

Development through Policy Reform



Cities Alliance

5. Development through Policy Reform

The examples just reviewed give confidence that discrete projects and programs across a range of sectors can be successfully executed in municipalities. The reality, however, is that such projects and programs often succeed in spite of the broad policy environment in which they are implemented, rather than being facilitated by it. Donors often circumvent these problems as best they can by demanding special operational arrangements for specific projects. For its slum upgrading projects, for example, the Inter-American Development Bank (IDB) requires that (a) the national government transfer project funds to the municipality; (b) procurements be done by the municipality following IDB regulations; (c) a qualified technical staff be in place for the project; and, (d) a single decision point be established for all project aspects (water, land, etc.), which is usually the municipal planning department. Not surprisingly, given the difficult policy environment, a continuing challenge for municipalities is in “scaling up” demonstration projects to activity levels that significantly mitigate the problems addressed.

This section addresses four policy blocks whose shortcomings often inhibit local governments from achieving more. Sometimes municipalities control these policies, but often the constraints are imposed by national legislation. Working with municipalities and national governments to design and implement better policies is the single most productive action the donor community can take to enhance the impact and sustainability of interventions. In its guidelines, the World Bank distinguishes among broad policy packages for specific locations by degree of urbanization (with each needing further adjustment for local circumstances):

- Where urbanization is incipient (i.e., the place is largely rural) ensure key services are in place that benefit everyone regardless of location, i.e., a “spatially blind” policy package—the focus here is regulations regarding land and labor and social services as education, health, water and sanitation.
- For intermediate urbanization cases, add in a timely way transportation, water and sanitation, and communications infrastructure that enhances access within cities and binds hinterlands to them.
- Where urbanization is advanced, add targeted interventions to address slums that will have almost certainly developed. The IDB’s view is that the policies and investments implemented at the previous two urbanization stages will not be sufficient by themselves to tackle such slums. Hence, geographically targeted improvements in water and sanitation, improving tenure security, expanding micro-loans programs to accelerate housing consolidation, and strengthening education and health services would all be pursued.

The IDB’s expert consensus is that effective policy coordination among national, state, and local governments is essential to implement the policies outlined. Is it realistic to expect such coordination? The discussion immediately below addresses this important question.

The Benefits of Decentralized Governance and Revenue Generation

Governance

Municipal governments in developing countries are typically allocated a limited core set of service delivery responsibilities in areas like firefighting, refuse collection, parks, traffic management, local transit service, primary and secondary education and public health. Even for these core services they are reliant on higher levels of government for capital expenditures.

National ministries for water, transportation, and other types of infrastructure control the allocation of funds among local governments for new capital investment projects and often control their designs as well. Most countries lack a Ministry for Urban Development but even where one exists the key infrastructure agencies are not subordinate to it. In reality the Ministry of Finance or Ministry of Planning is the key player in deciding on the type of urban investments funded. Typically, these ministries lack expertise to develop such programs—which probably creates a bias against comparatively complex transportation, slum upgrading, and other major infrastructure projects in the largest cities.¹⁹ The result is extreme fragmentation in municipal-national government relationships—relationships that are typically made even more complex by regional governments also having an active role.

Local governments’ efforts at comprehensive planning within such a fragmented framework are extremely complex and time consuming owing to the number of players involved and cities’ limited powers. The result too often is partially developed plans. The situation also creates the distinct possibility of a series of uncoordinated investments working against each other in determining a city’s future development. A clear policy improvement would streamline these intergovernmental relationships, with municipalities leading a comprehensive planning process that includes all relevant government agencies.

The local planning and implementation process itself often requires improvement along two dimensions. First, most cities’ boundaries include only a limited part of the metropolitan area, requiring planning to be done at the metropolitan level for investments in areas like transportation services, water supply, and pollution control that fundamentally effect the location of economic activity in space. Either through creation of metropolitan governments (by the national legislature) or by more sector-specific ad hoc solutions, design of metropolitan-wide solutions for areas like transportation is essential for effective interventions.²⁰ Second, local government agencies need to strengthen their capacity to plan and implement investment programs. Moreover, distinct agencies must break out of their silos and work more closely together for strong plans to result.

Care is also needed not to devolve responsibility before cities are ready to take on this role. Readiness requires both technical competence and a viable political agreement among city, regional, and national governments.

Donors can play a key capacity building role. In the meantime quicker action can be taken to simplify investment funds allocation (see below) and make them more dependable, thus simplifying the investment decision process.

The rewards to good planning can be large. Chinese cities’ aggressive infrastructure investments and facilitation of private housing construction, for example, largely prevented the creation of squatter communities. And Curitiba, Brazil has largely prevented the development of new informal settlements through good planning and timely investments in transport that provide good access to housing sites that are comparatively distant from most jobs.

Revenue Generation

Municipalities’ planning environment is complex at best, and the structure of government finances generally makes it worse. It is often the case that municipalities have little authority to raise revenue themselves, but rather rely on grants from and direct service provision by higher government levels. The following figure helps to illustrate

that sub-national governments in most countries collect well under 20 or even as little as ten percent of total revenues and spend about the same amount. India and China with their federal systems are exceptions—although local governments in India spend under five percent of the total because of the dominance of state governments. Multiple problems stem from the current funding structure.

One such problem is the uncertainty of local government revenues. This is particularly severe for investment funds, but can be problematic even for basic operations. At least as important, such strong dependency on higher levels of government makes it impossible for local officials to be held accountable for service shortfalls because they can always blame problems on lack of funds from higher government levels. (To be fair, not all local governments take full advantage of the tax bases they do control, property taxes being the clearest case in point.)

An obvious solution is to permanently assign more revenue to local governments—either by granting them the right to levy taxes on a specific base and to set the tax rate or, alternatively, by allocating them a share of a national sales or income tax. However, with the additional resources comes increased responsibility for financing certain services and investments. Inequities arising from differences in localities' tax bases can be compensated through equalization grants from the national government. Critically important is that capacity building accompanies the reassignments. Decentralization of this type is under way in some countries, but progress is slow. Again, capacity building before the devolution is essential.

Need for Substantial Long-Term Capital

Cities will need large amounts of capital to fund the necessary investments. These can come from several sources:

capital markets, national governments, and donor loans and grants. Access to long-term funding is essential and appropriate because the infrastructure thus financed serves multiple generations.

Municipalities sometimes operate under prohibitions or tight limits on borrowing, which makes financing large infrastructure projects even more challenging when they have the authority to do so. Additionally, in part because of insufficient own revenue sources, many cities, especially in Sub-Saharan Africa, are not creditworthy. This is an area where USAID has played a strong role by working with local governments in India, Mexico, and the Philippines among others, to shore up their finances in order to gain

creditworthy ratings and help design initial bond issues.

The multi-lateral development banks have a clear role to play, as do the principle bi-lateral agencies, such as the Overseas Private Investment Corporation (OPIC). OPIC can stimulate capital supply (by reducing financiers'

risks) for a range of tasks, from housing to infrastructure investments. The Millennium Challenge Corporation's large grants could be well-used for urban investments, as could funds from the Senator Paul Simon Water for the Poor Act of 2005.

Redefining a country's fiscal architecture can only be done by the national government and parliament. It is a demanding task, but it carries high rewards in accountability and service delivery efficiency.

Local Ownership

We know from the successful project examples cited earlier that deep citizen involvement is a key component for most

urban initiatives. Such participation results in projects that meet users' actual needs and are therefore more efficient and effective than top-down project development.

Community-based organizations (CBOs) are valuable participants in these efforts. Donors can help to strengthen CBOs and to facilitate the civil society-government interaction that is essential to sustainable development. For example, CBOs are full participants in the preparation of City Development Strategies in the Cities Alliance process, which have served successfully as the foundation for practical plans for city development in Yemen and in dozens of other cities in countries where the Alliance has worked. As laudable as these and other cases are, however, a broad consultative process is still not common. More broadly, there are additional constructive roles for CBOs. First, citizen monitoring of local government spending and revenue collection has been highly successful in increasing government accountability where operational. Second, mature CBOs under proper conditions can effectively deliver services. The Mumbai toilet campaign cited earlier is such an example. In an increasing number of cases, CBOs are operating at scale to help the poor. A well-known example is BRAC (Bangladesh Rural Advancement Committee) that now assists more poor people than does the national government. Strengthening NGOs is also important. In Africa, where local governments hardly function in smaller towns and cities, NGOs are the dominant provider of services in several sectors. Strengthening the capacity of both NGOs and governments will result in accelerated improvements, in part because NGOs' close work with CBOs results in broad dissemination of better practices.

Often the approval of an elected city council is viewed by city governments as sufficient citizen input into the decision making process. In practice, of course, its members are little involved in developing plans for major projects, let alone those at the neighborhood level. They also tend to belong to the city's elite. Inclusion of NGOs, CBOs, civil society, and other stakeholder groups representing the whole community should be standard practice in municipal planning and project development.

Opening up governance, increasing transparency and strengthening accountability are clearly tasks for local government and ones that have been assisted under USAID-supported local government democracy projects. As A. Shah and S. Shah state in, "The New Vision of Local Governance and the Evolving Role of Local Governments":

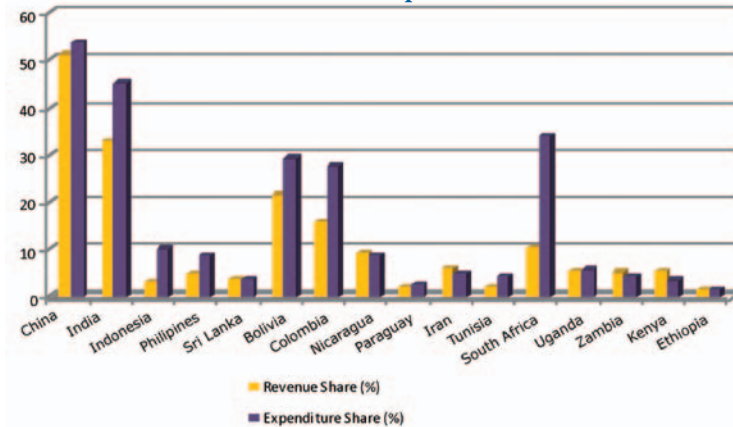
...local governance is not just about providing a range of services but also about preserving the life and liberty of residents, creating space for democratic participation and civic dialogue, supporting market-led and environmentally sustainable development and facilitating outcomes that enrich the quality of life of residents.

Americans can look from their own experience at the benefits from the empowerment of inner-city CBOs during President Johnson's War on Poverty that launched the vast expansion of the African-American community's political participation.



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Sub-national Governments' Share of Total Government Revenues and Expenditures



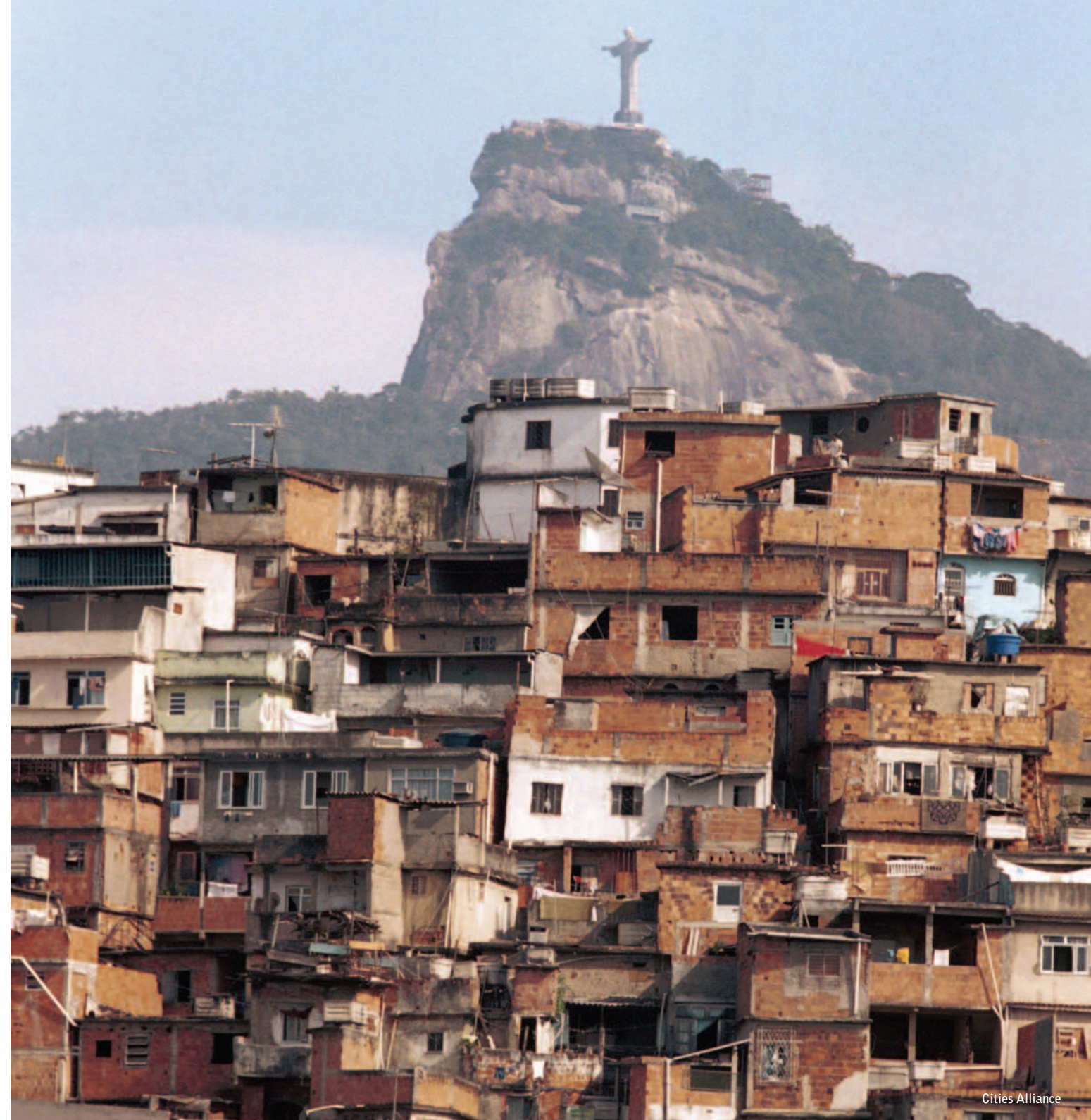
Based on IMF data; figures for late 1990s.
Source: Tannerfelt and Ljung, *More Urban Less Poor*, Table A.11.

Land Rights, Management, and Regulation

Getting land policies “right” is frequently cited as the single most important contributor to balanced and equitable urban development for all elements of the population. Several different policy elements come under this umbrella. Secure land tenure is the most often discussed. Confidence in land rights has been shown to affect the investment that poor households will make in their dwellings and informal businesses on their premises. Despite wide recognition of this point, progress in granting and registering secure land rights is slow in informal settlements and even in upscale areas in some countries—just ten percent of urban properties are registered in Egypt, for example. In part this is because the documentation required to prove plot ownership for a conventional title to be granted is too expensive and complicated for most informal settlement residents. It is generally recognized that a range of less costly intermediate instruments can serve well, as has been successfully demonstrated in countries as diverse as Kenya and Bolivia. Buckley and Kalarickal, in their 2006 publication, *Thirty Years of World Bank Shelter Lending: What Have We Learned?* list the following examples: declarations of possession and future use rights in Colombia; housing permits in francophone Sub-Saharan Africa; certificates of comfort in Trinidad and Tobago; credit contracts in Bolivia; certificates of rights in Botswana; concession to the real right to use in Brazil; community land trusts in Kenya; temporary occupation licenses in India and Kenya; communal ownership in South Africa; and, land rentals in Thailand.

Land management and regulation are also critically important. One component is land use zoning, particularly a system that operates flexibly to accommodate necessary changes in land use in central areas as the city develops.²¹ As access to the center becomes more valuable, increased population densities in the same formal neighborhoods are striking. Amman, Jordan, for example, has undergone such transformations over the past 50 years. Efficient development of housing for the poor requires realistic standards for rights-of-ways, pavement standards, plot sizes, construction materials, and utility services so that dwellings can conform to the rules in a way that is affordable to most families.

Finally, affordable fees for registration and other real estate transactions are key to achieving widespread adoption of property registration and the reporting of accurate sales prices. For instance, if fees are computed as a percentage of the price and the rates are high, there exist strong incentives to underreport values. Some of these policies, e.g., zoning rules, are generally under local control. In contrast, in many countries property registration requirements and fees are set at the national level, making it difficult for reforming municipal governments to improve policies independently. It is encouraging that national governments are increasingly recognizing the impediments caused by high fees—Egypt cut its registration fees dramatically in 2006, for example, and Rwanda did so in 2008.



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