

Country Case Studies on Intergovernmental Transfer Schemes and SDC support:

Bangladesh

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1. The objectives and design elements of the supported transfer

The Upazila Fiscal Facility (hereafter the Facility) is an example of a formula-based transfer system. The objective is to support sub-districts (Upazila Parishad, UZP) in directly contributing to improved basic service delivery within the responsibilities assigned to them¹ and contribute to achieving the MDGs and Bangladesh's Development goals (Vision 2021). As importantly the transfers aim at strengthening the UZPs' leadership role in relation to local sectoral agencies to foster an integrated local planning umbrella.

Political/contextual considerations that influenced objectives and design

The Facility has been established as part of a broader project that started shortly after the Government decided to re-establish this unit of Local Government (Upazila Parishad Act 2009) and held the election of their chairs and vice-chairs. The project further intervenes for i) capacity development of Upazila public officials in political and administrative functions; ii) an integrated planning at Upazila level and iii) policy support.

The broader project intends to encourage the Upazila Parishad to play the mandated role in promoting the development of the Upazila involving all stakeholders and to reinforce the governance mechanisms therefore. This includes establishing their leadership for the challenging function of coordinating the action of 13 transferred line departments providing services related to 17 subjects.

Type of transfer

The transfer is formulae-based and determined by a basic allocation which is then weighted according to the performance of the local government. The transfers are intended to co-finance development activities in order to link together on-going activities taking place (along with the resources tied to them) at the Upazila and lower Union levels (horizontal and vertical linkages), to derive synergy and expand the impact.

Financial mechanism

The Upazila Fiscal Facility is being piloted by the Government of Bangladesh to provide 14 UZPs (from the total 487) with formula-based allocations. Presently, the Facility transfers complement other grants received from the national budget. Hence in those 14 UZPs an average 40% of the total transfers come from the Facility. In an ideal situation, the system introduced by the Facility is intended to replace the existing ad hoc transfers to make transfers transparent and predictable.

The basic allocation for each UZP is calculated on the basis of the following formula:

- A fixed or equal share 30% of the total amount
- An amount proportional to UZP population 30% of the total amount
- An amount proportional to UZP land area 30% of the total amount
- An amount proportional to UZP backwardness 10% of the total amount

¹ UZPs are mandated by the Local Governance (Upazila Parishad) Act 2009 to provide services in the sectors of education, health, water, agriculture, livestock & fisheries, rural infrastructure, cooperatives and income generation.

The basic allocations are thereafter aligned with the principles of performance based grants, whereby the basic allocation are weighted by relative performance of the targeted UZP in relation to a set of selected indicators that reflect governance practices prescribed by law. The performance indicators relate to four areas that are: a) mandated structures, b) administrative processes, c) financial management and d) specific requirements.

Performance areas	Mandated structures	Administrative processes	Financial management	Specific requirements
Indicators	<ul style="list-style-type: none"> - 17 Standing committees formed and operational - Regular coordination meeting held and officials participated 	<ul style="list-style-type: none"> - Budget formulated & content complied - Mandatory steps followed - Budget disclosed 	<ul style="list-style-type: none"> - Revenue collection targets achieved - Development expenditure targets achieved - Bidding process used 	<ul style="list-style-type: none"> - Project Selection committee formed and operational - Grant disbursement norms complied - Reports submitted timely

There is one additional feature worthwhile mentioning. In each of the 7 covered districts 2 UZP receive the top-up resources. Every year the two best performing UZP in these districts receive a transfer composed of the fixed entitlement described above, plus an amount influenced by equity considerations and the total is being weighted according to performance evaluated in yearly performance assessments.

In all participating subnational units, the impact of the performance calculations influences the final transferred amount by 20 to 25% in average. The latter step of weighting the allocation by the performance of the UZP serves as an incentive for them to perform better in terms of effective and transparent governance practices.

Hence the introduction of a formulae-based system for transfers to Upazila Parishads has the main advantage of making the sub-national transfers more predictable and transparent, in an environment where incentives for sub-national good governance cannot be taken for granted.

Once the transfers are received, the UZPs have to comply with three rules in their utilization of the grants:

- Development schemes are prioritized based on the five year development plans elaborated by the UZP with close involvement of sectors and lower level Union Councils under its jurisdiction.
- Transfers are used for co-financing (max. 40%) activities that benefit the population of multiple Unions or the entire Upazila and/or involve activities that require the collaboration between multiple sectors.
- The decision-making and oversight of the funded activities to be under the political leadership of the Upazila Council.

There is a negative list of costs that cannot be financed using the transfers including the purchase of vehicles, construction of administrative buildings, private goods, support to religious activities and payment of recurrent salaries or office maintenance of UZP.

Accountability dimensions

Accountability towards the citizen is ensured through different steps in the project cycle. First through the participatory planning process leading to the five-year and annual development plans which are the basis used to determine which interventions will be financed. Second through the involvement of citizen in the committees in charge of overseeing the interventions and third through the reporting done at the occasion of open budget meetings where UZP report to the public about the utilization of their budgets.

The UZP follow half yearly financial reporting on all resources received by the central government. The resources received from the Facility are part of this general report.

2. The supported transfer within the intergovernmental fiscal system

An SDC mandated study estimated that only 2.6% of total public expenditure was executed by Local Governments in the fiscal year 2011-12 (J. Boex, 2012). It can also be noted that per capita allocation of intergovernmental transfers in Bangladesh is still below 1 USD which is relatively low compared to neighboring countries (Christensen et al., 2014).

Much of what UZP can raise from own revenue –which amounts to about 24% of their income²- is used to defray day-to-day expenditure (honorariums, building maintenance etc). Upazila Parishads mostly depend upon central government transfers to implement development projects. In the 14 UZP benefitting approximately 40% of the transfers received come from the Facility. However, the unconditional grants provided to all UZP are under-regulated and greatly subject to political considerations.

3. The key challenges for implementation of the supported transfer.

The Upazila Fiscal Facility intervention faces certain challenges related to its design and its implementation. Other challenges stem from the current position of the Upazila Parishad as a young and relatively weak institution as well as from the overall normative framework.

Challenges related to the design

The Facility has been introduced as a pilot in addition to other transfers. Nevertheless, from the onset the attempt has been to establish a formula that reflects different principles to be considered in a system of intergovernmental transfers and that could replace other less transparent transfers. In this way the formula entails first a fixed amount to cover processes that take place in every UZP independent of its population profile and size, second a varying amount based on equity objectives and third performance considerations with the weighting of the allocation after assessing performance. However the balance of those principles in the formula needs more careful analysis as the fixed 30% share seems overemphasized if we consider for its justification fixed costs faced by all UZP such as holding statutory meetings and organizing participatory planning processes. Over-emphasis here which is probably resulting from a political consensus in which smaller UZP

² A. Barkat et al. (2015) *Local Governance and Decentralization in Bangladesh: Politics and Economics*. Dhaka, Pathak Shamabesh, p.114

claim “fair entitlements”, although the equal share allocation implies the creation of per capita inequities.

Another challenge related to the design of the Facility is its complexity in design which may limit further scaling-up in this large country (counting 487 UZP) where UZP elected members face capacity and other political constraints. Indeed the effort to make the system transparent and understandable to all UZPs as well as the effort needed for an independent yearly performance assessment seems to be judged as “too heavy” by the government in its current up-scaling plans.

It is worth keeping in mind that fiscal transfer systems do not suffice as a sole incentive for performance and good governance. Beyond this mechanism other avenues for accountability need to be in place.

Challenges related to execution

Three rounds of transfers have been made based on the Facility so far. Initially the project was designed in a manner whereby the annual performance assessments were supposed to be made prior to the planning and budgeting process at a local level in order to establish the amounts of the transfers for the next fiscal year. Based on the predicted figure the UZP could then plan and budget its interventions. However, delays in project start and procurement of assessment teams resulted in non-aligned cycles and time-lags between performance and actual allocation of more than a year. Other resulting difficulties are that UZPs were given the grants at the end of a fiscal year and found themselves confronted with short times to use the funds. As a consequence the linkages between planning, budgeting and project execution are getting blurred.

Position and normative framework

UZP are mostly dependent on intergovernmental fiscal transfers for financing their development interventions as their own revenue only suffices to cover running costs. This give intergovernmental transfers substantial leverage, however over the long term local tax effort would need to be stepped up given that it is critically important for efficiency and accountability objectives. The sense here is that once the local government proves it is delivering effective public services, tax-payers will be more willing to pay taxes and the trust relationship between citizen and local governments will be strengthened.

As explained earlier the Upazila Parishad is expected to play a coordination role between line departments as well as lower level local governments and foster an integrated local planning that considers the priorities of the citizens. However, we still observe persistent parallel planning and financial management arrangements through line departments and UZP delivery mechanisms. The usual system of service delivery through line departments is pursued without the local government –and its significantly lower resources from the transfers - playing a major role on the way services are prioritized and delivered.

Similarly, with its position as middle tier local government, the UZP still has difficulties to surpass parochialist practices where transfers received tend to be divided in equal shares to lower level local governments, the UZP hence serving merely as a transmission channel. One can say that as a young institution the UZP has yet to establish itself and prove its added value for service delivery.

Finally the Facility grants are not yet integrated into the legal system and budgetary framework of Bangladesh. They are thus not registered in the treasury and the budget classification at local level does not follow central level coding so that sectoral analysis of budgets requires complex

accounting procedures. The normative framework needs to be adapted for ensuring that the system is sufficiently institutionalized and sustainable.

4. Success elements

The Facility has been introduced in combination to Capacity Development interventions. This approach proves to be effective in terms of improved planning and budgeting processes as well as inclusive targeting. Indeed after two years a citizen perception survey showed that the proportion of citizen satisfied with the services provided by the UZP was at 58% against 40% in the control areas. Moreover the project mid-term evaluation showed that approximately 70% of development schemes financed through the Facility are MDG oriented and that 10% of total grants have been used to specifically address needs of marginalized groups. (Christensen et al, p.84). Furthermore the schemes are reflecting needs in various sectors such as health, education, agriculture etc. and not only used for hard-core infrastructure as was the previous practice, but also other types of service delivery.

The discretionary nature of the Facility transfers support the principle of having local governments establish local priorities through participatory planning. The provided resources can indeed be used according to local priorities on the contrary to the other grants provided from the national budget that come with pre-defined proportions to spend by sector (f.eg. 3% for watsan etc). This is a useful combination and complementarity of the different grants.

The rule-based nature of the Facility is fostering stronger local political processes such as the requirement to co-finance schemes that lays first steps of integrated local planning and strengthens the collaboration between the elected local government and the line departments. The Facility also lays a promising system for transparent and predictable transfers to prevail over politically-motivated allocations.

The recent decision of the GoB to scale-up the Facility to all Upazila Parishads nationwide using a loan provided by JICA is certainly a successful step towards the sustainability of the system.

5. The role of SDC with regards to transfers

Intergovernmental fiscal transfers are instrumental for local governments to play an effective role and provide adapted local services. The SDC support described in this case study is a co-financing arrangement³ to a project in a component of which the United Nations Capital Development Fund (UNCDF) supports the Government of Bangladesh (GoB) in establishing the Upazila Fiscal Facility and in other components the United Nations Development Programme (UNDP) accompanies the GoB in providing capacity building to local governments and offers policy support.

At the early stage of project design SDC provided technical assistance (with an opening credit) to analyze political economy dynamics at local level and ensure inclusion in the local political processes. Being involved from the start had the advantage for SDC to be in a position to bring added-value with inputs ensuring a close link between technical support, fiscal transfers and good governance principles.

³ A further development partner contributing to the project is the European Commission.

Moreover the experience in Bangladesh suggests that an active involvement in policy dialogue on fiscal decentralization and a capacity building component for recipient local governments are together with the transfers mutually reinforcing elements given the complexity of setting up an intergovernmental transfer system and the training needs related to it.

Since the GoB took over the design of the Upazila Fiscal Facility and simplified some of its elements to scale it up nationwide, there are reasons for SDC support to be phased out gradually. It remains to be seen if the GoB will go another step further and replace the other ad hoc transfers by this or another formula-based system or if both will continue to be provided in parallel leaving significant leverage for the central administration to reward compliant or “politically close” local governments. While the decentralization reform advances other needs of Upazila Parishads remain to be tackled such as strengthening the capacity of the Upazila Parishad to oversee and coordinate line departments in the provision of basic services in order to establish itself as the planning umbrella at sub-district level.

Further sources of information:

- Local Government Division (2013) *Upazila Fiscal Facility Operational Manual*.
- J.P. Christensen, S. Aminuzzaman et al. (2014) *Mid Term Evaluation UPGP and UZG*. Sponsored by UNDP, UNCDF, EU, Denmark and Switzerland.
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