipal competencies and prevent duplication under the principle of “One Administration, One Competence”. The reform aims at reducing competencies which are not attributed by law or delegated by other administrations without adequate resources (known as “improper competencies”). The Local Reform intends to improve the definition of local competencies. To do so, a list of core competencies was established. Competencies which are not included in this list are referred to as “non-core competencies”. In the event of any agreements delegating competencies from upper levels of government – usually, the Autonomous Communities – to lower levels of government, it is compulsory to provide corresponding resources earmarked for financing the services involved.

Unitary countries

- In recent years, Denmark, Japan and the Netherlands have introduced reforms to clarify competencies of central and local governments and areas of intergovernmental co-operation.
- Denmark reformed its subnational government in 2007. The reform reassigned the tasks among levels of government, merged municipalities and reduced the number of intermediate governments (counties). As a result of the reform, counties were granted responsibility for the most demanding healthcare services, including hospital services. Municipalities gained responsibilities for health promotion, social welfare and education. One of the aims of the structural reform was to reduce the degree of shared assignments and reduce incentives for cost shifting between government levels. In order to tackle the latter problem, the municipalities were obliged to co-finance the rehabilitation services and training facilities provided by the counties.
- In Japan, the 1999 decentralisation law eliminated opaque central decision-making on local responsibilities and clarified competencies more generally. Subsequent waves of reform have continued to develop the goals of greater municipal autonomy, clear delineation of responsibilities, and proper financing.
- In the Netherlands, the Dutch decentralisation reform of 2012-15 aimed to reallocate competencies between the different levels of government, in particular by re-enforcing provincial and municipal responsibilities and by establishing a simpler and clearer division of responsibilities among the different public actors, avoiding the overlapping of functions.

What are the pitfalls to avoid/risks?

- For concurrent powers, a legal framework must establish which order of government has legislative supremacy in the event of a conflict. If multiple orders of government have exclusive jurisdiction in sub-areas of a function, for example, environmental impact assessment, then inter-governmental agreements must specify the precise processes to reach an agreement and to resolve conflicts in allowing projects to proceed. In the absence of such clarity, critically important projects may be unduly delayed or even abandoned.
- The separation of operating and capital expenditure functions contributes to catastrophic service failures by not having proper upkeep of critical infrastructure facilities or building infrastructure for which there is no financing for upkeep, i.e. creating white elephants.

What are the recommendations?

- Develop a framework of representative assignment of responsibilities based on assignment principles (Kim and Dougherty, 2018^[8]; Broadway and Shah, 2009^[9]). Use this as a starting point for developing an inter-governmental consensus for clarity in responsibilities (including sub-functions and major tasks) that is tailored to local circumstances and mutually acceptable and

agreeable to all orders of government. Given the predominance of shared rule especially between provincial/regional and municipal levels, in practice “[...] the question is not of a clear-cut allocation of responsibilities, but rather of how to manage shared functions and responsibilities”.

- Clear assignment is critical for accountability, monitoring and effectiveness of investment and service delivery policies. The more a responsibility area is shared across different government levels, the greater clarity is needed to reduce duplication and overlaps.
- Clarity does not mean that shared responsibilities should be avoided, as this is by definition impossible. It means that the way responsibilities are shared should be explicit, mutually understood and clear for all actors, including citizens.
- Ensure balance in the way different responsibilities and functions are decentralised. Balanced decentralisation, that is, when the various responsibilities are decentralised to a similar extent, is important to local economic development and growth (OECD, 2016^[4]). OECD work has shown that “infrastructure investment alone has little impact on regional growth unless it is associated with human capital (investment) and innovation” (OECD, 2014^[10]).
- It is important to ensure balance in the way various policy functions are decentralised, to allow for complementarities across decentralised policies and integrated policy packages, for effective territorial development approaches (OECD, 2014^[10]). Balanced decentralisation – i.e. when the various policy functions are decentralised to a similar extent – is conducive to growth (OECD, 2016^[4]).
- An effective regional or local development strategy requires a balance in the way policy areas are decentralised. If decentralisation only takes place in two or three policy areas (like health or housing) in an unbalanced way vis-à-vis other policy areas, this will prevent subnational governments from designing integrated regional and local development strategies.
- Within each function, the responsibilities should be balanced. For example, it is not recommended for one level to have an exclusive focus on operating functions. Within functions, if a level of government is involved in financing, it is recommended to have a balanced focus on operating versus capital expenditure, rather than a focus only on operating expenditure.
- Reform is “eternal”. Conduct periodic (e.g. every 10 years) joint reviews of the working of the whole of government, especially performance in service delivery, to seek further improvements in the existing assignment.
- For social services, consider devolving service delivery and network co-ordination responsibilities to local governments, especially in the case of redistribution. Central and regional governments, however, should retain responsibility for financing and setting national minimum standards to ensure equitable provision. Also, network co-ordination (including horizontal inter-municipal co-ordination) should be encouraged and rewarded by higher order governments. This is done in Finland.

- Strengthen institutions of executive and legislative federalism (inter-legislative and inter-governmental consultation and co-ordination) and ensure their functioning on a regular, pre-determined, as well as emergency, basis.
- For natural disasters consider empowering subnational governments to assume the lead role in co-ordinating the response to all orders of government and beyond government entities.

Guideline 1. Clarify the responsibilities assigned to different government levels

Checklist	Yes	Partially	No
Legislative powers of various orders are clearly demarcated by: ● Constitution ● National legislation ● Other (executive orders, agreements) ● All of the above?			
For shared functions, is there clarity in the division of powers: ● Who sets the policy ● Who decides on the standards ● Who is responsible for oversight ● Who is responsible for financing ● Who is responsible for service provision ● Who produces the service ● Who monitors and evaluates service delivery ● How do citizens provide feedback			
For each of the shared functions and sub-functions, are there institutional mechanisms in place for: ● Consultation/co-ordination ● Burden sharing ● Conflict resolution			
Sub-functions within each function are decentralised to a similar extent			
Subnational governments are empowered to pursue integrated approaches to local economic development			
There is a separation of decision making for capital and operating expenditures			
The authority to hire, fire and set terms of reference and day-to-day management/supervision for own employees rests at the same level for each function			
There is a separation of decision making among various levels on planning, policy, finance and provision for each function			

Guideline 2: Ensure that all responsibilities are sufficiently funded

Definition

- Jurisdictional fiscal equity requires that responsibilities for spending (expenditure needs) must be consistent with revenue means (own revenues, shared taxes and transfers) for each order of government to discharge its public service responsibilities consistent with its mandate.

What are the key trends/data?

- The alignment of responsibilities and revenues remains an area of concern in most countries. In most countries, subnational expenditure far exceeds subnational tax revenues indicating a vertical fiscal gap that is filled by other sources of revenue, i.e. non-tax revenues and transfers.
- In almost all OECD countries, spending is more decentralised than revenue. This is partly because central governments need more finances than their direct expenditure requirements to ensure equity and balanced development.
- The decentralisation of taxes on mobile bases can distort the allocation of mobile factors of production and can induce wasteful tax competition across subnational governments. This mismatch should be managed by equalisation and output-based transfers and sufficient revenue autonomy for decentralised taxes. In the absence of these, the national government may be inclined to use its spending power too intrusively and may be too heavy-handed in influencing subnational government priorities. Also, any negative changes in the national government fiscal situation may have adverse consequences for basic regional/local services. This misalignment represents an unmet challenge in many OECD and most developing countries.
- A rough indicator of mismatch of own revenues with expenditure needs is given by the vertical fiscal gap. A vertical fiscal gap refers to the fiscal deficiency arising from differences in expenditure needs and revenue means of local government. These deficiencies are partially or fully overcome by higher-level financing. Therefore, a vertical fiscal gap is a measure of fiscal dependence of local government on higher-level financing.
- The design and nature of higher-level financing have implications for the fiscal autonomy of local governments. It must be recognised that a vertical fiscal gap, while being a useful concept, cannot be considered in isolation. Also, other related indicators should be used in order to reach better judgement on local fiscal autonomy. In all regions, there are subnational governments with a high share of expenditures and high reliance on financing from above (e.g. Brazil, Ireland and Turkey).

Rationale and benefits

- Consistency between revenue-generating means with expenditure needs is conducive to political accountability and responsiveness to local preferences. This is especially so when revenue means are dominated by own or concurrent tax revenues.

- Shared taxes and unconditional and equalisation transfers are also helpful if they are stable and predictable.
- Conditional grants with input conditionality weaken incentives for local accountability and responsiveness to local preferences. The risk is somewhat reduced if most transfers are unconditional formula-based grants. Nevertheless, there are some cases where earmarked grants, especially output-based grants, can be used in an efficient way.

What are examples of good practices?

Federal countries

- In Canada, subnational governments have access to all the revenue sources, except customs duties. To encourage harmonisation of concurrent tax bases, the Federal Government of Canada has, in the past, offered tax abatement (reduction of federal rate to allow more room for provincial tax rates) and tax-base sharing (levying a supplementary rate on a uniform federal base) options to provincial governments while waiving cost of federal collection of the provincial share. More recently, it offered provinces and the private sector representation on the board of the autonomous tax collection agency.

Unitary countries

- In Sweden, the subnational financing system is mostly based on own-source revenues and the system provides a sound base of funding for all subnational governments, while also enabling autonomy in subnational decision-making (OECD, 2017_[11]).
- In Poland, the 2004 Act on Local Government Revenue modified the financing of subnational governments. They gained more financial autonomy with a decrease in the share of central transfers. The use of earmarked grants especially was reduced. At the same time, tax sharing on personal income tax (PIT) and corporate tax revenues was introduced (OECD, 2008_[12]; Regulski and Drozda, 2015_[13]).

What are the pitfalls to avoid/risks?

- Unfunded and underfunded higher-level mandates undermine local accountability and can endanger service provision.
- Conditional (earmarked) input-based transfers should be avoided because they weaken incentives for local accountability and responsiveness to local preferences.
- Fiscal equity may be undermined by significant tax decentralisation unless accompanied by fiscal equalisation transfers.
- Lack of clarity in responsibilities is a major contributing factor to misalignment of revenue means with expenditure needs.
- Redistribution should not be solely based on local financing because of the externalities involved.

- Business should be taxed only for services to business and not for redistributive services.
- Profit, output, sales and movable asset taxes may drive business out of the local jurisdiction. Therefore, business services should be mainly financed through onsite/land value taxes and user charges.
- Resource rent taxes should either be centralised and redistributed through a national fiscal equalisation system, or alternatively, if such taxes are decentralised then they should be accompanied by an inter-state (net) equalisation programme.

What are the recommendations?

- Access to finance should be consistent with functional responsibilities. The division of financing responsibilities should ensure that there are no unfunded or under-funded assignments or mandates.
- Higher-level mandates must be fully financed by the higher-order government.
- Taxes on immobile bases, resource royalties, conservation charges, payroll taxes, single stage sales taxes, sin taxes, taxes on “bads”, motor vehicle registration taxes, business taxes, excise taxes, land and property taxes, frontage charges, poll taxes and user charges are all suitable for subnational assignment (Table 5.1).
- In addition, subnational governments may be allowed to piggyback on national taxes on (residence-based) personal income, wealth and carbon taxes. Table 5.1 presents a representative view of tax assignment. However, this view requires adaptation to suit local circumstances, for instance, the extent of assigned responsibilities.
- The decentralisation of revenue-raising responsibilities should be accompanied by a system of equalisation of revenue-raising capacities designed to ensure that different subnational governments have the potential to finance a comparable level of public services at comparable tax rates (see Guideline 10).
- Specific purpose transfers should embody output-based conditionality.
- The formulae for determining central government transfers, grants and earmarked funds from the centre to lower levels of government should be transparent and non-discretionary.

Table 5.1. Representative tax assignment

National	National/provincial	State/provincial	Local	All levels
Customs	Personal income	Single stage sales	Property	Sin taxes
Value-added tax	Taxes (residence-based)	taxes	Land	Taxation of “bads” (environmental pollution)
Corporate income tax		Motor vehicle registrations	Betterment/frontage charges	
Resource rents/profits	Payroll	Business	Surcharge on personal income tax	Poll
Wealth/Inheritance	Excises on alcohol and tobacco	Royalties		User charges
Carbon		Conservation charges	Parking	

Guideline 2. Ensure that all responsibilities are sufficiently funded

Checklist	Yes	Partially	No
There are no unfunded mandates			
• At the provincial/regional levels			
• At the local levels			
Some subnational governments do not fail to reach service standards			
There is a large variation in tax bases between subnational governments			
Equalisation transfers are in place			
• For cost equalisation			
• For revenue base equalisation			
The formulae for determining central government transfers, grants and earmarked funds from the centre to lower levels of government are transparent			
There are tax base sharing options available for residence base personal income taxes and carbon taxes			
• To provincial/regional governments			
• To local governments			

Guideline 3: Strengthen subnational fiscal autonomy to enhance accountability

Definition

- *Fiscal autonomy* refers to the ability of a subnational government to undertake fiscal tasks (taxing, spending, debt raising and financing) without seeking approval/clearance/authorisation from another order of government. For taxing powers, it implies that the subnational government has the constitutional/legal/administrative authority to determine the rate and base of local revenue sources both for tax collection and administration and also for some higher-level revenues it is empowered to levy supplementary rates on a higher-level tax base.
- *Revenue autonomy* would be strong if own revenues more or less matched responsibilities, i.e. finance majority of own expenditures, and also if higher order transfers are predominantly formula-based and unconditional. In addition, subnational governments have the unconstrained opportunity to access the capital market to finance long-lived investments by issuing bonds or through borrowing.
- *Expenditure (spending) autonomy* refers to the independence of the subnational government in making sectoral allocation choices, deciding on the level and composition of spending on specific areas within their own responsibility, setting service standards, determining modes of production, distribution/delivery, local planning and procurement without making any reference to a higher order government.
- Subnational accountability refers to the subnational government being accountable primarily to own electorate for its decision making.
- The term “tax autonomy” captures various aspects of the freedom subnational governments have over their taxes. It encompasses features such as the subnational government’s right to introduce or to abolish a tax, to set tax rates, to define the tax base or to grant tax allowances or reliefs to individuals and firms (Table 5.2). In a number of countries, taxes are not assigned to one specific government level but shared between the central and subnational governments. Such tax sharing arrangements deny a single subnational government control on tax rates and bases, but collectively subnational governments may negotiate the sharing formula with the central government.

Table 5.2. OECD Rating Methodology for Taxing Power

a.1	The recipient subnational government sets the tax rate and any tax reliefs without needing to consult a higher-level government.
a.2	The recipient subnational government sets the rate and any reliefs after consulting a higher-level government.
b.1	The recipient subnational government sets the tax rate, and a higher-level government does not set upper or lower limits on the rate chosen.
b.2	The recipient subnational government sets the tax rate, and a higher-level government does set upper and/or lower limits on the rate chosen.
c.1	The recipient subnational government sets tax reliefs – but it sets tax allowances only.
c.2	The recipient subnational government sets tax reliefs – but it sets tax credits only.
c.3	The recipient subnational government sets tax reliefs – and it sets both tax allowances and tax credits.

d.1	There is a tax-sharing arrangement in which the subnational governments (SNGs) determine the revenue split.
d.2	There is a tax-sharing arrangement in which the revenue split can be changed only with the consent of SNGs.
d.3	There is a tax-sharing arrangement in which the revenue split is determined in legislation, and where it may be changed unilaterally by a higher-level government, but less frequently than once a year.
d.4	There is a tax-sharing arrangement in which the revenue split is determined annually by a higher-level government.
e	Other cases in which the central government sets the rate and base of the subnational government tax.
f	None of the above categories a, b, c, d or e applies.

Note: This is the classification used in the data collection exercise but there may be a need for clarification in the future. For example, the sub-division of the “c” category cannot be applied to sales taxes (including VAT) where the concepts of allowances and credits (in the sense that they are used in income taxes) do not exist. Also, it may be more appropriate to qualify the definition of the “d.3” category by saying that the change is normally less frequent than once a year, as specific legal restrictions on frequency may not exist.

Source: OECD (n.d.^[14]), *OECD Fiscal Decentralisation Database - OECD Network on Fiscal Relations across Levels of Government*, <http://www.oecd.org/media/oecdorg/directories/centrefortaxpolicy/ndadministration/A%20taxonomy%20of%20tax%20autonomy.doc>.

What are the key trends/data?

- Tax autonomy has increased slightly in OECD countries in recent decades. Since 1995, tax autonomy has increased, at the expense of tax-sharing systems (Blöchliger and Kim, 2016^[15]).
- The structure of subnational government revenue varies greatly across countries. Countries with the highest level of taxes (excluding social contributions) in their subnational revenues include Canada, Denmark, Finland, Germany, Iceland, Japan, Switzerland, Spain, Sweden and the United States. The share of tax revenue is not an indication of tax autonomy, which depends on many factors, such as the right to introduce or to abolish a tax, to set tax rates, to define the tax base or to grant tax allowances or relief to individuals and firms
- In OECD countries, local fiscal autonomy is fairly high, whereas such autonomy is lacking in most developing countries, especially in Africa and the Middle East regions.

Rationale and benefits

- Subnational governments work best when local residents self-finance local services through local taxes and charges (Geys, Heinemann and Kalb, 2010^[16]; Blöchliger and Kim, 2016^[15]). This enhances the efficiency and accountability of local service provision by encouraging local residents to evaluate the costs and benefits of local service provision, and benchmark local government performance against itself as well as with neighbouring jurisdictions. Such performance evaluation enhances voice and exit options for residents and facilitates both voting by ballot as well as voting with feet behaviours.
- This also facilitates yardstick competition, which encourages local politicians to maximise the welfare of local residents instead of promoting their own self-interested goals. An empirical study by Geys, Heinemann and Kalb using a broad panel of German municipalities demonstrates that local fiscal autonomy has a positive, significant effect on voter involvement which in turn has a positive significant impact on cost efficiency (2010^[16]).

What are examples of good practices?

Federal countries

- Canada, Switzerland and the US have a high degree of fiscal autonomy at the state and local levels. The Canadian Federal Government provides police services to smaller municipalities on a fee-based basis². Tax collection services are offered by Revenue Canada to provinces without fee if they agree to harmonise their tax base with the federal government, and provincial and private sector representatives serve on its governing board.

Unitary countries

- Denmark, Finland, Iceland, New Zealand and Sweden have a high degree of local fiscal autonomy. Examples of countries that have fairly recently enhanced subnational fiscal autonomy include the Netherlands, Poland and the UK (in a more modest sense).

What are the pitfalls to avoid/risks?

- Financing systems with a minor share of own-source funding should be avoided especially in the case of local public services. Self-financing and full fiscal autonomy is most desirable to finance municipal and economic services.
- Fiscal transparency is critical for local accountability. Local accountability works best in the presence of democratic political governance and citizen-voter activism but this requires that voters are fully informed about the government operations. Unclear systems with vague information should be avoided.
- For redistribution, a full or major share of local funding is not ideal without further measures because in these cases subnational governments do not necessarily take the externalities into account. Therefore, in the case of social services, subnational governments should be given autonomy in local design and delivery of services, but financing and minimum standard setting by higher levels would be desirable in the interest of equity in service provision due to varying fiscal capacities of subnational governments.
- Very loose fiscal rules can be problematic especially if central government transfers form a major share of funding for subnational governments. Therefore, for subnational government borrowing, a higher-order regulatory framework to deal with bankruptcy and insolvency issues, as well fiscal rules for fiscal discipline, is desirable to minimise fiscal risks and to restrain imprudent fiscal behaviours.

What are the recommendations?

- Subnational governments should have a certain degree of autonomy in the design and delivery of their public service responsibilities within the limits set by normative regulations, such as minimum service standards.
- It is important for subnational governments to have a balanced system based on a basket of revenues. Subnational governments should have a diversified

funding system based on grants (for delegated functions), tax revenues, tariffs and fees, and property income. Tax revenues should be a mix of shared and own-source taxes, including a minimum level of own-source taxes in particular to finance exclusive responsibilities. A higher own-tax share may contribute to making subnational governments more efficient and accountable and help mobilise resources at the state/regional and local levels.

- Subnational governments should be able to co-ordinate services provided by all orders of government in their jurisdiction and private and non-profit interest-based networks in the local area.
- Central government should retain control at least over major tax bases such as personal and corporate income tax (PIT and CIT). Since the central government is responsible for economic stability and for redistribution, the central government should be able to co-ordinate tax policy.
- Subnational governments should be encouraged to enter into partnership arrangements for service delivery to reap economies of scale and scope with other governments and beyond government providers. Subnational governments should be empowered to contract out some services for a fee to other governments and beyond government providers.

Guideline 3. Strengthen subnational fiscal autonomy to enhance accountability

Checklist	Yes	Partially	No
On tax bases assigned to them, subnational governments have autonomy to: <ul style="list-style-type: none"> • Set revenue bases • Set tax rate • Be responsible for tax collection • Set supplementary rates on higher order bases • Set user charges/fees for own services 			
Subnational government own revenues finance a large share of their expenditures			
Higher order transfers are mostly: <ul style="list-style-type: none"> • Formula based • Unconditional • Stable • Predictable 			
Subnational governments have the freedom to access capital market finance: <ul style="list-style-type: none"> • Borrowing for long term infrastructure projects • Issue bonds 			
Subnational governments have the autonomy: <ul style="list-style-type: none"> • To decide on sectoral allocations • To decide on level and composition of spending on any category of own service • To set service standards depending on service • To choose modes of production (outsourcing, own production, co-production) • To decide on procurement within limits set by central governments • To decide on local planning taking into account regional and national planning strategies • To enter into co-operation agreements with governments and beyond governments 			

Guideline 4: Support subnational capacity building

Definition

- A subnational government's capacity refers to its ability to perform its mandatory functions effectively, efficiently and sustainably. It refers to a subnational government's constitutional/legal/traditional empowerment, resources, competencies, skills and organisation as a whole, its ability to undertake collective action and create and sustain public value.
- Administrative capacity refers to the ability of a subnational government to deliver its mission/mandate in an efficient, fair, accountable, incorruptible and responsive manner. It entails the subnational government having the: i) ability to deliver high quality services in an efficient and equitable manner; ii) ability to hire, fire and set terms of employment of own employees; iii) capacity to co-ordinate or co-deliver policies and programmes with other governments (horizontally and vertically) and beyond government stakeholders; iv) wherewithal to carry out prudent fiscal and financial management with a high degree of transparency; and v) ability to audit and evaluate own services.
- Institutional capacity refers to having an effective legislative, executive, intergovernmental and beyond-government partnership and co-ordination, audit, evaluation and citizen feedback institutions in place.
- Strategic capacity refers to the ability to set strategic goals for social, political and economic outcomes and having the administrative and institutional capacity to realise those goals within the stated time frame.
- Financial management capacity refers to the ability of subnational governments to ensure the effective use of internal and external resources with integrity. This includes cash management, transparent procurement processes to mitigate corruption, ability to decide on how and when to use debt, how to assess debt affordability, what debt to use, how to issue and how to manage debt, how to use internal controls and internal and external audits to ensure efficiency and integrity.

What are the key trends/data?

- Decentralisation reforms have enhanced the relative importance of subnational governments in the finance and delivery of public sector programmes. To perform the newly assigned tasks more efficiently, there is increasing emphasis placed on enhancing subnational government capacity to meet newer challenges. While subnational governments strive to meet these challenges, they face formidable obstacles in view of resource constraints or deficient capacity more generally.
- A survey conducted by the OECD and the EU Committee of the Regions in 2015 indicates that subnational government capacities vary enormously within countries in all countries surveyed and are not consistent with their responsibilities. Smaller municipalities are hampered by having an inadequate pool of managerial and technical talent and service providers. Larger municipalities, on the other hand, face complex transport, urban

planning and infrastructure tasks and do not have the workforce skills to address these tasks effectively.

Rationale and benefits

- Administrative, institutional and strategic capacity is critical to the working of a (subnational) government. This is especially critical for regional development strategies that require substantial citizen input and co-ordination across and beyond governments.
- Uniform service delivery requirements by all local governments pose additional bottlenecks if some local governments do not have the capacity or local priority to meet these requirements. In the presence of heterogeneous capacities, competitive grants, capital market finance and Public Private Partnerships (PPPs) compound the difficulties for deficient capacity in local governments, especially among rural local governments, and can contribute to wider local inequalities.

What are the examples of good practices?

Federal countries

- In US, the National League of Cities (NLC), a voluntary organisation of municipalities, has established an NLC University to impart online and face-to-face training in municipal governance. It also produces toolkits and other training materials of use to municipal leaders and officials. In Canada, the Federation of Canadian Municipalities (FCM) plays a similar capacity development role.
- In Switzerland, Regiosuisse is the network unit for regional development. It was launched in 2008 by the State Secretariat for Economic Affairs (SECO) as an accompanying measure for the implementation of the New Regional Policy (NRP), and it supports SECO in the policy's implementation at the state, cantonal and regional levels. This is done by providing systematic knowledge management, opportunities for networking and further education. The main task of Regiosuisse is to build up knowledge management for the NRP and regional development in general. Regiosuisse maintains and continuously develops a set of interrelated tools for knowledge management.

Unitary countries

- In 2007, Chile created the *Academia de Capacitación Municipal y Regional* to strengthen subnational capacities. It aims to be a technical reference for subnational staff and to strengthen human resources in municipal and regional governments to support a broad spectrum of knowledge of use in various territorial situations. It provides free training, in-person and online training for public servants. In addition, a Fund for the Training of Municipal Public Servants was created in 2014, financing technical and professional studies for municipal personnel (OECD, 2017^[7]).
- In Colombia, KiTerritorial is a toolkit developed by the Department of National Planning (DNP) that offers specific instruments to support local leaders in the formulation of their territorial development plans (PDT). The

toolkit is organised around four pillars of operation that local governments should follow when developing their PDTs: i) diagnosis; ii) strategy; iii) investment plan; iv) monitoring and evaluation. The DNP has also developed an index of institutional capacity in municipalities, which permits measuring municipal performance along four dimensions: effectiveness, efficiency, compliance with legal requirements and management. Indices are published annually, contributing to the enhancement of accountability to citizens (OECD, 2016^[17]).

- The European Union has strengthened its focus on administrative capacity for the use of funds for 2014-20. EU countries are required to set performance criteria, clearly define responsibility, separate managing and auditing functions, and ensure stability and qualifications of staff. Almost EUR 4.3 billion will be allocated to building additional institutional capacity for public authorities and increasing the efficiency of public administration and services (an increase of 72% compared to 2007-13). For the post-2020 financial period, the European Commission is proposing that member countries be required to develop roadmaps of actions planned to reinforce administrative capacities for the management of EU funds, notably targeting subnational governments.

What are the pitfalls to avoid/risks?

- One size does not fit all. Capacity development programmes must be tailored to the needs of individual local government units based upon a careful assessment of local needs.
- Capacity should not be seen as a constraint to get the government right, i.e. having a principled and transparent division of powers across governments. Bottlenecks in capacity can be overcome with time whereas in the short run such capacity gaps could be filled through borrowing/contracting capacity from associations of subnational governments, higher orders of government or the private sector, for example.
- Capacity-building programmes often lack a long-term dimension. Building and strengthening subnational capacities is a long-term commitment which requires sustained resources and political commitment from both subnational and central/federal government levels.
- Capacity building programmes are often too narrow, focusing on training and technical assistance, without a comprehensive diagnosis of the different dimensions involved.

What are the recommendations?

- Governments should seek to reinforce the capacities of public officials and institutions with a systemic approach, rather than adopting a narrow focus on technical assistance only.
- Central government should assess capacity challenges in the different regions on a regular basis and adapt policies to strengthen capacities to deal with the various needs of territories.

- Staff training should be established that covers local public financial management and it should be mandatory that relevant staff pass this training. Institute mandatory training for budgeting department staff in budget methods, budget formulation, budget execution, revenue analysis, as well as strategic planning.
- Distribute formal/standardised guidance documents in areas such as planning, project appraisal, procurement, or monitoring and evaluation is very cost-effective.
- Promote open, competitive hiring and merit-based promotion as well as policies, such as special pay scales for areas of needed technical expertise.
- Creating special public agencies accessible to multiple jurisdictions in areas of needed expertise helps support subnational capacities (e.g. PPP units, regional development agencies).

Guideline 4. Support Subnational Capacity-building

Checklist	Yes	Partially	No
Subnational governments have the administrative capacity to: <ul style="list-style-type: none"> • Prepare physical and financial plans and to evaluate alternative plans • Develop and implement appropriate policies • Develop regulatory and legal frameworks • Develop and manage partnerships • Co-ordinate the activities of multiple stakeholders • Prepare own budgets • Determine revenue requirements for budgetary balance and raise any additional revenues • Determine own capital financing needs • Access capital market finance on a need basis • Determine staffing needs • Develop a human resource management framework • Facilitate alternative service delivery mechanisms • Carry out internal controls and internal audits • Ensure integrity and transparency of procurement processes • Carry out periodic evaluation of own programs 			
Subnational governments have the strategic capacity to: <ul style="list-style-type: none"> • Develop strategic plans for local and regional economic development • Set realistic objectives and goals 			
Subnational governments have the financial management capacity to: <ul style="list-style-type: none"> • Decide on better practices for financial accounting and reporting • Issuing and managing debt 			

Guideline 5: Build adequate co-ordination mechanisms among levels of government

Definition

- To make multi-level governance work, a dense network of national/regional/local political and bureaucratic interactions, especially for shared rule, becomes a necessity. This requires developing formal and informal, vertical and horizontal mechanisms and processes of inter-governmental consultation, co-ordination, co-operation and joint decision-making. This should also involve senior policymakers and officials, i.e. the so-called inter-governmental fora and legislative consultation through inter-legislative fora. The interactions through these fora can be co-operative and consultative, or in some cases coercive, depending upon the power relations among the various orders of government in a country.

What are the key trends/data?

- Although challenges remain numerous, a number of OECD countries – in particular, federal countries and Nordic countries – have made progress toward better vertical co-ordination among levels of government (OECD, 2019 forthcoming^[18]).
- Platforms for vertical co-ordination have been established in several OECD member states, in particular, federal countries. Eleven OECD countries have put co-ordination structures in place. These are often related to environment, infrastructure, transport, technology and development. In 14 countries, the national government needs to consult subnational governments prior to issuing new regulations (OECD, 2017^[19]).
- The 2007-08 financial crisis spurred investment in both ad hoc and permanent bodies for horizontal and vertical co-ordination in several countries, though in some cases only at the intermediate level. Fiscal councils and internal stability pacts have been used since the crisis to strengthen multi-level fiscal co-ordination in macroeconomic management. Austria, Belgium, Brazil, Germany, Italy, Portugal and Spain, have all strengthened or expanded these institutions in recent years (OECD, 2017^[19]).
- Standing commissions and intergovernmental consultation boards that create a permanent conduit for co-operation and communication across parties and levels of government can facilitate reform when the time comes, despite their expense and the time needed to establish them. Creating a culture of co-operation and regular communication is crucial for effective multi-level governance and long-term reform success.
- Among 15 dimensions of institutional quality for efficient public investment management, central-local co-ordination is the dimension where advanced economies tend to fare the worst (IMF, 2015^[20]).

Rationale and benefits

- Multi-level governance implies managing mutual dependence among levels of government, and a series of gaps or co-ordination failures that may occur among them (OECD, 2014^[10]; 2013^[21]; Charbit and Michalun, 2009^[22]). Such

co-ordination failures may be overcome by governance tools such as dialogue platforms, partnerships/contracts across levels of government, co-financing arrangements, etc.

- Inter-governmental fora hold the potential to improve the working of multi-order systems with relatively low transaction costs by reaching executive/legislative agreements. However, to ensure the durability and wider political acceptance of such compacts, especially those on issues of constitutional significance, such compacts must be subjected to ratification by concerned legislatures and also be open to review.
- Some mutually dependent conditions can facilitate an effective dialogue among levels of government: simplicity of information and feedback, transparency of rules; transversal engagement, credibility, ownership.
- Countries with well-developed co-ordination arrangements, such as inter-governmental committees and regular formal meetings, have a comparative advantage for the introduction and implementation of reforms (OECD, 2017_[19]; 2013_[21]).

What are examples of good practices?

Federal countries

- In Australia, the Council of Australian Governments (COAG), established in 1992, is the peak intergovernmental forum with representation from all orders of government. The role of COAG is to initiate, develop and monitor the implementation of policy reforms that are of national significance and which require co-operative action by Australian governments (for example, health, education and training, Indigenous reform, early childhood development, housing, microeconomic reform, climate change and energy, water reform and natural disaster arrangements). Issues may arise from: ministerial council deliberations; international treaties, which affect the states and territories; or major initiatives of one government (particularly the Australian Government) that affect or require the co-operation of other governments. COAG meets on a needs basis but usually once every quarter. The outcomes of COAG meetings are contained in memoranda released at the end of each meeting. When formal agreements are reached, these may be embodied in intergovernmental agreements.
- In 1971, Austria's Federal Chancellery and the *länder* established the Austrian Conference on Spatial Planning (*Österreichische Raumordnungskonferenz*, ÖROK) as a common platform of spatial planning co-ordination involving all federal ministries, the *länder*, and the umbrella associations of municipalities and social partners. Today, the ÖROK operates as a central network interface for regional policies and the EU's Structural Funds programmes in Austria. Its executive body is chaired by the federal chancellor and includes all federal ministers and state governors, the presidents of the Austrian Union of Towns and the Austrian Union of Communities and the presidents of the social and economic partners as advisors. Decisions are consensus-based. Thematic committees and working groups, formed by senior officials of the territorial authorities and social and

economic partners, were set up at the administrative level to carry out ÖROK's tasks and projects.

- In Germany, an integrated or co-operative model of federalism has been adopted where the federal government has pre-eminence in legislation³ and policymaking, and *länder* governments, in collaboration with local governments, have the responsibility to implement these policies. Executive federalism is therefore of absolute necessity in making federalism work in Germany. Recognising this, Germany has developed a dense inter-governmental network. The chancellor and the leaders of the 16 lander governments, *Ministerpräsidenten*, meet periodically to agree on major issues, such as tax sharing and fiscal equalisation, and the implementation of federal laws. These meetings are supported by the Conferences of the Ministers of Economics and ministers in all functional areas and Meetings of High Officials of relevant ministries. Originally, these meetings were part of the constitutionally mandated process of “joint tasks (ventures)”. The 2006 constitutional reforms eliminated this requirement, but the dense network of formal and informal federal-länder contacts continues to grow due to the integrated nature of German federalism (Lhotta and von Blumenthal, 2010_[23]).

Unitary countries

- In France, territorial strategies are formalised as contractual arrangements across levels of government through state-region planning contracts (*contrat de plan État-région*) that stipulate co-decision and co-financing of interventions.
- In Italy, three separate conferences – state-regions, state and local governments, and state-regions-local governments – serve as the inter-governmental fora.
- Denmark, Finland, Norway and Sweden have regular meetings of central and local governments (through their associations of local governments) to discuss policy and implementation issues. Finland offers financial incentives for inter-municipal co-operation for service delivery.
- In 2015, Portugal established the Council for Territorial Dialogue chaired by the prime minister, and with the representation of central and local governments, in order to facilitate continuing dialogue on important policy and programme issues. Beyond permanent fora of inter-governmental consultation, ad hoc committees and commissions also serve to facilitate intergovernmental and civil society dialogue on some intractable issues.
- The Local Government Commission in New Zealand is an independent, permanent body for inquiry into local reform created by the Local Government Act in 2002 specifically with the aim of building a relationship across party lines in the context of multi-level governance needs (OECD, 2017_[19]).

What are the pitfalls to avoid?

- It is important to avoid multiplying co-ordination mechanisms with no clear role in the decision-making process and with important transaction/opportunity costs.
- An open and transparent system of inter-governmental co-ordination with broad legislative and civil society participation is likely to be expensive, time-consuming and may result in gridlock and/or a “joint decision trap”, while increasing transaction costs for principals (citizens).
- In countries where the upper house of the parliament sees itself as a prime institution of inter-governmental co-ordination (e.g. France and Germany), there may be some political resistance to inter-governmental fora.

What are the recommendations?

- Since most responsibilities are shared, it is crucial to establish governance mechanisms to manage those joint responsibilities. Creating a culture of co-operation and regular communication is crucial for effective multi-level governance and long-term reform success. Such tools for vertical co-ordination include dialogue platforms, fiscal councils, contractual arrangements, standing commissions and inter-governmental consultation boards.
- Formal instruments (e.g. contracts for regional development) are helpful to build trust between parties and provide a long-term perspective.
- It is important to avoid unilateral decisions without consultation as this undermines trust and to find the right balance between top-down and bottom-up approaches.
- Intergovernmental fora (IGF/ILF) have the potential to help clarify, co-ordinate, and develop reform options, joint provision or partnership arrangements for tax, expenditure, revenue sharing and transfers, public services delivery and regulatory policies.
- Inter-governmental for a can be used to facilitate: i) clearer division of powers among various orders of government so that there could be more complete contracts of citizens with each order of government; ii) facilitate greater access to information by citizens, interested sectors of civil society and legislators, enabling them to better hold those agents to account; iii) minimise transaction costs associated with participation, monitoring and decision making, agency costs (i.e. costs incurred by principals and other agents to ensure that agents involved act faithfully in serving their mandates), and uncertainty costs; and iv) create an incentive structure for both the legislative and administrative agents to comply with their compact with the citizens (principals).

Guideline 5. Build adequate co-ordination mechanisms across levels of government			
Checklist	Yes	Partially	No
There are formal institutions of vertical co-ordination among national, regional and local governments. If yes, are these mandated by the: <ul style="list-style-type: none"> • Constitution • National legislation • Executive order? 			
The mandates of these institutions are: <ul style="list-style-type: none"> • Specifically stated • Broadly specified in terms of objectives 			
There are separate institutions of vertical co-ordination for central and line/sectoral ministries? If yes: <ul style="list-style-type: none"> • Are there mechanisms for feedback of sectoral ministries into central agency decision making and vice versa? 			
Are these institutions mandated to meet? <ul style="list-style-type: none"> • On a regular basis • On a need basis only 			
Are agreements reached at these meeting? <ul style="list-style-type: none"> • Disseminated to the public • Monitored for implementation compliance 			
Are the following tools used for facilitating vertical co-ordination? <ul style="list-style-type: none"> • Conditional transfers • Partnership agreements • Formal contracts • National and regional directives • Monitoring using indicators for service outcomes • <i>Ex ante</i> and <i>ex post</i> analysis 			
Does central government have the capacity to set guidelines, monitor the outcomes and alter policies if problems occur?			
Is higher-level government actively engaged in the co-ordination institutions?			

Guideline 6: Support cross-jurisdictional co-operation

Definition

- Cross-jurisdictional co-ordination can take a variety of forms, with the appropriate approach depending on the characteristics of the locality or region as well as the policy objectives and investment(s) being considered. At one end of the spectrum are integration arrangements, such as municipal or regional mergers, which can include the creation of a metropolitan government by merging multiple municipalities. However, economies of scale and thus “optimal size” can vary by investment, such as in transport, education and sanitation. Decisions to merge should be based on a comprehensive assessment of a variety of factors, not only particular investments.
- More flexible co-ordination arrangements may be best suited to achieving policy goals or to making the most of particular investments. These include establishing joint authorities, co-ordinated investment strategies, polycentric co-operation in urban areas, rural-urban partnerships, trans-border co-operation and platforms for cross-jurisdictional dialogue and co-operation
- It is essential to encourage subnational horizontal co-ordination for effective public service delivery and investment in the presence of positive spillovers, to increase efficiency through economies of scale, and to enhance synergies among policies of neighbouring (or otherwise linked) jurisdictions.
- Co-operation is important for physical infrastructure provision where the efficient scale often exceeds the boundaries of individual regions or localities, and for investments in human capital development and innovation where administrative and functional boundaries may not coincide. Horizontal co-operation is important also for subnational public service delivery, especially in the case of small subnational governments with limited resources.
- The central government has an important role in making sure that major externalities are internalised, and that services are provided at an adequate scale. The central government can encourage voluntary horizontal co-operation with a transfer system or it can simply target matching grants to specific projects to ensure efficient scale of local public investments or service provision. Subnational governments may also have an incentive to co-operate without central government intervention, especially if subnational governments fund a major share of service provision from own source revenues and if services are steered with strong normative regulations. To keep costs in control, subnational governments can actively seek co-operative arrangements.
- Rural-urban partnerships are a form of co-operation in functional areas. The partnerships cover a territory with rural and urban areas connected by one or more functional linkages (e.g. value chains, commuting, natural resources, etc.). These linkages form the basis for a co-operative partnership, which in turn manages these linkages for different possible purposes (e.g. supply chains, territorial branding, service delivery, environment protection, etc.). Benefits include the production of public goods, accounting for negative

externalities, achieving greater economies of scale, overcoming co-ordination failures and strengthening capacity.

What are the key trends/data?

- As a result of merger reforms, the number of municipalities and regions has been declining in many countries. Merger reforms usually also decrease inter-municipal or inter-regional co-operation because the size of subnational government units is increasing and so the need for co-operation is decreasing. During the past decades, municipal merger reforms have been carried out, for instance, in Denmark, Finland, Ireland, Japan, the Netherlands and Sweden.
- In parallel, reforms enhancing co-operation between subnational government units are increasingly popular in many countries, including Italy, Poland and the United Kingdom. The reforms apply not only to municipal levels but also to intermediate levels, such as in Italy.
- The number of metropolitan governance authorities has increased during the past decades. Often, the aim has been to find governance solutions that would better take into account the evolved functional areas in metropolitan regions, i.e. the mismatch between existing administrative borders and current activities in the metropolitan areas.
- Yet another trend is regionalisation, resulting in the creation (or strengthening) of an autonomous regional level and up-scaling of existing regions and/or their institutional reinforcement. Regionalisation reforms have been carried out for instance in France, Greece, the Netherlands, Spain, Sweden and the UK.

Rationale and benefits

- Inter-municipal co-operation allows municipalities to internalise externalities in the management of the services and to benefit from economies of scale for utility services (e.g. water, waste, energy), transport infrastructure and telecommunication. Services may be shared as well: back office and administrative functions (e.g. payroll, finance, compliance and control activities, etc.), telecommunications and information technology, environmental services and parks maintenance, joint procurement, frontline services such as customer services, etc.
- At the same time, inter-municipal co-operation allows municipalities to retain their identity and those functions that either do not require a larger scale of production or do not affect neighbouring municipalities.
- One important motivation behind the abovementioned reforms has been the financial crisis, which has put pressure on governments to find ways to improve territorial structure and to find efficiency gains through economy of scales. The reforms also target reducing municipal fragmentation.
- Inter-municipal co-operation allows local governments to invest at the right scale, leads to better and more diverse local services and improved processing times, supports the adoption of innovative, high-tech and specialised services (e.g. through the application of shared technologies) and finally leads to improvements in staff performance and access to expertise,

especially in remote locations that experience skills shortages. Shared services arrangements are well-developed in countries such as Australia, Ireland, New Zealand and the United Kingdom. France is the only OECD country that has given own-source taxing power to inter-municipal entities.

What are examples of good practices?

- Inter-municipal co-operation arrangements are well developed in the OECD and also extremely diverse, varying in the degree of co-operation, from the softest (single or multi-purpose co-operative agreements) to the strongest form of integration (supra-municipal authorities with delegated functions and even taxing powers). Other shared services arrangements are common in countries such as Australia, Ireland, New Zealand and the United Kingdom.
- In addition, it often happens that one municipality adheres to several inter-municipal groupings, and the size of these groupings may vary from two to dozens of municipalities, covering regional scales.

Federal countries

- Institutions of horizontal co-ordination serve as a check on federal powers and are fast becoming an important institution of horizontal co-operation in most federal countries.
- In 2006, the Australian States established the Council of the Australian Federation (COAF) for horizontal co-ordination among states, harmonisation of policies and influencing national policies (Philimore, 2010^[24]).
- In Canada, the Council of the Federation comprising provincial and territorial premiers was established in 2003. It formalised the Annual Premiers Conferences (APC) that had previously served as an informal venue for horizontal co-ordination. The APC aims to develop and present common Provincial/Territorial positions in their dealings with the federal government, and to facilitate collaboration between Provinces and Territories in their own areas of jurisdiction.
- Germany has a long tradition of inter-*länder* co-ordination to achieve “uniform” (now “equivalent”) living conditions in areas of exclusive *länder* competency and to have *länder* inputs in European Union policymaking. These consultations take place through the Conferences of Lander Ministers, which are held regularly and also attended by federal ministers as observers. There are regular meetings of officials and experts to learn from each other’s experiences.

Unitary countries

- Several countries use grants and other financial incentives to encourage horizontal partnership in service delivery. In France, inter-municipal co-operative units can also have their own sources of tax revenue. Local government co-operation and issue/task specific committees serve important channels of horizontal co-ordination.
- In Finland, the single-tier subnational government level is formed by 320 municipalities. Finnish municipalities are often too small to provide

health, secondary education or social services by themselves. Therefore, voluntary inter-municipal co-operation is very common. The most common way to organise co-operation is the joint municipal authority, which is a legal entity, financed by member municipalities and led by a board assigned by member municipalities. Joint municipal authorities are not subject to central government transfers. While in general inter-municipal co-operation is voluntary, municipalities are obliged to form a joint municipal authority for specialised healthcare (hospitals) and regional planning. Although in recent years there have been voluntary municipal merger reforms, inter-municipal co-operation is still common as it has enabled utilising economies of scale especially in rural and sparsely populated areas. Inter-municipal co-operation has allowed municipalities to focus on tasks that best suit their capacities. In recent years, the trend has been to form even larger co-operative units, which are able to integrate all health and social services in order to utilise both economies of scale and scope. Some municipalities have also outsourced health and social service production to private companies with long-term contracts.

What are the pitfalls to avoid/risks?

- Co-ordination does not come without costs. Encouraging inter-municipal or inter-regional co-operation and municipal mergers with cash transfers or other financial incentives can be expensive and lead to inefficient structures without thoughtful planning of measures.
- Inter-municipal or inter-regional co-operation may lead to a democratic deficit if the decision-makers of co-operative organisations are nominated by the member organisations instead of elected by the local resident. Such governance models can be unclear for citizens and lead to accountability problems especially if the decision-makers are self-interested.
- Comprehensive metropolitan governance models can be politically and administratively hard to achieve. As a result, metropolitan governance may be limited to certain core competencies. This can lead to organisational and administrative silos, which can be hard to govern efficiently.

What are the recommendations?

- Horizontal co-ordination can be carried out using specific matching grants, with inter-municipal and inter-regional co-operation, or mergers of subnational government units. The legal system should allow such tools.
- Co-ordination measures should be based on high-quality information on externalities, economies of scale, local democracy aspects and efficiency differences in service delivery. Information used in decision-making should be based on research and databases that describe subnational government service production from coverage, quality and efficiency aspects.
- Voluntary co-operation and mergers could be encouraged with temporary grants that cover part of the cost for setting up such arrangements. The main incentive for co-operation and mergers should be the expected efficiency improvement and better quality of services, not the financial support from the higher level of government.

- If a forced merger or co-operation reforms are adopted, decisions should be based on a national reform plan of subnational government structure. The resulting multi-level structure should support the overall fiscal policy targets.
- Matching rates should be based on the size of externalities. Too high a matching rate can easily lead to overspending. Low matching rates will benefit only the wealthiest subnational governments, especially if the revenue equalisation system is weak or non-existent.
- In all cases, formal and informal negotiation frameworks should be established for continuous dialogue between subnational and central government representatives. The dialogue should be arranged periodically to discuss the service level and quality targets, subnational government financing, and current and planned reforms. Systematic negotiations between the central government and subnational governments help promote co-operative arrangements and enable more co-ordinated actions.
- Rural-urban partnerships should be promoted as a form of cross-jurisdictional collaboration to enhance inclusive growth by bringing multiple benefits, such as expanding the benefits of agglomeration economies, to overcome co-ordination failures and strengthen capacity.

Guideline 6. Support cross-jurisdictional co-operation			
Checklist	Yes	Partially	No
There are formal institutions of horizontal co-ordination: ● Among regions ● Among local/municipal governments			
There are formal mechanisms or incentives to encourage co-ordinated response. If so, by: ● Regions ● Municipalities ● Municipality and its stakeholders (private for profit, non-profit, etc.)			
The legal system allows co-operation and mergers between subnational governments			
There is readily available information of externalities and economies of scale in subnational government service provision and investments			
There is a national reform plan of optimal subnational government structure, and horizontal co-ordination is based on such plan			
Functional regions are identified and used in investment policy			
There are publicly available indicators on public service production, service coverage, needs, quality and efficiency			
There is a nationwide plan for metropolitan policy, based on functional areas			
There are regional and national dialogue frameworks in place for metropolitan area development			
Urban-rural partnerships are enabled			
Financial support and incentives are established for planning and executing reforms on metropolitan governance			
Systems are transparent and rules are clearly communicated to citizens			
Co-operative bodies are led by decision-makers who are elected by local residents or they are otherwise made responsible to residents they serve			
Efficiency benchmarking is carried out periodically and data of such analysis is openly available			

Guideline 7: Strengthen innovative and experimental governance, and promote citizen engagement

Definition

- Participatory governance (at the subnational level) refers to approaches to local public governance that facilitate the participation and engagement of private citizens and other stakeholders (e.g. private for-profit, private non-profit, interest-based or hope/faith-based networks, self-help groups, etc.) in deliberations on public policy choices and the delivery of local public services in partnership or in competition with the formal public sector.
- There is a diverse range of approaches to building participatory governance. These include a focus on transparency, for example using open government methods such as open and competitive procurement, performance budgeting, maximum disclosure, citizens right to know, and citizen-centric or participatory governance, using such tools as participatory planning and budgeting, civil society performance monitoring, social audits, direct democracy provisions (e.g. referenda on major initiatives/projects, recall of officials for dereliction of duty). Innovations in accountable and responsive governance is another mechanism and can promote local government as a facilitator of network governance to improve economic and social outcomes. Client/citizen charters and new public management approaches are another means to support participation through result-based management to government accountability, e-government/ information and communications technology (ICT) innovations, and pilot projects with a potential for regional or nationwide replication to improve service delivery.

What are the key trends/data?

- Overall, local governments around the world are often the leaders in innovations that aim to ensure government works better, costs less and is more responsive and accountable to local residents.
- Subnational governments strive to introduce experiments that aim to inform and engage citizens, such as performance budgeting and open government initiatives. These are undertaken by some US local governments. Participatory planning and budgeting, initially as introduced by local governments in Brazil and a few other Latin American countries as well as the Republic of South Africa, have now extended to many other parts of the world. Other examples include social audits and citizen scorecards as used in India, direct democracy provisions as practised in Switzerland and the United States, innovations in internal and external government accountability such as the results-based management and competitive provision of local public services in New Zealand, and local government as a facilitator of network governance as practised in Vancouver, British Columbia, Canada.
- Empirical evidence on the impact of citizen engagement on local governance is scant. Broader citizen engagement in local government affairs remains an unmet challenge even in OECD countries.
- Recent innovations in local public governance aim to engage residents in all aspects and phases of local government operations from ideas to policy to

implementation. By doing so, they are building people's trust in local government while improving integrity, efficiency and equity of local government operations. This enhanced trust contributes to greater public support and improved finances for local government core business as well as for new initiatives. These innovations also broaden citizen voice, choice and exit options and thereby introduce strong incentives for local governments to strive for better performance in service delivery.

- Participatory planning and budgeting offer citizens at large an opportunity to learn about government operations and to deliberate, debate, and influence the allocation of public resources. It is a tool for educating, engaging and empowering citizens and strengthening demand for good governance. Participatory budgeting has the potential to strengthen inclusive governance by giving marginalised and excluded groups the opportunity to have their voices heard and to influence public decision-making vital to their interests. Done right, it has the potential to make governments more responsive to citizen needs and preferences and more accountable to them for performance in resource allocation and service delivery.
- The use of data that accumulates from public services provided by subnational governments is currently a hot topic in many countries. As a result of the rapid digitalisation of public services, the need to solve issues of data sharing, analysis, and privacy protection in public services is urgent. Solutions that help abolish vertical silos in public administrations and enhance co-operation among jurisdictions and levels of government are currently being sought. These solutions include facilitating the use of linked data and creating a shared view of data and information, including open data, within and across levels of governments (OECD, 2017^[25]). All of this should help governments prioritise the adoption of an overall sharing strategy to co-ordinate efforts. Open data also enables public access to information and can promote more direct involvement in decision-making.

What are examples of good practices?

Federal countries

- Australian local governments collaborate on using common smart forms for local applications, common ICT platforms for tracking enquiries/transactions, measuring service delivery response times and surveying customers, set benchmarks for performance and measuring and reporting results (ALGA, 2010^[26]). Australia's "Value Creation Workshops" are valuable resources for strengthening local government officials' capacity to engage citizens through training and access to relevant expertise.
- In Brazil, the experiment carried out in the city of Porto Allegre represents one of the earliest and most successful trials in participatory planning and budgeting. This experiment is widely recognised for its positive impact on citizen engagement and improved service delivery, especially to the poor.
- In Canada, in the 1990s, Metropolitan Vancouver government took the lead in facilitating network governance by bringing together all relevant stakeholders (i.e. private sector, civil society organisations, provincial and

federal governments) to form a partnership to overcome urban blight and to combat drug use and other crimes in the inner city. The metropolitan government co-ordinated and supervised the activities of all partners and successfully transformed the inner city into a safe, clean and a thriving work and residential environment. Several cities in Canada produce annual performance reports on their fiscal, financial and service delivery performance. A number of Canadian (and Finnish) municipalities also measure residents' expectations, priorities and degrees of satisfaction with local services in order to improve service delivery (OECD, 2017^[7]).

- Switzerland is the ultimate champion of citizen empowerment through direct democracy provisions in the constitution. Citizens with appropriate majorities in referenda can overturn legislation and have the right to be consulted through referenda on major projects, deficits and debt levels, and significant changes in tax burdens.
- In the United States, the concept of performance budgeting owes its origins to US local government innovations to enhance the transparency of their operations and showcase (benchmark) their performance as a means to demonstrate that local tax dollars advancing the local public interest. Direct democracy provisions on citizen-based initiatives concerning local taxing, spending and borrowing and the recall of local public officials also help in enhancing local government accountability to local residents. Local governments in Canada and the US have also adopted the single phone number 311 as a one-stop access point for all local services.

Unitary countries

- In recent years, Chile has followed a multi-faceted approach to promote transparency and citizen engagement in public processes. These include strengthening institutional frameworks for the citizens right to know. It has also promoted civic participation with mandatory requirements for establishing a municipal advisory council of civil society organisations (*Consejo Comunal de Organizaciones de la Sociedad Civil*, COSOC) for citizen engagement and to provide civic education.
- Finland's local governments engage citizens through a variety of fora to seek inputs on service delivery improvements.
- New Zealand pioneered results-based accountability of government through contract-based public employment and management. Public managers have full flexibility in input choices and delivery mechanisms but are held accountable for performance against contract expectations.
- The UK innovation foundation, NESTA, is one of the most prominent pioneers of public and social labs as a means of addressing societal challenges through evidence-based local experiments.

What are the pitfalls to avoid/risks?

- Participatory processes also come with risks. They can mask the undemocratic, exclusive or elite nature of public decision making, giving the

appearance of broader participation and inclusive governance while using public funds to advance the interests of powerful local elites.

- Participatory budgeting can be abused to facilitate an illegitimate and unjust exercise of power. To prevent these abuses, the participatory process must fully recognise local politics and formal and informal power relations, so that the processes yield outcomes desired by the median voter.
- Another risk is “fatigue” on the part of the citizen, especially when they are consulted or when they are engaged but do not see related or associated results or outputs, or when their input has not been fully taken into consideration. This is more likely to happen when participatory approaches become box-ticking exercises rather than undertaken as a strategic input to decision making. There is a balance that needs to be struck.
- Participatory approaches at the local level must be guided by local councils. As elected bodies, local councils voice citizen choices and preferences and provide oversight on behalf of the voters. Approaches that by-pass local councils may risk weakening democratic governance and accountability at the local level.

What are the recommendations?

- Citizens should be empowered through the right to know and benefit from direct democracy provisions. Care must be taken if imposing participation requirements through legal and regulatory frameworks as such requirements could impose significant costs but may elicit pro forma responses by local governments and citizens.
- Ensure that elected local councils have the ownership and control of citizen participation and engagement initiatives.
- Complement transparency provisions with governmental systems that create incentives for citizens-based accountability, e.g. output based grants for merit services where citizen voice, choice and exit options have a direct impact on the grant amount received by a provider.
- Higher-order government should consider encouraging citizen engagement and innovative and competitive service delivery through tournament-based output grants and recognition awards.
- Use ICT/e-government tools for better service delivery. ICT tools can help government to better understand who the service users are and to learn about their needs. Integrate ICT infrastructure, skills and services and systems and processes to create a connected government for efficient and effective service delivery. Pick pilot projects that can show quick results. Choose the right services to transform using ICT and the best delivery channels. Collaborate with other governments and delivery partners. Use ICT to measure, monitor and disseminate own performance.

Guideline 7. Strengthen innovative and experimental governance, and promote citizens' engagement			
Checklist	Yes	Partially	No
Some subnational governments practice participatory budgeting If yes, the process impacts budget priorities and allocation			
The subnational government uses ICT/e-government tools for: <ul style="list-style-type: none"> • Measuring and monitoring performance • Reporting on performance • Improving access, efficiency and quality of public services • Enhancing citizens engagement 			
The subnational government strengthens citizen voice, choice and exit options though: <ul style="list-style-type: none"> • Citizens' charter • Service standards • Annual performance report • External performance audits • All decisions including procurement, costs of concessions posted on the web • Citizens friendly output budgets and service delivery performance report • Open public hearing 			
Subnational governments engage citizens for: <ul style="list-style-type: none"> • Consensus building dialogues and conferences • Deliberative mapping of policy and program options • Deliberative polling on issues • Deliberative (focus groups) meetings on public policy issues • Uses electronic/digital media for engagement • Meetings on vision for the future or to discuss a specific theme • Participatory appraisal • Participatory strategic planning • Service users' panels for service evaluations • Youth empowerment • Convene a citizens' jury/panel to consult or to pass judgement on local services • Form and convene networks of local beyond government service providers 			

Guideline 8: Allow for and make the most of asymmetric decentralisation arrangements

Definition

- Asymmetric decentralisation refers to the fact that the political, administrative and fiscal arrangements across jurisdictions (i.e. at the same government level) may differ. It can apply to both federal and unitary countries. Political asymmetric decentralisation refers to situations where some subnational governments are given political self-rule that deviates from the norm or average assignment. In administrative terms, asymmetric decentralisation means that the devolved responsibilities might differ across jurisdictions. In fiscal terms, asymmetric federalism or decentralisation means that subnational government units at the same level have different revenue powers. Asymmetric decentralisation might occur at the regional level (state, province, *länder*), the metropolitan level and the local level.

What are the key trends/data?

- Territorial disparities are high and persistent within OECD countries and have been rising across urban and rural areas in a number of countries. Such disparities tend to be higher in developing countries.
- Trends in asymmetric decentralisation are changing: whereas between the 1950s and the 1970s asymmetric arrangements mostly occurred at a regional level, the present trend seems to apply asymmetric decentralisation in major urban areas. Capital city districts, in particular, have experienced a growth in asymmetric decentralisation arrangements, perhaps because the benefits of urbanisation and agglomeration economies have become more widely understood and accepted. As a result, the number of metropolitan governance authorities has increased during the past decades. Currently, around two-thirds of the metropolitan areas in the OECD have a metropolitan governance body.
- In 1950, around half of the 81 countries covered by the Regional Authority Index (RAI) had some kind of differentiated governance at the regional level. In 2010, almost two-thirds of the countries in the RAI had implemented asymmetric arrangements in some form.
- Asymmetry is often a basic characteristic of the federal countries. There are, however, different gradients of asymmetry: some federal countries are quite asymmetric (Canada and Spain, for example) whereas others are more symmetric (Australia, Austria, Germany, Switzerland and the United States). However, even the most “symmetric federations” have elements of asymmetry.
- Asymmetric decentralisation is increasing in unitary countries. There is thus a greater convergence between unitary and federal countries in the trend toward greater differentiated governance at the subnational level.

Rationale and benefits

- Subnational governments vary greatly in scale and capacities within countries. Subnational governments with low population levels may suffer from inadequate economies of scale, depending on their ability to co-operate and outsource; and sometimes on limited fiscal and administrative capacities.
- Given the important differences across subnational governments in fiscal, institutional and human resource capacities, a “one size fits all” approach is not necessarily the most appropriate way to organise decentralisation policies and multi-level governance systems.
- The age structure and service needs of the population may vary greatly between regions within a country. In some cases, there are important ethnic or political differences between regions. These are just a few examples of circumstances that challenge the ability of governments to maintain the unity and balanced development of the state.
- Asymmetric decentralisation may be politically motivated. There may be historic, cultural and/or ethnic reasons for the special treatment of some regions or subnational governments. The aim can be to safeguard the unity of a nation-state. It may also be motivated by economic issues, or to address efficiency considerations. In addition, the motive can be to address heterogeneity in the capacity levels of subnational governments. The economic motives for asymmetry are usually linked with efficiency considerations.

What are examples of good practices?

Federal countries

- In Canada, asymmetric decentralisation is mostly based on “menu federalism”, where the “opt in” or “opt out” choices are made available to all provinces. The province of Quebec has been using this option more frequently than the other provinces.

Quasi-federal countries

- In South Africa, several classifications are used to group the 278 municipalities. The different classification methodologies recognise that municipalities need differentiated approaches that take into consideration their different characteristics and needs. However, the South African Financial and Fiscal Commission has argued that differentiation approach is not always clear, and some classifications are not always useful for making decisions or allocating resources (Financial and Fiscal Commission of South Africa, 2012^[27])

Unitary countries

- In the Czech Republic, in the process of decentralisation, the responsibilities of the 76 abolished state “districts” were largely passed on to 205 “municipalities with extended powers” in 2003. These municipalities perform central government delegated functions such as child protection and issuing

passports on behalf of smaller surrounding municipalities. These functions are associated with additional funding. Smaller municipalities can also delegate additional functions to the municipalities with extended powers (ORP) that they do not want to provide, or cannot provide because of their lack of capacities (OECD, 2017^[7]).

- In Denmark, between 2012 and 2015, nine local municipalities were granted exemptions from government rules and documentation requirements in order to test new ways of carrying out their tasks, in a policy experiment known as the “Free Municipality” initiative. The main focus has been on simplification, innovation, quality and a more inclusive approach to the individual citizen, with many of the experiments focusing on employment. The Free Municipality experiment is being evaluated, in order to form the basis for potential future legislation on de-bureaucratisation for all municipalities. The concept of Free Municipalities continues in an adjusted form until 2019 and is being extended to more municipalities (OECD, 2017^[19]).
- In Italy, a 2014 reform ended two decades of gridlock over metropolitan governance reform and created the legal structure for the introduction of differentiated governance in ten major metropolitan areas – Bari, Bologna, Florence, Genoa, Milan, Naples, Reggio Calabria, Rome, Turin and Venice – and four additional cities in special regions: Catania, Messina and Palermo in Sicily, as well as Cagliari in Sardinia.
- In Sweden, the counties themselves gradually and voluntarily implemented regional reform since 1990s. This resulted in asymmetric and bottom-up regionalisation as a gradual and experimental process (a laboratory of regionalisation). The voluntary reform eventually led into decision to extend the reform to cover all Swedish counties since beginning of 2019. The underlying idea is that decentralised policymaking leads to more innovation in governance.

What are the pitfalls to avoid/risks?

- Putting in place a very complex differentiated system, which is not transparent and clear for citizens, can risk blurring accountability lines and raising the co-ordination costs of multi-level governance.
- Increasing disparities in capacity across regions, if adequate equalisation systems and capacity-building policies are not put in place.
- Not reaching national goals for universal service levels and quality standards in a very heterogeneous service provision system.
- Not monitoring the outcomes of asymmetric decentralisation, thus not allowing adjustments in the system.
- Questioning national unity.

What are the recommendations?

- Asymmetric decentralisation should be part of a broader strategy of multi-level governance and territorial development. Asymmetric decentralisation is not an end in itself, it is a means to achieve multi-level governance goals.

- Asymmetric decentralisation should be supported by effective vertical and horizontal co-ordination mechanisms.
- Asymmetric decentralisation needs to go hand in hand with an effective equalisation system.
- The type of asymmetric decentralisation should be well defined (political, administrative/management or/and fiscal) and have a clear rationale as the objectives and instruments will differ in each case.
- The scale and scope should be clear (large part of the territory vs. restricted, regional, metropolitan, local levels; permanent vs. transitory, timing, pilot/experimental).
- The way asymmetric responsibilities are allocated should be explicit, mutually understood and clear for all actors.
- An asymmetric decentralisation approach should be based on dialogue, transparency and agreements between all main stakeholders.
- To the extent possible, participation in an asymmetric arrangement should remain voluntary. The central government or a higher level of subnational government can take responsibility for service provision in non-participant areas.
- A variety of incentives (not just financial) should be used to foster participation in voluntary schemes or pilot experiences.
- A well-defined and transparent approval system for prospective participating subnational governments should be in place.
- The effects of asymmetric decentralisation should be carefully monitored on a regular basis and the results of such evaluations should be used to revise the plans if needed (including the effects on equity and national cohesion).
- A system for communicating good practices and lessons learned from the asymmetric arrangements should be organised.
- It is important to keep a rational number of asymmetric arrangements within the same country to limit co-ordination costs and complexity.

Guideline 8. Allow and make the most of asymmetric decentralisation arrangements

Checklist	Yes	Partially	No
The type of asymmetric decentralisation is well defined (administrative, fiscal, political)			
The scale of asymmetric decentralisation is clear (regional, metropolitan, local levels)			
The number and types of asymmetric arrangements/instruments remain limited			
The way delegated responsibilities are allocated to specific subnational governments is clear and explicit			
There are vertical co-ordination mechanisms in place			
There are horizontal co-ordination mechanisms in place			
An equalisation system is in place			
There are incentives to foster the participation subnational governments (SNGs) in asymmetric arrangements schemes			
The participation of SNGs in asymmetric arrangements schemes remains voluntary			
There is a well-defined and transparent approval system for prospective subnational governments			

Guideline 9: Consistently improve transparency, enhance data collection and strengthen performance monitoring

Definition

- Transparency can be defined as openness to the general public with respect to a comprehensive and detailed view of government structures, processes, finances, operations, net worth and results. It involves ready public access to reliable, timely and easily comprehensible information that could be used to evaluate openness and inclusivity of government processes of decision-making. Moreover, freely available information enables performance measurements and benchmarking between governments and their agencies and entities.
- Data collection refers to the capacity of government entities to collect and disseminate information on their operations.
- Performance monitoring refers to the ability of citizens, higher-order governments, private sector and other interested parties to know what government entities are doing and how well they are performing their tasks.

What are the key trends/data?

- Government transparency in general, and fiscal transparency in particular has been on the rise due to the impact of the information revolution and globalisation.
- Subnational government transparency is also on the rise. This is because local governments are increasingly aiming for greater transparency by introducing performance-based budgeting and participatory budgeting techniques and making pro-active efforts to engage citizens in local government policymaking. Budgeting transparency throughout the investment cycle provides visibility to investments, clarifies recurrent budgetary implications and strengthens public accountability.
- Other recent initiatives to strengthen transparency include the Transparency and Accountability Initiative (TAI), which offers a forum for sharing information on innovative initiatives to improve transparency and accountability. Meanwhile, Publish What You Pay (PWUP) advocates the disclosure of contracts, revenue payments and receipts for extractive industries.

Rationale and benefits

- Transparency is critical to building trust in public policies as well as among citizens. Empirical evidence further suggests that transparency contributes to improved social and economic outcomes and reduced corruption (Ortiz-Ospina and Roser, 2017^[28]; Acosta, 2013^[29]; Hameed, 2005^[30]). A survey of the past 25 years of empirical evidence suggests that transparency has a positive impact on legitimacy, citizen participation, trust in government, citizen satisfaction, government accountability, and can result in less corruption, better performance and better public financial management (Cucciniello, Porumbescu and Grimmelikhuijsen, 2016^[31]). Greater fiscal

transparency is also shown to improve sovereign credit ratings and lower borrowing costs. It contributes to citizen empowerment and leads to efficient and equitable use of government resources due to heightened citizens-based accountability. Transparency enhances voice and exit options for citizens.

What are examples of good practices?

Federal countries

- Australia is well recognised for how it disseminates timely, reliable, accurate, meaningful and understandable, comprehensive information on public decision-making processes and procedures, as well as government performance, including on its impact and outcomes.
- Canadian subnational governments pro-actively seek citizen participation and engagement in their policymaking and operations.
- Brazil's landmark Fiscal Responsibility Law 2000 further strengthened the fiscal transparency and accountability of Brazilian governments by introducing hard fiscal rules and empowering citizens to sue governments for any observed breach of the provisions of this law.
- In the United States, local governments pioneered approaches to open government and performance budgeting to earn the trust of the people.

Unitary countries

- Italy has always placed great attention on the construction and use of indicator systems, to monitor programme implementation (financial and output indicators), to support policymaking processes and to analyse policy results (statistical indicators). Throughout the programming cycle, significant financial and organisational resources have been devoted, on the one hand, to the construction and updating of a national monitoring system (using an open data approach <https://opencoesione.gov.it/en/>) and, on the other, to the availability of timely and territorial disaggregated statistical data for all policy areas relevant for regional development (available on the national statistical office website <https://www.istat.it/it/archivio/16777>).
- New Zealand is a good example of transparency in governance and government accountability for results in view of the results-based management framework it adopted in the 1980s for internal and external accountability of government. It outperforms all countries in the public access to information on government decision-making processes and makes available detailed information on a results-based chain (programme objectives, programmes, activities, inputs, outputs, outcomes, impact and the reach) of all government operations.
- Norway has implemented KOSTRA, a comprehensive system in monitoring and disseminating information on government operations and performance. KOSTRA system is considered a leading good practice in government transparency.

What are the pitfalls to avoid/risks?

- It is essential to avoid a complex information dump. The reporting of information must be user-friendly, otherwise, it will not advance public access to information.
- Time is of the essence. Information that is made available after long delays would not be useful in reviewing current operations.
- Information must be comprehensive and give a complete and accurate picture of government operations. Typically, such comprehensive information is not available in most developing countries. Information gaps often include development assistance, the local government sector as a whole, state-owned enterprises, tax expenditures, contingent liabilities, quasi and extra-budgetary operations, natural resource revenue management.
- Information must be contextual (linked to policy and outcomes), hierarchical (organised by orders of government and hierarchy in each order), and easily related to governmental units. Information that does not relate to governmental units is not valuable for oversight and accountability.
- The integrity of the information must be assured. Lack of integrity contributes to citizen mistrust in government.
- For local governments, complex ad hoc and add-on self-standing monitoring and evaluation systems are costlier and less useful than built-in tools and mechanisms for government transparency, self-evaluation and citizen-based accountability, such as local government output budgeting and output based fiscal transfers to finance local services.

What are the recommendations?

- National governments should develop performance-monitoring systems to monitor decentralisation and regional development policies. These systems need to remain simple with a reasonable number of requirements/indicators.
- Subnational governments need to be subjected to higher-level regulations and fiscal rules to ensure fiscal discipline and fiscal sustainability. These typically include compliance with the laws and reporting requirements for financial flows, assets and liabilities.
- Higher-level governments may impose a reporting requirement for service delivery performance in critical services. Higher order governments must also regularly monitor subnational government performance in critical service areas based on a minimum set of standardised indicators, provide timely feedback, and benchmark local performance in service delivery, allowing for comparison and learning.
- Higher-order governments must regularly monitor and provide timely feedback on the fiscal health of subnational governments.
- Higher-order government oversight must be based on normal subnational government systems (e.g. fiscal transparency requirements, quarterly audited, financial statements, output based budgeting, output based transfers, etc.) rather than imposing formal add-on and ad hoc monitoring systems.

- Subnational governments need to be encouraged to adopt pro-active policies for information disclosure, and to seek citizen engagement for all operations.
- Setting up independent evaluation institutions can be beneficial for policy credibility, trust and enforcement, and may help increase the uptake of monitoring and evaluation results.

Guideline 9. Consistently improve transparency, enhance data collection and strengthen performance monitoring

Checklist	Yes	Partially	No
Subnational governments publish timely data on key performance indicators for its major public services			
Subnational governments maintain an open website to register complaints			
Subnational governments pro-actively disseminate performance information and seeks citizens' feedback			
The freedom of information legislation is guided by the principle of maximum disclosure – all information is accessible subject only to a narrow set of exceptions			
The principle of maximum disclosure takes precedence in the event of conflict with other legislation			
Exceptions are clearly and narrowly defined			
Public entities are required to publish key information needed to assess integrity, efficiency and equity of their operations			
Requests for information are processed rapidly within defined time frame			
The costs of requesting information are reasonable and affordable by an average citizen			
Meetings of government entities are open to public and media			
Individuals who release information on abuse of public office or other malfeasance are protected			
Subnational government performance indicators are used			
Subnational governments work through competitive provision, results-based management and benchmarking			

Guideline 10: Strengthen national regional development policies and equalisation systems

Definition

- National regional development policies are essential to reduce territorial disparities and strengthen urban-rural linkages, as mega-trends have an asymmetric impact on regions and cities within countries, and tend to increase disparities.
- In most countries, regional governments have varying fiscal capacities and varying fiscal needs and therefore varying ability to provide local public services.
- Equalisation transfers are used to reduce fiscal disparities between central government and subnational government (a vertical fiscal gap) and between subnational governments (a horizontal fiscal gap). The purpose of fiscal equalisation is to enable subnational levels of government to provide approximately comparable levels of public services at comparable tax burdens.
- Regional and local fiscal equalisation could be administered through vertical federal and/or state programmes (in federal countries) or a central programme (in unitary countries). It can also be administered through two types of horizontal programmes (inter-regional or inter-local equalisation) where wealthy regional/local governments contribute to the pool and fiscally poor regional/local governments receive a subsidy from this pool according to a defined equalisation standard.
- Under a “Robin Hood” horizontal equalisation programme, the state or the central government collects these monies from richer jurisdictions and distributes to the poorer jurisdictions. Under a solidarity programme, the equalisation programme is administered by regional governments themselves.

What are the key trends/data?

- Most OECD countries have national regional development policies in place to support place-based policies, address urban-rural linkages and reduce territorial disparities. Nineteen out of 27 OECD countries surveyed in 2018 report having a national public investment strategy with a territorial dimension (OECD, 2019 forthcoming^[32]).
- Fiscal equalisation is in vogue in most countries, using various mechanisms and yardsticks. Only in a handful of countries does an explicit equalisation standard determine both the pool and individual allocations. Most countries use arbitrary pool and ad hoc fiscal capacity and need factors in determining allocations. Fiscal need calculations are data intensive and especially difficult to do. Countries have adopted second-best approaches to expenditure need determination that vary from cherry picking a few need factors to choose sophisticated quantitative methods to determine significant factors and constructing relative needs/cost disability indexes for various jurisdictions. Experience has shown that complexity in the methodology does not necessarily result in greater fiscal equity.

- Vertical fiscal equalisation programmes have grown in popularity in recent decades and are now practised in a large number of countries. Horizontal fiscal equalisation is in vogue in only a handful of OECD countries, most notably in Germany, the Nordic countries and Poland. The German interstate solidarity (horizontal) equalisation programme is, however, being allowed to expire in 2019.

Rationale and benefits

- Fiscal equalisation transfers are advocated to deal with regional fiscal equity and fiscal efficiency concerns. These transfers are justified on political and economic considerations.
- Large regional/local fiscal disparities can be politically divisive. Equalisation transfers support national/state objectives in creating a common economic and social union. They strengthen a sense of national citizenship among residents of diverse localities. They facilitate decentralised public decision making and local autonomy and enable local governments to deliver a menu of public services consistent with local preferences. Overall, these transfers are seen as a glue that holds the region/state and the country together.
- Public sector interventions that impede the free flow of factors of production within the nation have adverse consequences for the efficiency of the national economy. Most equalisation programmes in vogue are intended to promote such mobility of factors by ensuring reasonably comparable levels of public services at comparable burdens of taxation. Such a level playing field facilitates movement of factors in response to economic stimuli but retards their movements in response to fiscal considerations alone.
- Therefore, such programmes, if properly designed, may enhance fiscal equity (citizens are treated equally by the public sector regardless of their place of residence) and fiscal efficiency (by discouraging fiscally induced migration – mobility of factors in response to differential net fiscal benefits across the nation).
- They can potentially play a positive role in strengthening an internal common market and common economic, social and political union. For these reasons, equalisation is often seen as “the glue that holds a federation together”.
- Care must be exercised in the design of such programmes so that they do not inadvertently contribute perverse incentives that may lead to a misallocation of resources, thereby retarding regional and national economic growth.

What are examples of good practices?

- Better practices in equalisation suggest that for the sustainability of the programme, there must be broad political and societal consensus on the degree of equalisation and the means to finance such transfers. Simplicity, transparency, objectivity and predictability of design should take precedence over precision and sophistication or academic excellence. Furthermore, an explicit equalisation standard must determine both the total pool of funds allocated and the allocation of transfers. For example, the pool and allocation

can be defined using a formula. An arbitrary pool given by a revenue sharing programme is not desirable.

Federal countries

- Equalisation methods differ among countries. For instance, Canada and Germany primarily equalise fiscal capacity with Germany providing an adjustment for population size, density, and whether a city is a harbour. Switzerland devotes 19% of the equalisation pool to cost equalisation, and compensates for infrastructure deficiencies through a supplementary cohesion fund. Australia takes a comprehensive view of both fiscal capacity and expenditure/cost equalisation. In addition, the Australian programme is the only one among mature federations that also equalises for capital expenditure needs and associated capital financing.

Unitary countries

- In Nordic countries, the role of the intermediate order of government is either very limited (i.e. in Denmark, Finland and Norway) or highly constrained (i.e. Sweden). Local governments are mostly self-financing but do receive central assistance for health, education, social welfare and local fiscal equalisation. In general, specific purpose transfers relate directly to demand factors for local public service. Local fiscal capacity equalisation programmes use an explicit standard of equalisation that determines total pool and allocation among local governments. The programme is administered based on either solidarity principles (fiscally wealthy municipalities contribute to the pool and fiscally poorer municipalities receive from the pool in a horizontal equalisation programme). In Denmark, Finland and Sweden, a mixed programme using a central component and Robin Hood components (central government taxes wealthier jurisdictions and transfers these funds to poorer jurisdictions in a vertical equalisation programme) are in place. Norway uses the Robin Hood principle in the financing and allocation of these transfers. Expenditure need equalisation is organised on solidarity principles in Denmark, and Norway uses a solidarity programme plus central grants for smaller local governments, northern counties and faster growing local governments. Finland and Sweden use a central programme of cost equalisation for selected services such as health, education and social services.

What are the pitfalls to avoid/risks?

- Avoid very generous equalisation schemes. Equalisation transfers that are too open-handed may create disincentives for local economic development.
- Equalisation transfers may create incentives for lobbying, inefficiencies and disincentives for improving tax base and amalgamation. They can also create false prices for local public goods. At worst, fiscal equalisation can open a development trap for poorer jurisdictions and even increase long-term disparities.
- Equalisation systems that weaken incentives for inter-regional migration may induce inefficiency in the inter-regional allocation of resources. This happens

if the grants discourage the outmigration of labour to high-income regions where it would be more productive.

- Avoid situations where the transfer system distorts the dependence of own revenues and spending. If the transfer system is allowed to separate taxing and spending decisions, it may also undermine local government accountability to residents.
- Avoid overly complex transfer systems. Complex equalisation systems may have unintended negative consequences through implicitly perverse incentives (e.g. the use of need factors for government employment, incidence of crime, etc.), which may contribute to higher public employment and a reluctance to initiate policies to curb crime, etc.

What are the recommendations

- Fiscal equalisation policies need to be accompanied by pro-active regional development policies to offset the potentially negative incentives of such systems.
- Equalisation arrangements need to be carefully designed to promote the tax and development efforts of subnational governments (OECD, 2007^[33]).
- Policymakers should strive to respect the following principles in designing and implementing intergovernmental transfers:
 - Keep it simple. In the design of fiscal equalisation transfers, rough justice is better than precise or full justice if it achieves wider acceptability and sustainability.
 - Focus on a single objective (equalisation for equalisation transfers) in a grant programme and make the design consistent with that objective. Setting multiple objectives in a single grant programme runs the risk of failing to achieve any of them.
 - Introduce ceilings on equalisation grant funds. Such limits could be linked with macro indicators and floors to ensure stability and predictability of transfer funding.
 - Introduce sunset and stability clauses. It is desirable to have the equalisation grant programme reviewed periodically – say, every five years – and renewed (if appropriate). In the intervening years, no changes to the programme should be made, in order to provide certainty in budgetary programming for all governments.
 - Determine both the total pool of resources used for transfers and allocations in the equalisation formula. Solidarity-based systems are more likely to strike the right balance on an equalisation standard. Paternal and Robin Hood programmes lack internal discipline and could lead to too much or too little redistribution.
 - Equalise per capita fiscal capacity to a specified standard in order to achieve fiscal equalisation separately among various local governments grouped together by size/class and urban/rural distinctions. Such a standard would determine the total pool and allocations among recipient units. Calculations required for fiscal capacity equalisation using a representative tax system for

major tax bases are doable for most countries. Fiscal need equalisation is best achieved through a demand for services approach that allocates funds by service population, e.g. school-age population for school finance. Alternately, fiscal need equalisation can be achieved through output-based sectoral grants that also enhance results-based accountability.

- A national consensus on the standard of equalisation is crucial for the sustainability of any equalisation programme. The equalisation programme must not be looked at in isolation from the broader fiscal system, especially conditional transfers.
- Recognise population size, the area served and the urban/rural nature of services in making grants to local governments. Establish separate formula allocations for each type of municipal or local government.
- Establish “hold harmless” or grandfathering provisions that ensure that all recipient governments receive at least what they received as general-purpose transfers in the pre-reform period. Over time, as the economy grows, such a provision would not delay the phase-in of the full package of reforms.
- Make sure that all stakeholders are heard, and that an appropriate political compact on equalisation principles and the standard of equalisation is struck.

Guideline 10. Strengthen national regional development policies and equalisation systems to reduce territorial disparities

Checklist	Yes	Partially	No
Active regional development policies are in place to support the development of lagging regions as a complement to equalisation policies			
The objectives and fundamental principles of fiscal equalisation are clearly defined. If so, by: <ul style="list-style-type: none"> ● Constitution ● National law ● Executive order/regulations 			
The legislation defines the type of programme			
The programme is intended to be: <ul style="list-style-type: none"> ● Gross equalisation (national transfers to have-not jurisdiction but no explicit equalisation tax on richer jurisdictions) ● Net equalisation (fiscal capacity of poorer jurisdictions is upgraded while richer jurisdictions are downgraded) ● Mixed 			
Total pool of transfer funds is determined <ul style="list-style-type: none"> ● By equalisation standard ● Arbitrary 			
Fiscal capacity is equalised <ul style="list-style-type: none"> ● Potential per capita revenue from each base ● Actual per capita revenues ● By macro indicators 			
Fiscal need is determined <ul style="list-style-type: none"> ● Considered as equal per capita ● Ad hoc determination ● Regression based approaches 			
The overall complexity of the programme is perceived as: <ul style="list-style-type: none"> ● High complexity ● Medium complexity ● Low complexity 			
There is a sunset clause			
There is a stability clause			

There are ceilings and floors to circumvent large yearly fluctuations in entitlements			
Who recommends the formula? <ul style="list-style-type: none">• Independent grant commission or similar body• Ministry in charge			

Notes

¹ See also Allain-Dupré (2018_[5]).

² In many cases, there is also a provincial police force and the municipalities in those cases will have their policing needs provided by that provincial police force rather than the RCMP. For example, in Ontario, major cities have their own police forces (Toronto Police, Ottawa Police, etc.) and outside of these major cities, there is the Ontario Provincial Police (OPP), which provides services in rural areas and small municipalities. British Columbia on the other hand does not have a provincial police force, and so in that case it is the federal RCMP that provides the police services in small municipalities there.

³ The *länder* governments are directly represented at the Bundesrat, the upper house of the parliament with veto power over issues affecting *länder* interests, to incorporate regional interests in federal legislation.

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Annex A. Subnational government organisation and finance: Sources and methodology

Sources of fiscal data

Data at country level are derived mainly from the OECD National Accounts harmonised according to the new standards of the System of National Accounts (SNA) 2008, implemented by most OECD countries since December 2014. They are complemented by data from Eurostat, IMF (Australia and Chile) and national statistical institutes for some countries or indicators (in particular, territorial organisation). Data were extracted in February 2018 and are from 2016, unless otherwise specified.

The statistical data for Israel are supplied by and under responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law."

Methodology

General government: the term "public" is used for "general government" sector (S.13). It includes four sub-sectors: central/federal government and related public entities (S.1311); federated government ("states") and related public entities (S.1312); local government i.e. regional and local governments and related public entities (S.1313) and social security funds (S.1314). Data are consolidated within S.13 as well as within each subsector (neutralisation of financial cross-flows).

- **Subnational government:** it is defined here as the sum (non consolidated) of subsectors S.1312 (federated government or "states") and S.1313 (local government).
- **Expenditure:** they comprise current expenditure (compensation of employees, intermediate consumption, social expenditure, subsidies and other current transfers, taxes, financial charges, adjustments) and capital expenditure.
- **Expenditure/investment by area:** they are defined according to the ten functions established in the Classification of the Functions of Government (COFOG): general public services; defence; public order and safety; economic affairs; environmental protection; housing and community amenities; health; recreation, culture and religion; education; and social protection.
- **Capital expenditure:** they consist of investments (see below) and capital transfers (i.e. investment grants and subsidies in cash or in kind made by subnational governments to other institutional units).

- **Investment:** it includes gross capital formation and acquisitions, less disposals of non-financial non-produced assets. Gross fixed capital formation (or fixed investment) is the main component of investment. NB: since the new standards of the SNA 2008, expenditures on research and development and weapons systems are included in gross fixed capital formation.
- **Revenue:** they comprise tax revenue, transfers (current and capital grants and subsidies), tariffs/user charges and fees, property income and social contributions.
- **Tax revenue:** tax revenue in this publication exclude revenue from social security contributions, which are included in the OECD definition of taxes (please see section A2 of the OECD Interpretative Guide for further information). They comprise taxes on production and imports (D2), current taxes on income and wealth (D5) and capital taxes (D91). They include both own-source (or "autonomous") taxes and shared taxes (tax revenue shared between central and subnational governments). NB: the SNA 2008 has introduced some changes concerning the classification of some shared taxes. In several countries, certain tax receipts have been recently reclassified as transfers and no longer as shared taxes.
- **Debt:** based on the SNA 2008, gross debt includes the sum of the following liabilities: currency and deposits + debt securities + loans + insurance pension and standardised guarantees + other accounts payable. Most debt instruments are valued at market prices. NB: OECD definition differs from the one defined in the EU Maastricht protocol which is restricted to the sum of the first three items (i.e. mainly borrowing).
- **OECD and EU averages:** they are in almost cases weighted ("OECD area average"). However, unweighted averages ("OECD country average" i.e. simple arithmetic average) have been used in some cases. The difference between weighted and unweighted averages can be significant. For example, subnational expenditure accounted for 40.4% of public expenditure in the OECD and 16.2% of GDP on weighed average but 31.8% of public expenditure and 13.5% of GDP on unweighted average. Both approaches are valuable. In one case (unweighted), a small country will have a same weight that a large country. In the other case, the weight of each country in the total is taken into consideration for the calculation. In weighted figures, the biggest countries drive the results because their population for a major share of OECD. Intermediary averages have also been used to make the distinction between OECD federal countries and OECD unitary countries.

Annex B. Methodology of the Regional Authority Index

The Regional Authority Index (RAI) evaluates individual levels of government (or individual regions in asymmetric arrangements) on an annual basis across ten dimensions of regional authority. A mix of primary sources (constitutions, legislation, statutes), secondary literature and consultation of country experts are employed to achieve reliable and valid estimates. The coding scheme and the method have proven successful – and withstood the test of academic scrutiny – for estimates of regional authority in 81 democracies for 1950-2010 (Hooghe et al., 2016_[1]; Hooghe, Marks and Schakel, 2008_[2]; 2010_[3]). The same methodology is applied to the update from 2010 to 2016.

The Regional Authority Index is grounded in a well-established set of concepts. Authority is defined as legitimate power, that is, power recognised as binding because it is derived from accepted principles of governance (Dahl, 1968_[4]). Formal authority is defined as authority exercised in relation to explicit rules, usually written in constitutions, legislation, treaties or statutes. A regional government has some degree of authority, with respect to some territorial jurisdiction, over certain actions. The proposed instrument, therefore, specifies: i) the territory over which a government exercises authority; ii) the depth of that authority; and iii) the spheres of action over which it exercises authority.

- With respect to the territorial scope of authority, a government may exercise authority in its own jurisdiction or co-exercise authority over a larger jurisdiction in which it is part. This is the distinction between self-rule and shared rule. The expression of authority in self-rule, that is rule over those within the regional territory, is fundamentally different from that in shared rule, that is rule in the country as a whole.
- With respect to depth of authority, one needs to estimate the degree to which a government has an independent legislative, fiscal, executive organisation, the conditions under which it can act unilaterally and its capacity to rule when opposed by the national government.
- With respect to spheres of action, a regional or international government can have authority over a smaller or broader range of policies. Authority over taxation and borrowing, and over constitutional reform are especially important.

The coding scheme presented in the table below sets out the ten dimensions that constitute the latent variable of regional government. They engage the following questions: i) What is authority and how might it be disaggregated into discrete dimensions?; ii) How can these dimensions be operationalised unambiguously?; iii) What rules can be specified to code governments on these dimensions?; iv) What ambiguities arise and how might one sensitively adjudicate them?; v) How robust are the resulting estimates to the assumptions that generate them?; vi) How might one evaluate systematic and random error in the estimates?

Table A B.1. Ten dimensions of authority for regional government

SELF RULE	Authority exercised by a regional government over those living in its territory	0-18
Institutional depth	The extent to which a regional government is autonomous rather than deconcentrated	0-3
Policy scope	The range of policies for which a regional government is responsible	0-4
Fiscal autonomy	The extent to which a regional government can independently tax its population	0-4
Borrowing autonomy	The extent to which a regional government can borrow	0-3
Representation	The extent to which a regional government has an independent legislature and executive	0-4
SHARED RULE	Authority exercised by a regional government or its representatives in the country as a whole	0-12
Lawmaking	The extent to which regional representatives co-determine national legislation	0-2
Executive control	The extent to which a regional government co-determines national policy in intergovernmental meetings	0-2
Fiscal control	The extent to which regional representatives co-determine the distribution of national tax revenues	0-2
Borrowing control	The extent to which a regional government co-determines subnational and national borrowing constraints	0-2
Constitutional reform	The extent to which regional representatives co-determine constitutional change	0-4

Source: Hooghe, L., G. Marks and A. Schakel (2010[3]), *The Rise of Regional Authority. A Comparative Study of 42 Democracies*, Routledge, London.

Annex C. Subnational governments in the OECD

The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

Table A C.1. Type and numbers of subnational governments in the OECD: Country by country, 2017-18

	Municipal level	Intermediate level	Regional or state level
Federations and quasi-federations			
Australia	562 (local government areas)		8 (6 states + 2 territories)
Austria	2 098 (municipalities)		9 (<i>Bundesländer</i>)
Belgium	589 (municipalities)	10 (provinces)	6 (3 regions + 3 communities)
Canada	3 959 (census subdivisions)		13 (provinces and territories)
Germany	11 054 (municipalities)	401 (294 rural districts and 107 district-free cities)	16 (<i>Länder</i>)
Mexico	2 463 (municipalities)		32 (31 states + federal district)
Spain	8 124 (municipalities)	50 (provinces)	17 (autonomous communities)
Switzerland	2 222 (municipalities)		26 (<i>cantons</i>)
United States	35 879 (municipalities, towns and townships)	3 031 (counties)	50 (states)
Unitary countries			
Chile	345 (municipalities)		16 (regions)*
Czech Republic	6 258 (municipalities)		14 (regions)
Denmark	98 (municipalities)		5 (regions)
Estonia	79 (municipalities)		
Finland	311 (municipalities)		1 (autonomous region of Aland)
France	35 357 (municipalities)	101 (<i>départements</i>)	18 (regions)
Greece	325 (municipalities)		13 (regions)
Hungary	3 178 (municipalities)		19 (counties)
Iceland	74 (municipalities)		
Ireland	31 (county and city councils)		
Israel	255 (local governments)		
Italy	7 960 (municipalities)		20 (regions)
Japan	1 741 (municipalities)		47 (prefectures)
Korea	229 (cities, counties and autonomous districts)		17 (regional-level entities)
Latvia	119 (municipalities)		
Luxembourg	102 (municipalities)		
Netherlands	390 (municipalities)		12 (provinces)
New Zealand	67 (territorial authorities)		11 (regional councils)
Norway	422 (municipalities)		18 (counties)
Poland	2 478 (municipalities)	380 (314 counties and 66 cities having the status of county)	16 (regions)
Portugal	308 (municipalities)		2 (Azores and Madeira)
Slovak Republic	2 930 (municipalities)		8 (higher territorial units)
Slovenia	212 (municipalities)		

Sweden	290 (municipalities)	21 (county councils)
Turkey	1 397 (municipalities)	81 (provinces and metropolitan municipalities)
United Kingdom	391 (local councils)	27 (county counties, only in England) 3 (Northern Ireland, Scotland and Wales)
OECD35	132 287	4 000 519
EU28	86 840	969 263

Note: There are 589 municipalities to date in Belgium. From 2019 onwards, some mergers of municipalities are foreseen (in the Flemish Region), that will result in 581 municipalities.

Sources: Adapted from OECD (2018^[5]), *Subnational Governments in OECD Countries: Key Data (brochure)*, <http://www.oecd.org/regional/regional-policy>; OECD (2017^[6]), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, <https://doi.org/10.1787/9789264272866-en>.

Annex D. Decentralisation and recentralisation processes in selected OECD countries

Table A D.1. Decentralisation and recentralisation processes in selected OECD countries

Belgium	<ul style="list-style-type: none"> • 2001: Revision of the Constitution Special Act. Lambermont Agreement provides regions with more tax autonomy, regulatory powers. 2011: 6th State reform, transferring in 2014 additional responsibilities to regions (labour market policies, mobility and justice) and communities (family allowance, long-term care, health) and increasing own-source tax resources. The regions had already several responsibilities on labour market policies and mobility, and the 6th state reform transferred additional responsibilities to the regions in these fields (but they remain mixed responsibilities). Justice remains a mainly federal matter. However, the so-called "justice homes" have become a responsibility of the communities since the 6th state reform and not a responsibility of the regions. Concerning health, certain aspects of the healthcare policy have been transferred to the communities, but the major part of health remains a federal (central government) responsibility. • Since 2014, regions are able to raise additional "enlarged" percentages of individual income tax revenue. Since 2014, the regions can levy a regional personal income tax (PIT) by means of a regional additional tax on PIT. Personal income tax consists now of two major components: federal (central government) PIT and regional PIT. • Region's tax competencies are also increased regarding tax bases and exonerations. • Both Flanders and Wallonia are engaged in local government reforms (decrease in responsibilities and taxing power at the provincial level; more autonomy, scope of action and revenues for municipalities).
Chile	<ul style="list-style-type: none"> • 1992: Adoption of two organic constitutional laws, one creating a "mixed" regional government system and the other on the first elections at universal suffrage of mayors and municipal councillors held in 1992. • 1999: New constitutional law extended municipal powers and responsibilities in the field of economic development, environment, planning, equal opportunities, etc. • 2009: New push towards a decentralisation agenda, especially through the constitutional reform establishing direct election by citizens of regional councillors, creating a democratically-elected body to manage regional development. The first direct elections took place in 2013 and regional councillors took office on March 2014. • 2017: Publication of the law establishing transforming the "mixed" regional system (deconcentrated and decentralised) into a full self-government system thanks to the direct election of the regional executive (governors) by popular vote every four years. Transfer from the national government to the new self-governing regions of responsibilities in three areas (economic development, social development and infrastructure and housing) should follow as well as a reform of the funding system.
Czech Republic	<ul style="list-style-type: none"> • 2000-2002 decentralisation reform: Creation of a new regional tier in charge of secondary education, regional roads, economic development and planning, health); the Municipal Act 128/2000 defines the legal framework, organisation and responsibilities of municipalities. The Local Finance Act 243/2000 defines the regional and municipal financing system based on tax sharing. • 2005 and 2013: Fiscal reform increasing of municipal tax revenues. • 2015: Some municipal responsibilities transferred from small municipalities to larger municipalities (to overcome municipal fragmentation) and to the central government in the framework of the social reform.
Denmark	<ul style="list-style-type: none"> • 1970-2000: Several waves of decentralisation reforms between 1970 and 2000, including the 1998 reform: "Denmark as a case study for a renewal of the public sector to boost quality and efficiency at all levels and introduction of market-oriented mechanism or competitive public management". • 2007 reform: Municipalities gained responsibilities for social welfare and education, making them responsible for most citizen-related tasks. The five new regions were granted responsibilities for healthcare services, regional development, regional transport and the environment. Establishment of a new financing and equalisation system: municipal tax revenues were modified while new regions lost their taxing power, replaced by central government transfers.

Estonia	<ul style="list-style-type: none"> • 1989: Re-establishment of decentralisation by the 1989 Local Government Act, followed by the 1993 Local Government Organisation Act which abolished counties as local government tier. • 2001: Municipalities (and central government) are not more responsible for healthcare which is privatised (limited companies or foundations). • 2016: Territorial-Administrative Reform Act adopted; the number of municipalities decreased from 213 to 79. This territorial reform could be accompanied by a reform of tasks and financing framework.
Finland	<ul style="list-style-type: none"> • 1995: A new enabling Local Government Act gave local governments more freedom to organise their affairs, based on the experimentation of the “Free Commune Act” (1988); major reform of grants system. • 1999: Local autonomy is guaranteed by the 1999 Constitution. • 2007: PARAS reform (Act on Restructuring Local Government and Services). • 2013: Municipal Structure Act. • As of 1 January 2019: Creation of 18 autonomous elected regions (replacing the joint municipal bodies) having responsibility for the organisation of healthcare and social services (transferred from joint municipal authorities, local authorities and central government) as well with responsibilities in the area of regional economic development, transport, environment and rescue services.
France	<ul style="list-style-type: none"> • 1982-83: Decentralisation laws establishing the principle of “free administration”, and organising the transfer of responsibilities (education, social affairs, etc.) and resources (staff, finances), in particular to the departments and the regions, created as self-governing bodies by the above-mentioned laws (“first Act” of decentralisation). • 2003-04: “second Act”: New responsibilities transferred to departments and regions (social sector; spatial planning and regional development; local and regional transport and national roads; vocational training, etc.), more financial autonomy and the ability of local governments to carry out experiments in several areas. • 2010 reform: Multi-faceted local government reform, including a clarification of responsibilities; the setting up of common “territorial councillors” for regions and <i>départements</i>; a reform of the local taxation system (reduction of local taxing power) and equalisation mechanisms; a streamlining of inter-municipal co-operation; the creation of a new status of <i>métropole</i>, etc. Important parts of the 2010 legislative package were revoked. • 2013-15: “Act III of decentralisation”: New territorial and decentralisation reform resulting in the law on metropoles (2014), regional mergers (2014) and the law NOTRe (2015) which modifies allocation of responsibilities across levels of subnational governments, reinforcing those of regions (economic development, territorial planning, environment protection, vocational training).
Germany	<ul style="list-style-type: none"> • 2006 Federal Reform (<i>Föderalismusreform I</i>): <i>Länder</i> gained additional responsibilities regarding economic activities and trade, education (universities), environmental protection, crime punishment, staff management, etc. The reform also clarified the distribution of responsibilities between the federal and the states governments. • 2009 federal reform (<i>Föderalismusreform II</i>): New changes introduced, in particular, new financial arrangements. • 2001: Introduction of the “debt brake” to reduce future public debts. • Municipalities are governed by <i>länder</i>'s legislation.
Greece	<ul style="list-style-type: none"> • Principles of decentralisation and local autonomy mentioned in the 1975 and 2001 Constitutions. • 1986: Creation of the current regions as a second-level administrative entities, complementing the prefectures. • 1997: <i>Kapodistrias</i> reform of local and regional government gave more powers to the regions and merged municipalities. • 2010: <i>Kallikratis</i> reform (entered into effect on 1 January 2011), creating 13 full self-governing regions with new responsibilities in the area of regional planning and development including structural funds (transferred from the prefectures) and merging municipalities. The reform also transferred some responsibilities relative to local development, child protection, elderly care, and social assistance to jobless and poor people and health prevention to municipalities.
Hungary	<ul style="list-style-type: none"> • 1989-95: Restoration of the autonomy of municipalities and counties, notably through the 1990 Act of Local Government. The local governments are given broad responsibilities and autonomy in terms of financial management. • 2012 Constitutional reform and 2011 Cardinal Law on Local Governments: Recentralisation process: counties lost several major responsibilities (healthcare, notably hospitals, social initiatives and secondary education) to be now in charge of regional development for the most part. Municipalities are no longer being responsible for primary education. The central government took over a vast array of subnational responsibilities and reinforced its oversight over legal compliance and administrative functioning of subnational governments. • 2013: Reform of the subnational financing system: reduced and stricter system of central government transfers from an income-based system to a task-based system (earmarked funds); setting up of an authorisation framework for borrowing. • 2010: In parallel, the central government launched an important State Territorial Administration Reform (STAR), thus fundamentally reshaping the jurisdictional, organisational and human resource foundation of public service delivery at all levels of the public sector in Hungary.

Iceland	<ul style="list-style-type: none"> Local self-government is guaranteed by the constitution and legal arrangements governing municipalities are laid down in the Local Government Act of 1998, amended several times. 2011: municipalities gained new responsibilities regarding service provision and support for disabled people. Other transfers are currently discussed (e.g. elderly care, entire healthcare sector) but the obstacle is the small size of many municipalities; Local Government Act (LGA) established new fiscal rules for municipalities together with enhanced arrangements for fiscal oversight of municipal finances and new fora for central-local fiscal co-ordination.
Ireland	<ul style="list-style-type: none"> 2001: Local Government Act introduced the range of reforms set out under “Better Local Government” White Paper. 2012: “Reforming Local Government” plan and “Putting People First Report” deal with issues of structures, functions, funding, efficiency and service, and governance and accountability, the goals being to strengthen local authorities’ responsibilities, functions, leadership and financing mechanisms. 2013: Introduction of a local property tax with rate-setting powers at the margin. 2014: Local Government Reform Act merged 114 local councils into 31 local governments, abolished the previous 8 regional authorities (replaced by 3 regional assemblies, not elected by universal suffrage) and clarified the allocation of responsibilities, reassignment of water services to Irish Water, recentralisation of some functions and allocation of several new responsibilities for local and community development, in addition to an enterprise support and economic development role.
Italy	<ul style="list-style-type: none"> 1990s: Important decentralisation process, including the 1990 law on the “Regulation of Local Autonomies” and the 1997 Bassanini reform which implemented the subsidiarity principle through different laws, referred as “administrative federalism”, and significantly modified fiscal, administrative and political framework at the subnational level. 2001: Major move towards decentralisation through the constitutional reform which entrenched regions, provinces and municipalities in the constitution, placing them on the same level as central government. A clause listing the responsibilities of the central government was introduced while regions receive all residual competencies. Several implementing decrees were not adopted, however (“unfinished agenda”). 2006: National referendum rejecting the constitutional reform further strengthening of the regions, leading the way to a federal state. 2009: Adoption of a new framework law on fiscal federalism, reshaping subnational government functions and relations across levels of government as well as fiscal framework. 2014: Abolition of provinces by Law 56/2014 as self-governing entities. They are transformed into inter-municipal co-operation bodies, which also became “metropolitan cities” in each of the ten metropolitan areas designed by the law. 2016: National referendum rejecting the constitutional reform which intended to clarify the allocation of responsibilities between the central government and ordinary regions, abolishing “concurrent competencies” and recentralising several responsibilities (e.g. transport, labour, public finance and taxation).
Japan	<ul style="list-style-type: none"> 1995-2000: Decentralisation Promotion Reform launched in 1995 and supported by the Decentralisation Promotion Committee led to the adoption of the “Omnibus Decentralisation Law” of 2000 which abolished the system of agency-delegated functions (in which regional governors and mayors serve as regional representatives of the central government) and increased subnational autonomy and responsibilities. This law introduced revisions to more than 475 anterior laws. 2002-06: Trinity Reform laid the financial component of the decentralisation reform, with three major components: creation of a tax-sharing system between the national and subnational level, a reform of the equalisation tax (local allocation tax) and the abolishment of several national earmarked grants. 2006: Launch of the Second Decentralisation Promotion Reform, complementing the first reform to grant further authority to local governments, rationalise their functions and continue municipal mergers.
Korea	<ul style="list-style-type: none"> 1987: “Declaration for Democratisation” followed in 1988 by the reform of the Local Autonomy Act and the Local Finance Act. 1991-95: First local elections held for local councillors (1991) and local executives (1995). 1999: Launch of a large reform of the public sector which included a comprehensive decentralisation programme, monitored by a Special Committee on the Devolution of Government Affairs. 2004: Special Act on the Promotion of Decentralisation, enacted under the impulsion of the Presidential Commission for Decentralization, clarified principles and methods for decentralisation, transferred new functions to local governments and abolished special administrative agencies. 2005: Fiscal reform establishing the “Special Account for National Balanced Development” which transformed many specific-purpose grants into integrated national grants for regional development; rationalisation of the national and local tax system. 2017: Autonomy and decentralisation was selected as a core task within the Top 100 national tasks of the Moon Jae-In administration. 2018: A new Presidential Committee on Autonomy and Decentralization was set up in January 2018. The revised bill of the “Special Act on Autonomy and Decentralization and Local Administration System” was promulgated on March 2018. Constitutional reform is proposed, including adding to Article 1 of the Constitution the mention “Republic of Korea”

	<p>promotes decentralization” and giving local governments more autonomy.</p>
Lithuania	<ul style="list-style-type: none"> ● 1994 and 2002: Local Government Act defining municipal functions and ensuring their autonomy. ● 2010: Elimination of state counties leading to the transfer of their competencies to municipalities (primary healthcare, education and social services) and to the central government. Counties have been replaced by regional development councils composed of municipal councillors. ● 2014: Full responsibility for social assistance is given to municipalities (funding and management).
Mexico	<ul style="list-style-type: none"> ● Late 1980s: Fiscal and regulatory decentralisation, including devolution to states of basic education (1992) and healthcare (1996) responsibilities; reform of the National System of Fiscal Co-ordination in 1998. ● Municipal autonomy recognised by the constitutional reforms in 1983 and 1993. ● 2007 Fiscal reform: States were given more taxing powers; simplification and improvement of the incentives embedded in the formulas for the distribution of federal transfers. ● 2013: Nation-wide political reform introducing, among other things, re-election of mayors; bill transforming the federal District of Mexico into a state, with the same legal and administrative status. ● 2014-15: Fiscal reform (part of <i>Pacto Por Mexico</i>) improving the tax system, strengthening the fiscal responsibility framework and overhaul rules for states and municipal debts.
Netherlands	<ul style="list-style-type: none"> ● 2002: Act of “dualisation” separating composition, functions and powers of the deliberative council and the executive. ● 2007: Decentralisation programme transferred new responsibilities to provinces and municipalities. ● Since 2015: Start of a new decentralisation process with large responsibilities to be transferred to municipalities in the social sector (youth health, long-term care and employment support for young disabled people). Creation of a new fund for social affairs to accompany the decentralisation in the social sector; revitalising and strengthening the role of the provinces with more focused powers in regional planning, economic development and co-ordination.
New Zealand	<ul style="list-style-type: none"> ● 1989: Local Government reform, monitored by an independent Local Government Commission, consisting in a large restructuring of local governments and special-purpose bodies, by reducing significantly the number of local authorities, creating regional councils and allocating functions. ● 2002: Local Government Act introduced a framework for local authorities, establishing responsibilities of local government and increasing their autonomy by providing them with a general power of competency. ● 2013: Local Government Act clarified responsibilities between regional councils and territorial authorities and includes several managerial measures, in line with the Better Local Government New Zealand Reform. ● 2018: Productivity Commission to investigate Local Government funding and financing.
Norway	<ul style="list-style-type: none"> ● 1992: Local Government Act sets the basic legal framework for municipalities and counties. ● 1999: Abolition of the national corporate income tax as a local tax in 1999. ● 2001: Recentralisation of the responsibility for hospitals from the counties to the central government in the framework of the national healthcare reform. ● 2003 and 2010: New responsibilities – and transfers – granted to counties (spatial planning, regional development and innovation policy) and municipalities (health and social care). ● 2014-20: start of large local government reform, resulting in the mergers of regions (from 18 counties to 11 from 2020, including Oslo municipality) and municipalities (from 428 in 2015 to 356 at the end of the process in 2020). Adoption of a new municipal law in June 2018, strengthening municipalities and relations across levels of government. Government plan to allocate new tasks and instruments to the new regions in order for them to become “stronger regional community developers” (scheme to be presented in October 2018).
Poland	<ul style="list-style-type: none"> ● 1990: Act on Municipality re-established municipal autonomy, giving them large responsibilities. ● 1998: Act on Local Government revenue, further reformed in 2003 and 2004 to provide subnational governments (SNGs) with more fiscal autonomy. SNGs gained more financial autonomy, with a decrease in the share of central transfers (and of earmarked grants), and increased shared tax revenues (higher proceeds from PIT and corporate tax). ● 1999: Local Government Organisation Act created the regional and intermediate levels (<i>voivodeships</i> and <i>powiat</i>s), transferring to them several responsibilities (secondary and higher education, public health, social aid, roads, regional economic development). ● 2009: Decentralisation of new tasks to regions (regional rail transport, waste and water management, and environmental protection). ● 2013: Adoption of strict fiscal rules applying to subnational governments.
Portugal	<ul style="list-style-type: none"> ● 2007: Reform of the Local Finance Act, expanding municipal competencies and reforming the grant system. ● 2013: Local Government Reform giving additional responsibilities to municipalities regarding healthcare, park management and city planning; Regional and Local Finance Laws (effective in 2014) were enacted with the goals of strengthening fiscal sustainability and increasing transparency and accountability.

	<ul style="list-style-type: none"> ● Since 2015, a new programme of decentralisation is under preparation, including the transfer of responsibilities to local councils in a wide range of areas as well as new Local Finances Law. ● 2018: Approval of Law no. 50/2018, august 16 (framework law on decentralization of competences to municipalities and inter-municipal communities) and revision of the Local Finance Law (Law no. 51/2018, August 16).
Slovak Republic	<ul style="list-style-type: none"> ● 1990: Municipal Autonomy Act. ● 2001: Decentralisation of new responsibilities to municipalities (social assistance, urban planning, housing, environment, primary schools, recreation, etc.) and creation of the regions (Higher Territorial Units), entered into force in 2002, now in charge of secondary, professional and vocational education, social welfare, regional roads and transport and regional economic development and territorial planning. ● Project of Further Decentralisation of Public Government for the years 2003-06 confirms the decentralisation process. ● 2005: Act on Local Financing deeply modified the subnational financial system by raising both shared taxes and own-source taxes, and reduced central government transfers to sub-national governments. ● 2014: ESO Programme (efficient, reliable and open state administration) restructuring the central government territorial administration to promote cost-efficiency and simplification, including better multi-level governance at the local level in public services delivery to citizens.
Slovenia	<ul style="list-style-type: none"> ● 1993: Adoption of the Local Self-Government Act. ● 2005: Reform of the Local Self-Government Act to determines the principles of regulation of municipalities and increase decentralisation. ● 2007: Financing of Municipalities Act reinforced fiscal decentralisation, introducing additional resources for municipalities and consolidating the system of vertical equalisation. ● 2008: Draft bill creating 13 regions rejected by referendum.
Spain	<ul style="list-style-type: none"> ● 2000-02: Transfer of education (2000) and healthcare (2002) to autonomous communities. ● Reforms of autonomous communities' status case by case (e.g. Catalonia and Valencia in 2006, Andalusia, Aragon and Balearic Islands in 2007, etc.) ● 2009: Law 22/2009 on the financing of autonomous communities (in effect since 2011): increase in the share of national taxes allocated to autonomous communities; reform of the equalisation system and intergovernmental. ● 2012: Organic Law 2/2012 on Budgetary Stability and Financial Sustainability introducing strict fiscal rules for subnational governments. ● 2013: Law 27/2013 for Rationalisation and Sustainability of Local Administration (following the work of the Commission for the Reform of Public Administration, CORA) aimed at clarifying of competencies between municipalities and provinces and preventing duplications; adoption of the law on funding municipalities and provinces.
Sweden	<ul style="list-style-type: none"> ● 1991: Local Government Act. ● Since 1997: Experimentation of asymmetric decentralisation in different waves, according to a bottom-up decentralisation process. Different regionalisation options were developed in different regions through four main waves. ● Different reforms of the equalisation system in 2005, 2012 and 2014. ● 2019: All county councils are responsible for regional development matters in their own region.
Turkey	<ul style="list-style-type: none"> ● 2004 and 2005: Package of reforms aimed at the restructuring of the Special Provincial Administrations (strengthened powers), the municipalities (additional responsibilities to them in the area of economic development and education infrastructure), the village administrations, the Local Government Unions and the Metropolitan Municipality. ● 2008: Law on Allocations from Tax Revenues under the General Budget to Special Provincial Administrations and Municipalities. ● 2012: New local government reform, in particular through the new Metropolitan Municipality Act.
United Kingdom	<p>Regional level</p> <ul style="list-style-type: none"> ● 1998: Devolution process creating three devolved nations in Northern Ireland, Scotland and Wales with a directly-elected "national assembly"/parliament and their own government and major competencies transferred to them. It created an asymmetric decentralisation across devolved nations (they do not have the same powers) and with England (no regional governments). ● 2004: Regionalisation process in England suspended in 2004 following the rejection of a referendum held in the north-east of England. ● 2007: Devolution restored in Northern Ireland. ● 2010: Extension of the powers of the Welsh Assembly after the 2010 referendum. ● 2012: New powers transferred to the Scottish Parliament by the Scotland Act 2012 (possibility to raise own taxes to come into effect in full in 2016 and introduction of a range of measures to strengthen the devolved administration in Scotland).

Local level

- England: Decentralisation under the form of “localism” emerged gradually since the 2000s, leading to the adoption of the Localism Act 2011 aimed at pushing decentralisation forward through a general power of competency for local authorities, new responsibilities (housing, social protection, health) and resources (localisation of the council tax, business rates retention as of 2013, grants’ reform). The Cities and Local Government Devolution Act allows greater devolution of powers to combined authorities (housing, transport, planning and policing powers) and introduces directly-elected mayors.
 - Northern Ireland: 2012-15 Local Government Reform devolving new powers and responsibilities to the new 11 councils.
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Sources: OECD elaboration based on research, OECD (2017^[5]), *Multi-level Governance Reforms: Overview of OECD Country Experiences*, <https://doi.org/10.1787/9789264272866-en>; OECD-UCLG (2016^[6]), *Subnational Governments Around the World: Structure and Finance*, <http://www.oecd.org/regional/regional-policy/sngs-around-the-world.htm>.

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