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**Political Accountability, Fiscal Conditions, and  
Local Government Performance – Cross-Sectional  
Evidence from Indonesia**

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**Political Accountability, Fiscal Conditions, and Local Government  
Performance –  
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***Abstract:** What makes governments tick? Why are some public institutions more successful than others in managing resources and delivering services? And even more vitally, how can malfunctioning institutions be reformed so that they perform their responsibilities more effectively? This paper contributes to our understanding of these overarching questions by exploring the interactions between political institutions and public sector performance in the context of decentralization and local governance. It shows -both theoretically and empirically- that performance outcomes are determined by the extent to which people can hold their governments accountable through political institutions. The basic hypothesis underlying this research is that political accountability, either by encouraging sanctions upon non-compliant public agents or simply by reducing the informational gap regarding government activities, will create forceful incentives for elected officials and civil servants to reduce opportunistic behavior and improve performance. Using a cross-sectional regression the hypothesis is empirically tested against evidence from newly empowered local governments in Indonesia. The empirical findings broadly support our hypotheses. Improved public services on the ground, both in terms of quantity and quality, require informed and well functioning decision making processes that allocate resources to priority areas that meet the demand of the broader community.*

**Key words:** governance, public services, fiscal decentralization.

**JEL codes:** D2, D7, H2, H7, O1

## 1 Introduction

What is the impact of decentralization reforms on local government performance and public service delivery? What role do political institutions and incentives play in shaping local government outcomes? This paper will contribute to the understanding of these overarching questions. Recent decentralization reforms substantially differ from pure administrative and fiscal deconcentration or decentralization in that they evoke more than a downward delegation of resources and authority to lower organizational levels within the public sector. They also imply a transformation of key political accountability chains between state institutions and the society (Blair (2000), (James Manor and Richard Crook, 1998) and (Richard Crook and James Manor, 2000)). Most importantly, democratic decentralization is supposed to create external links of political accountability between local governments, the public sector and the community. The local public sector becomes part of democratic system of checks and balances (usually in its electoral, representative form), and the local public administration consequently becomes formally responsible to a locally elected mayor or assembly. Democratic decentralization has become a global trend in recent years. Alongside with moves to more fiscal decentralization many developing countries have engaged in political devolution and have made local governments accountable through local level forms of electoral and representative democracy. Whereas in 1980 only 10 of the 48 largest countries in the World had elected sub-national governments, this number increased to 34 in 2000 (UNPAN, 2000). Recent legislations on decentralization, such as the Philippine Local Government Act enacted in 1991, the local government transition acts of 1993 and 1996 in South Africa, and Indonesia's decentralization law of 1999 and 2004 typically spell out rules for the power and roles of elected representatives as well as basic accountability relationships at the sub-national level (Worldbank, 2005). The working of local politics and political institutions become critical with these changes. Democratic decentralization must not only empower local governments through increased resources and responsibilities but simultaneously build responsive governance systems that ensure that they are held accountable downwards for delivery of public services (James Manor, 1999), (Hans Binswanger, 1999) (Richard Crook and James Manor, 2000) and (Worldbank, 1997a).

Against this background, this paper will empirically investigate causes of variations in the performance of newly empowered—democratic—local governments in Indonesia. To what extent have various local governments been able to manage the greater political responsibilities and revenue flows they have been granted under decentralization? Why are some local governments more effective than others? Although the method of this study is empirical, part of its intention is of a more theoretical nature. The principal hypothesis asserts that the performance of local governments is to a significant extent determined by the effectiveness of political accountability systems ensuring public control of government actions. In understanding the causal relationship between the reconfiguration of local political institutions underlying decision-making processes and the performance of local governments.

## **2 Relationship to the literature**

The functioning of democratic local governments has long merited attention in both the theory and practice of public policy (Matthew Andrews and Anwar Shah, 2003), (Diana Mitlin, 2000), (Harald Fuhr, 1999), (William Dillinger, 1994). Decentralization—the devolution of political authority, responsibilities, and public resources—to lower levels of government is still enthusiastically praised as an effective remedy in the reform of governance systems, particularly in developing countries (William Dillinger, 1994). As Andrews and Shah (2003) point out

“Decentralization is common in many developing countries. Local governments are becoming numerous in such countries and are increasingly required to play larger roles in providing services, alleviating poverty, and facilitating development.”

The existing theoretical and applied literature offers some strong arguments in favour of decentralization policies. Most importantly, decentralization should help to increase responsiveness, effectiveness and efficiency of the public sector. In this perspective decentralization is seen as a way to overcome informational constraints and align incentives in a political system. First, the empowerment of local governments is supposed to bring authorities in more direct contact with citizens and to increase accountability and the responsiveness of public services to local preferences (allocative efficiency) (Wallace Oates, 1993) (Richard E. Wagner, 1983).

Second, decentralization enhances competition among jurisdictions, which compete through taxation policies, expenditure, public service provision, and regulatory policies for mobile firms and individuals. In this framework competition among governments creates “market-like incentives” for local governments to provide attractive combinations of public services and policies at competitive local tax rates (productive efficiency) (C. Tiebout, 1956). Third, in addition to economic benefits, today’s decentralizers are motivated by generically political objectives. As Fuhr (1999) has argued, the recent wave of decentralization starting in the 1980s can be seen as a response to the declining political legitimacy of state centred, highly centralised models of governance and fiscal policies. Increasing the public sector’s political accountability and legitimacy is therefore ranked high on the political agenda in and of itself in many areas where decentralization policies are pursued today.

In sharp contrast to these theoretical claims is at least part of the empirical evidence—particularly from developing countries. Bird, Ebel, and Wallich (1995) present evidence from Eastern and Central Europe and suggest that public services can suffer as a result of decentralization, at least in the short run. In a similar vein, Crook and Sverrisson (1999) have provided evidence that despite extensive strides of devolution of authority and resources to democratically elected local governments, decentralization in Colombia, West Bengal, and Brazil has achieved little in improving service delivery. Focusing on local governments in urban areas of developing countries, Mitlin (2000) comes to the conclusion that by and large “[...] local governments fail to meet many of their responsibilities to large sections of the population within their jurisdiction.”

Why is it, then, that decentralization—more often than not—does not live up to the expected benefits? A number of recent studies suggest that the outcome of decentralization policies crucially depend on the extent to which central management is replaced by democratic institutions ensuring that the community can exercise control over government affairs at the local level. A World Bank Study on the topic concludes: “decentralization of resources and responsibilities without [...] political reforms would have been incomplete and, probably, not conducive to socially effective results.” (Worldbank, 1995) Clearly, giving authority to local governments that are not responsible to their local populations may not improve outcomes. If

political accountability is incomplete, decentralization may in fact create powerful incentives for local elites to capture the local political process and divert public resources to match their own aspirations rather than those of the broader community. In this case decentralization implies a power shift from central to local elites rather than improvement of the external political accountability of the public sector (P. Bardhan and Dilip Mookherjee, 1999) and (Dilip Mookherjee and P. Bardhan, 2000). On similar grounds, (Arun Agrawal and Jesse C. Ribot, 1999) state: “It is only when constituents come to exercise accountability as a countervailing power that decentralization is likely to be effective.”

A number of more contributions have explicitly focused on the costs of political aggregation technologies and accountability in the trade-off between centralised vs. decentralized provision of public goods. (P. Seabright, 1996) argues that accountability is a priori higher at the local level, since citizens who are better informed about government performance can vote these governments out of office. In national elections voter’s decisions are driven partly by assessments of government performance in other regions and of national policies. As result accountability is diffused and the potential for rent extraction and inefficiency increases. The model provided by (B. Lockwood, 1998) points in the same direction. (Mariano Tommasi and Federico Weinschelbaum, 2003) use a common agency framework to model the trade-off between scale effects of public policies favouring centralised modes of government and a cost advantage in controlling the government favouring decentralized modes of government, but they do not test their model empirically.

Another strain of literature has explored the political economy of public control of government action. In a general account, (Torsten Persson et al., 1997) examine how the separation of powers can affect political accountability of governments. They show how voters can combine electoral incentives with institutional checks and balances to control moral hazard and reduce politicians’ rents under different constitutional regimes (presidential, parliamentary, etc). (Timothy Besley and Stephen Coate, 1997) provide an econometric model of parliamentary democracy focusing on the selection of candidates and show how political competition affects accountability. (Timothy Besley and Robin Burgess, 2001) propose a political agency model showing how information flows and participation affect the government’s

decision to respond to citizens' needs or not. Their model suggests that both transparency and participation increase the political cost of not –responding, thus creating incentives for the government to be more responsive. Testing their hypothesis on panel data from Indian states, they find supporting empirical evidence for their model.

The existing literature suggests that management of local government officials' political incentives and the existence of institutions fostering local accountability of governments are necessary preconditions for effective local government performance—and thus for the success of democratic decentralization. Nevertheless, most of the existing theoretical and empirical research has dealt with the impact of intergovernmental administrative and fiscal relations on the performance of the governance system as a whole. Insufficient emphasis has been paid to the varying patterns in the adjustment of local accountability systems to the new institutional environment created by decentralization policies, e.g. the transformation of accountability relationships and their impact upon local government performance and public service delivery. The unfinished research agenda in the theory and practice of decentralization thus demands the exploration of how exactly local accountability systems are transformed (or created) and how they in turn affect local government performance and public service delivery.

### **3 Linking Accountability and Performance**

Based on these preliminary considerations the hypothesis that will be tested in this research holds:

H: The degree of local governments' political accountability to their constituents has a critical impact on their performance in delivering public services. Government performance is expected to be a function of the degree of political accountability in given district.

The hypothesis relies on the basic argument that mechanisms that increase political accountability, either by encouraging sanctions upon non-compliance of public agents or simply by reducing the informational problem related to government activities, will create forceful incentives for elected officials and civil servants to reduce opportunistic behaviour and improve public service provision, thus enhancing performance. Based on this hypothesis, we expect local administrations with higher

degrees of political, external accountability to exhibit higher levels of performance in service delivery in the empirical analysis. In turn, I expect that cases of poor public service delivery to be associated with political market failures, e.g. malfunctioning political accountability mechanisms.

Accountability has been identified as a key variable influencing the outcomes of democratic decentralization reforms. More generally, it also has become a key concept in public sector operations and administrative reforms. (B.G. Peters, 1996) even concludes that accountability “has been a dominant, if not the dominant, concern for the designers of democratic systems.” In a similar vein, the World Development Report 2004 places accountability succinctly at the centre of public sector reform and public service delivery (Worldbank, 2003b). In the context of Indonesia’s decentralization policy, Hans Antlöv, has argued that “the missing figure in the equation is accountability and public control over decision-making.” (Hans Antlöv, 2002)

Not surprisingly—as with many fashionable concepts—the notion of accountability has been defined slightly differently by various authors (Robert O. Keohane, 2002); (Bernard Manin et al., 1999); (Andreas Schedler, 1999); (Ronald J. Oakerson, 1989); (Amy Guttmann and Dennis Thompson, 1996); (Jesse C. Ribot, 2002), (R. Manasan et al., 1999). However, most definitions share three essential features. Firstly, accountability is thought of as an inherently relational term: a person or organization has to be accountable to someone else. Secondly, accountability includes the obligation of actors that are accountable to provide information and explanations for their actions. And thirdly, accountability requires the ability of those to whom these actors are accountable to apply sanctions when these actions are deemed unsatisfactory. Essentially, questions of 'who is accountable to whom and for what' are at the heart of all concepts of accountability (C Scott, 2000).

[Figure 1 about here]

Accountability prevails in very different kinds of organizational relationships within the public sector and between the public sector and the community. The existing literature offers several typologies, dimensions, and components. For example, (Barbara Romzek, 2000) distinguishes between political, bureaucratic, legal, and

managerial accountability. The 2004 World Development Report (WDR) presents a simple yet compelling integrated framework for the analysis of accountability relationships between citizens, politicians, and service providers and their effects on service delivery (Worldbank, 2003b). As shown in Figure 1 public sector accountability can be schematically thought of as a triangular model. With regard to service delivery the WDR framework distinguishes between “the long route of accountability” or “voice” that implies accountability of elected representatives and their ability to channel community demands through to the service providers and “the short route of accountability” or “client power” which implies direct accountability of service providers to their clients.

The focus of this research is on the long route of accountability. In the taxonomy of Romzek this can essentially be thought of as political accountability circumscribing the relationship between the demand and supply side of political markets. Political accountability measures the degree to which the community can control (hold accountable) the behaviour of public agents through political institutions. I follow the definition provided by the (Worldbank, 2000a):

“Political accountability refers to the constraints placed on the behavior of public officials by organizations and constituencies with the power to apply sanctions on them. As political accountability increases, the costs to public officials of taking decisions that benefit their private interests at the expense of the broader public interest also increase, thus working as a deterrent/disincentive to corrupt practices.”

In this sense, political accountability refers to specific conditions within the political system under which citizens (acting indirectly through the competition and cooperation with their representatives) have the ability to demand answers from agents within the public sector about their proposed or past behaviour, citizens’ ability to discern that behaviour, and to impose sanctions upon the public sector in the event that their behaviour is believed to be unsatisfactory by the citizens (Robert O. Keohane, 2002) and (Phillippe Schmitter and Terry Lynn Karl, 1991). Operationally, political accountability requires citizens to delegate authority to their political representatives and to hold them accountable through voting and political pressure. By passing laws and directives and by providing finance and other resources, the

elected representatives in turn trust the bureaucracy and service providers to carry out public policies and provide services to the community. The accountability of the executive to elected representatives is enforced through monitoring and oversight and the imposition of rewards and penalties (Worldbank, 2003b). In this understanding political accountability refers to mechanisms ensuring that public agents engage in collectively rational and representative actions.

Political accountability is understood as sets of various accountability mechanisms and their influence in the relationship between the community and the government (Robert O. Keohane, 2002), (Worldbank, 2003b). They consist of formal political institutions (elections, division of power) and sets of rules that govern monitoring and public control of the government in order to connect government officials' individual interests and community aspirations. While these formal accountability structures are important, they are only enabling factors that might not ipso facto produce political accountability, depending on the social context in which they operate. In addition, we need to look closely at the functioning of these institutions and focus on the actors involved, who controls decision-making, and how citizens are mobilized and included in political processes. In sum, it is necessary to comprehend "how people and issues are politicized" (O. Törnquist, 1998). Therefore, the study will include both institutional structures (electoral rules, oversight mechanisms, participatory institutions, etc.) and the practical functioning of these structures in effectively governing accountability relationships and behavior (transparency, electoral competition, political distortions, elite capture, informal practices, etc.).

#### **4 Empirical Backdrop**

In order to empirically investigate these questions I have chosen Indonesia's most recent move to decentralization as a case study. The decision to restrict the empirical context to a one-country setting and to employ an "in case comparison" was driven by the ability to control for a number of variables that potentially intrude with the effects of accountability on local government performance. Accountability is embedded in the broader political, institutional, economic and social context of a country. The design of local government institutions varies greatly across countries in terms of revenue and expenditure assignment, balance of power between local and central

government, the political and organizational setup of local governments and overall institutional development. Moreover, local government operations are also linked to the economic situation of given country, which will determine access to both financial and human resources. While such variations also exist in a one-country setting, there are likely to be more significant in a cross-country comparison. As Wildasin (1997) rightly asserts: “If it is difficult to appreciate fully the importance and interactions of all of these factors for any single country, it is probably impossible to do so for many countries taken together.”<sup>1</sup> In contrast to cross-country research, I examine conditions for effective local governments against the background of the principally uniform decentralization policy in Indonesia.

Why Indonesia? In recent years, Indonesia has made remarkable progress in creating a decentralized system of governance. Since the 1999 decentralization laws (Law 22/1999 and Law 25/1999) were enacted, local governments have assumed responsibility for vital government functions; more than 2.5 Mio. civil servants were reassigned (largely to the district/city level government); the central government has continuously increased the pool of resources transferred to sub-national governments in relative and absolute terms; a second round of democratic elections took place in 2004 in a credible fashion at both national and sub-national levels; and now all sub-national governments are headed by democratically elected mayors/regents or governors. Without doubt these reforms promoted unprecedented changes in the way local governments operate across Indonesia.

Indonesia’s decentralization policy neatly reflects the concept of democratic decentralization. As suggested by the concept of democratic decentralization, decentralization fundamentally altered the institutional environment in which political authority is executed in Indonesia (B. Hofman and K. Kaiser, 2002). In particular Law 22/1999 prompted a major reorganization of political accountability chains. First, it eliminated the hierarchical relationship between the central, provincial, and local governments. In a break from the past, the mayor and district government officials are elected by and responsible to the locally elected assembly (DPRD). Second, for

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<sup>1</sup> (David E. Wildasin, 1997), p. 14.

locally assigned responsibilities, the branches of sectoral ministries in the districts were transferred under the jurisdiction of local governments.

As elsewhere, decentralization was accompanied by hopes and fears. Proponents of decentralization promised to bring government closer to the people resulting in better governance, enhanced accountability and performance of local governments. In line with long standing theoretical propositions local governments were expected to tailor public goods and services to the particular preferences and circumstances of their constituency thus increasing community welfare. At the same time, more critical voices were concerned that decentralization could increase the extent to which local elites are able to capture resources and re-orient policies (and resources) to serve their private interests rather than those of the broader community. In the absence of transparency and accountability at the local level it was feared that decentralization would bring about corruption, the rise of “little kings” (or Raja Kecil) in the regions and degradation of services formerly delivered by the central government.

It is likely that both views contain grains of truth. In Indonesia, as in many other countries pursuing large scale decentralization reforms, examples of both phenomena exist simultaneously (Asia-Foundation, 2002). Local government performance increasingly varies depending on the extent to which local government took advantage of the opportunities offered by decentralization. A significant number of local governments have forged ahead with reforms and became the locus for innovative forms of governance and better public services. Elsewhere, however, local political contexts became charged with malfeasance, fraud, lack of accountability and failure to respond to the needs of local residents (Asia-Foundation, 2002); (I. Saad, 2001). At the same time there is plenty of anecdotic evidence that suggests that key political accountability mechanisms are only weakly developed in some of the newly empowered local governments (Micheal S. Malley, 2003); (Vedi R. Hadiz, 2003); (K. Kaiser and B. Hofman, 2003). Allegations of vote-buying and political corruption surround elections of many mayors as well as the annual accountability reports they must submit to the local legislature (Worldbank, 2003a). This suggests that decentralization policies do not have a uniform impact on local governments but rather lead to a differentiation process (with regard to both performance and level of accountability) across localities that are adapting in different ways to the new

institutional environment. The principal aim is to understand how these different outcomes are brought about and if accountability and performance outcomes are interconnected.

## **5 Empirical Model**

The primary empirical units of analysis in my research are local governments in Indonesia. The period of examination spans the first four years after decentralization was fully implemented across Indonesia from January 2001 to the end of 2004. I thus focus on initial responses rather than long-term effects of decentralization policy. As in many policy analyses, my attention and curiosity was drawn to the immediate dynamics that were unleashed by this major reform attempt.

One of the key methodological problems that I faced in conducting this research was the measurement of the variables in question. Both concepts—government performance and political accountability—are rather elusive; and measuring or observing these variables poses considerable difficulties to the researcher. The specific measurement problems are linked to both, reasons rooted in the nature of the public sector operations and to the sheer practical problem of data availability. Compared to most parts of the private sector, performance measurement in the public sector is fraught with intricacy (H. O. Fried et al., 1993, P. Pestieau and H. Tulkens, 1993); (A. de Silva, 1999) (Matthew Andrews and Anwar Shah, 2003); (M. Estrella, 2001); (Norman Uphoff, 2003). There is no agreed upon, readily available set of indicators to measure the performance of public institutions (similar to profit margins, market share, productivity, etc. to measure the performance of private companies). In sum, public sector performance cannot be assessed by reference to some notional “bottom line.” Estimating meaningful quality-adjusted cost and productions functions is impossible for most part of public service delivery. In practice, this has often led to the application of several parallel criteria in the assessment of performance, including various perception-based indicators.

An equal difficulty arises in measuring my hypothesized key determinant of performance. Political accountability is a lofty goal, and no numerical measurement adequately captures the aspirations associated with the term (David Beetham, 1994). While it is possible to observe and thoroughly describe the formal framework of accountability relationships at least in the form of qualitative institutional analysis, considerable difficulty arises in operationalizing variations in the functioning of these

mechanisms. The complex social processes and interactions underlying effective political accountability can only be measured through the use of proxies like data derived from both citizen and expert surveys.

Employing a dataset covering a randomised sample of 177 districts, quantitative indicators for both the dependent variable (performance) and the explanatory variable (political accountability) will be derived. The dataset relies heavily on data collection work carried out by the World Bank Indonesia and on previous statistical analysis carried out by Kai Kaiser and Bert Hofmann of the World Bank, part of which is presented in (K. Kaiser and B. Hofman, 2003) and (Worldbank, 2003a). Large parts of the data come from the Governance and Decentralization Survey (GDS) that was fielded by the World Bank Indonesia in conjunction with the Centre of Public and Policy Studies at Gajah Mada University during 2002 as part of a larger effort to empirically understand the process of decentralization in Indonesia. The survey used a multi-stage randomisation process to create the sample of districts, sub-districts, villages, and respondents across Indonesia. The sampling ensured representativeness at both the national and the district level. In each of the sample districts, about 60 households were questioned using structured questionnaires covering household perceptions of various issues relevant to the analysis. In particular, the questionnaire included questions about perceptions of the quality of public services, perceptions of the workings of various political processes (elections and accountability speeches), participation, transparency, and the like. The GDS also included a limited number of interviews with members of local representative councils, the administration, representatives from the local media, and NGOs. In addition to these survey data, district-level fiscal and socio-economic data were included into the dataset. The fiscal data was retrieved from the Regional Finance Information System (Sistem Informasi Keuangan Daerah, SIKD). The socio-economic data are based on census data (SUSENAS) that is conducted annually by the Central Statistical Office (BPS).

Building on the principal hypothesis we posit that two broad factors are likely to influence the variation of performance across Indonesia's districts, as described by the following general equation:

$$P_{it} = f(A_{it}, FC_{it}) \quad (1)$$

This equation is a recapitulation of our general hypothesis. It suggests that the performance in a given district  $i$  at the time  $t$ , denoted as  $P_{it}$ , is a function of the level of political accountability and fiscal conditions in a given district  $i$  at the time  $t$ , denoted  $A_{it}$ , and  $FC_{it}$  respectively.

In order to estimate the causal relationships between performance and explanatory variables the general hypothesis is translated into the following linear regression model:

$$P_{i,t} = \beta_0 + \beta_1 \times A_{i,t} + \beta_2 \times FC_{i,t} + \varepsilon_{i,t} \quad (2)$$

where  $\beta_0$  (constant),  $\beta_1$ ,  $\beta_2$  are the parameters to be estimated and  $\varepsilon_{i,t}$  denotes the error term or unobserved effects to account for factors affecting performance (e.g. the pre-existing level of infrastructure, staffing levels, staff education, etc.) that are not available in our data.

## 6 Measuring Performance Improvements

The indicator measuring performance of local governments (dependent variable) employed in our empirical model is an index constructed from perception data measuring perceived changes in the quality of basic public services among households in each sample district as of 2002. The services in question included education, health service centres, and district offices. Specifically, respondents were asked whether these types of services had improved in 2002 compared to 2000. The use of perceived improvements (instead of simple satisfaction ratings) eliminates the effect of different qualities (and corresponding differences in the satisfaction ratings) at the outset of decentralization and focuses on changes that occurred since decentralization.

[Figure 2 about here]

What do household perceptions tell us about changes in the quality of public services since decentralization? In sum, the descriptive statistical evidence on perceived changes in public services suggests two findings. First, services seem to have

improved in the eyes of a large majority of household respondents. Decentralization apparently did not lead to a breakdown in services at the local level, as was feared by some observers, but sparked considerable improvement in reported satisfaction with services. As can be seen from Figure 2, the survey results draw quite an optimistic picture of the effects of decentralization. Two years after the big bang, the overwhelming majority of respondents perceived public services to either have remained the same or to have improved as compared to the period before decentralization. The highest rankings occurred in the health and education sector. As indicated by Figure 2, on average more than 40 percent of the questioned households reported improvements with regard to education and health services, for district offices. Only a small fraction of respondents perceived deterioration in the quality of the public services.

Second, despite this overall positive tendency, there are quite significant variations across districts, as illustrated by the radar diagram in Figure 3. In the districts that performed best according to the survey results, depending on the type of service, between 75 and 80 percent of all respondents reported improvements since decentralization. This compares to 1.6 and 15 percent (depending on the type of service) in the districts that performed worse according to the survey results.

[Figure 3 about here]

**Table 1 Net-Responses of Perceived Improvements in Public Services since Decentralization**

(Respondents reporting improvements, Percentage per District)

	Max	Mean	Min	Standard Deviation
Schools	78.3	40.2	-8.3	14.1
Health Centres	81.7	38.3	0.0	14.4
District Office	76.7	27.4	1.6	14.1
<b>Service Satisfaction Index</b>	<b>78.8</b>	<b>35.8</b>	<b>6.6</b>	<b>12.9</b>

**Source:** GDS 2002, Question HH RD7. N=150. Own Estimations.

**Note:** Standard Deviation refers to sample not to population.

Based on the survey responses we calculate a simple service satisfaction index for each district. We first subtract the percentage of respondents observing services

having worsened from the percentage of respondents reporting the respective services having improved in the given time span in order to receive net responses of improvements for each individual service per district. Then, we calculate the service satisfaction index as the cross-sectoral district average of all individual ratings. Table 1 reports descriptive statistics for both the individual services and the cumulative index. The standard deviation for perceptions of each type of service that is reported in the last column underlines a quite dispersed distribution of these variables. While there are also some notable cross-sectoral differences between perceptions of services in education, health sector, district offices, etc., the cross-district or spatial variation of the data is more significant. Moreover, ratings of the individual types of services are highly correlated for each district. As indicated by Table 2 bi-variant correlations yield correlation coefficients in the range between  $R=0.620$  and  $R=1$ . This implies that districts tended to consistently score low respectively high with respect to all measured service sectors. This suggests that variations in the perception of services are caused by underlying district characteristics rather than differences across sectors.

**Table 2 Cross Correlation between Service Scores**

(Pearsons Correlation Coefficient)

Variable		SSI	EDUS	BUPS	HEAS
Service Satisfaction Index	SSI	1	0.726**	0.726**	0.700**
School-Score	EDUS		1	1.00**	0.812**
Bupati Office-Score	BUPS			1	0.812**
Health- Score	HEAS				1

\*\* Significant at 1 percent level.

To test the reliability of our scale we assessed both internal consistency and dimensionality. Consistency and dimensionality must be assessed separately. If a test is uni-dimensional, then it will show internal consistency. But if a test is internally consistent, it does not necessarily entail one construct (Jeffrey M. Wooldridge, 2000). We have first conducted a Cronbach's Alpha test to check the internal consistency of our measurement scale yielding an alpha coefficient that is higher than 0.90, sufficiently high to let us conclude that the scale has internal consistency. Second, we

applied factor analysis, specifically principal component extraction to test unidimensionality of the scale, confirming our construct.

Checking the validity of the index and its components is more difficult. We have first correlated the SSI and its components with similar ratings of police services (another item from the GDS survey data). Since the police is one of the areas that were not decentralized we expect ratings of this service to be only weakly correlated to district performance, hence the SSI and its components, which is indeed the case. Some cautionary remarks are, however, with regard to the validity of the index in measuring underlying differences in the performance of local governments. The nature of perception based indicators might cause some problems. In fact, the overwhelmingly positive responses shortly after decentralization came into effect suggest that respondents might have a positive bias in their assessment of services. Positive perceptions might reflect causal factors other than service improvements induced by the decentralization policy. Respondents might, for example, be inclined to perceive positive changes because of an improvement of both public services and general living conditions, as Indonesia is recovering from the economic crisis in the late 1990s. Even if there is such a positive bias in the perception data, however, we can assume that it is evenly distributed across all districts. It thus does not hinder a cross-sectional comparison that is the main intent of this study.

## 7 Measuring Accountability and Fiscal Conditions

Consistent with our general theoretical proposition, we attempt to include a number of indicators into the equation that measure variation in the political accountability of local governments. To capture differences in the effectiveness of local elections as means to create political accountability I constructed two indicators to measure the nature of political competition across districts, based on the outcomes of the 1999 general elections. The first measures the party fragmentation of the local council (POLF). The indicator is the calculated probability that two randomly selected council members belong to the same party faction.<sup>2</sup> In order to make the analysis more

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<sup>2</sup> The index is constructed by the following formula:  $POLF = 1 - \sum_i^n p_i^2$  where p denotes the share of party i in the total membership.

elegant (higher values correspond with higher fragmentation), the scale of the index is reversed so that the index varies between 0, denoting full fragmentation and 1, denoting no fragmentation. The direction of the causal effect is difficult to predict since higher party fragmentation could result in stiffer competition (positive effect) or paralysis and dispersion of accountability (negative effect). I also included the percentages of votes the five major parties gained at the local level to see whether the strength of certain political parties is associated with certain service outcomes. Finally, I included the share of female representation in the local council (FEMREP). This indicator is expected to positively impact upon the quality of services, since higher female representation is associated with more representative structures.

To measure differences in the functioning of legislative oversight I introduced an indicator based on the percentage of households perceiving incidents of corruption in the annual accountability report delivered by the Bupati to the council (ACCOR). I expect this indicator to be negatively correlated with the performance indicator, since distortion in legislative-executive relationships will undermine the oversight function of the council. I also include a dummy variable depending on whether a regional head had been elected by the DPRD in 2000 or 2001 (BUPATI) rather than being appointed by the central government. Since I expect heads that are elected by the councils to be more responsive horizontally than those that were appointed by the central government, I predict a positive correlation with perceived improvement of public services for this indicator.

Measurement of differences in the access to information across districts is approached from two sides. First, I constructed a measure of the share of local households that reported that they follow local government elections to capture differences on the demand side of information (TRANS1). Second, from GDS 2002 media respondents I constructed a dummy measuring the presence of local media to capture difference with regard to the supply side. The dummy is 1 if two or more of the media respondents reported growing local media since decentralization (TRANS2). Since a more informed community and greater presence of local media are expected to increase accountability positive effects are predicted for both variables. In order to

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measure community participation in public activities I included the percentage of self-reported household attendance in health planning meetings (PART1). Since greater direct participation of the community in government affairs should increase accountability the causal effect is expected to be positive.

Since fiscal conditions, spending levels, and revenue and expenditure structures are expected to impact the performance of local governments, a number of variables capturing the most salient fiscal conditions are included in the analysis. All fiscal data refer to FY 2001, the first year after decentralization and one year before the fielding of the GDS survey. On the expenditure side, I control for total per capita expenditure, including routine, civil servant wage, and development expenditures (PCEXP). Higher spending levels are expected to increase performance. In addition, the percentage of the budget spent on wage outlays is also included (SHWAGE). Higher wage bill pressure (lack of public investments) is expected to be associated with lower performance. We also include a measure of the combined share of education and health development spending to capture whether differences in spending priorities affect satisfaction with services. Higher percentages of spending on health and education are expected to lead to higher satisfaction. On the revenue side I included the share of the general allocation grant in total revenues (SHDAU). Higher shares of transfers are expected to be associated with lower performance.

Table 3 presents descriptive statistics of the explanatory variables. A brief look at the data suggests an impressive variation with regard to the local conditions of political accountability and performance.

**Table 3 Descriptive Statistics of Explanatory Variables**

Variable		Max	Mean	Min	Standard Deviation	n
Share of Household perceiving political corruption in local elections (%)	ELECOR	98.3	30.5	0.0		18.0
Political Fragmentation of DPRD	POLF	0.86	0.71	0.24		0.13
Share of Households perceiving political corruption in accountability report (%)	ACCOR	73.3	19.1	0.0		14.7

Percentage of Citizens following local elections (%)	TRANS	100.0	56.0	7.0	0.22
Share of Households reporting attendance in health planning community meeting (%)	PART	48.0	14.6	0.0	9.2
Local Per Capita Expenditures ('000 Rp.)	PCEXP	3,962.58	632.2	187.8	632.6
Share of Wage Bill in Local Expenditures (%)	SHWAGE	97.0	54.5	3.0	19.3
Share of DAU in total expenditures (%)	SHDAU	93.3	72.9	14.5	16.4

**Source:** GDS 2002, SIKD, N=177.

**Note:** Standard Deviation refers to sample, not to population.

With regard to the functioning of the electoral process, perceptions of corruption in the local elections varies from no respondents reporting corruption in the districts with the lowest score to 98.3 percent of all respondents reporting incidents of corruption in the district with highest scores (ELECOR). This suggests a great cross district variation in the functioning of this key mechanism of political accountability. Both political fragmentation and the share held by the majority party in the council do vary quite significantly. Transparency and community participation variables also suggest significant cross-sectional differentiation. The share of informed citizens seems to vary with an impressive magnitude. While on average 56 percent of the GDS respondents reported they followed the local election, communities in some districts seem to be more informed than in others. In the district with the highest score, 100 percent, respondents said they are informed about local elections, whereas only 7 percent of the respondents did so in the district with the lowest score (TRANS1). Community participation, as measured by attendance rates in local health planning meetings, also shows deviation, ranging from none household reporting attendance to almost half of respondent reporting to have attended a planning meeting during the previous year (PART).

Finally, decentralization has resulted in vast comparative differences in the fiscal condition Indonesian local governments. Per capita spending in 2001 ranged from roughly IDR 187.000 to IDR 4M (PCEXP). With regard to the expenditure structure, differences of similar magnitude are revealed. Whereas the civil servant wage bill consumes 97 percent of the budget in the district with highest salary outlays, it only

accounts for 3 percent in the district with the lowest (SHWAGE). The variation in the importance of the general allocation grant (DAU) as a revenue source, ranging from over 90 percent to around 15 percent, reveals similar differences with regard to the revenue side of local budgets (SHDAU).

## 8 Explaining Performance: Empirical Results and Hypotheses

Did differences in local conditions for political accountability relate to differences in the performance of the local governments? In order to develop a better understanding of how the variables are correlated I estimated several variants of equation (9) for the cumulative service satisfaction index across the sample of 177 districts, using a simple OLS estimation. We have applied a number of standard procedures to check for the presence of heteroskedasticity and functional form misrepresentation in our models. As can be easily seen from the bivariate plots presented in figure 4, heteroskedasticity seems to be an issue in some of the bivariate correlations but running the error plots against predictor variables in the multivariate models indicated that heteroskedasticity is not present in multivariate models (I-IV). To be sure we applied the standard White test to all specifications of the model and found that heteroskedasticity is not an issue in the multivariate models. In addition, we have conducted regression specification error tests (RESET) for all models. As suggested by (J.B. Ramsey, 1969) we added quadratic and cubed terms of the predicted values of the dependent variable yielded by the initial regressions as explanatory variables to the equations and applied F-tests to these. Since the results were statistically insignificant, no functional form representation could be detected.<sup>3</sup>

[Figure 4 about here]

Table 4 presents regression results for a range of core explanatory variables. The results for other variants of the model with the additional variables are not reported, since they were not statistically significant and do not change the general results.

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<sup>3</sup> RESET is a general test of functional form misrepresentation in multiple regressions. It is an F test of the joint significance of squares and cubes of the fitted values from the initial OLS estimation, denoted as  $\hat{y}^2$  and  $\hat{y}^3$ . Note that  $\hat{y}^2$  and  $\hat{y}^3$  are just non-linear functions of our explanatory variables. Specifically, the F statistic for  $\hat{y}^2$  and  $\hat{y}^3$  in specification I, II, III and IV yielded F= 0.55, F= 0.55, F=0.54 and F=0.55 respectively. All are well below the 10% critical value in the F distribution (2.3), indicating that  $\hat{y}^2$  and  $\hat{y}^3$  have no statistically significant relationship with our dependent variable. See Ramsey (1969) and Wooldridge (2000).

**Table 4 Regression Results for Core Explanatory Variables**

Independent Variable		I	II	III	IV
Share of Households reporting attendance in health planning community meeting	PART	0.349** (5.434)	0.386** (5.535)	0.380** (6.008)	0.412** (5.997)
Corruption in Accountability Speech	ACCOR	-0.288** (-4.499)		- 0.264** (-4.148)	
Political Fragmentation of DPRD (1999-2004)	POLF		-0.175* (-2.462)		-0.193* (-2.747)
Local Per Capita GDP	PCGDP	-0.196** (-2.878)	-0.179* (-2.418)	-0.161* (-2.498)	-0.149* (-2.139)
Local Per Capita Expenditures (LOG)	PCEXP	0.243** (3.380)	0.178* (2.285)		
Share of Wage Bill in Local Expenditures	SHWAGE			-0.278* (-3.586)	-0.219* (-2.653)
Share Development Expenditures (Education+Health)	SDE	0.125+ (1.893)	.065 (0.873)	0.038 (0.502)	-0.002 (-0.027)
(Constant)		-0.334+ (-1.797)	-0.093 (-0.436)	0.427** (9.467)	0.492** (7.645)
R-Square		0.344	0.249	0.350	0.257
Adjusted R-Square		0.325	0.225	0.330	0.234
F-Statistic		17.646**	10.491**	18.056	10.959*
N		173	163	173	163

Source: GDS 2002, SIKD, SUSENAS.

Note: Standardized coefficients \*\* significant at 99% confidence level; \* significant at 95% confidence level; +significant at 90% confidence level. T-statistic for H0: coefficient=0 in parentheses. F-Statistic for H0: coefficient=0.

How do the results relate to our hypothesis? The statistically significant results provide some support for the hypothesis that higher political accountability makes better service outcomes more likely. In particular, non-electoral participation, identified as one of the main pillars of local political accountability, seems to be associated with perceived improvements in public services since decentralization. Higher attendance rates in planning meetings correlate with higher reported improvements in public services. This effect remained statistically robust across all specifications. Whether or not we can attribute this effect to a causal chain between participation, more accountable governments, and therefore improved services can be

contested. The result might also be driven other factors. For example, participation might by itself change household perceptions of services, simply by providing more information about changes and improvements in service delivery. While we should be cautious in interpreting the results as causality in the strict sense, they still reveal interesting patterns.

Our proxy for transparency—the percentage of respondents informed about local elections—is also positively correlated with service perceptions, but the effect was not stable once other factors were taken into account. Conversely, higher measures of corruption in executive legislative relations are consistently associated with lower scores in the service satisfaction index, again holding across various specifications of the model. The use of perception based indicators to measure the extent of corruption calls, however, for caution in the interpretation of these results, since respondents might not sufficiently discern political corruption and service quality in their responses. I therefore included supposedly harder measures to capture the nature of local political processes. The political fragmentation index seems to be negatively correlated with perceived improvements in service quality in some specifications. Again, interpreting the result is not without problems, since higher party fragmentation in councils is presumably a reflection of underlying heterogeneity in political preferences that might drive differentials in perceptions (supporters of opposition parties might simply be more critical of services regardless of their actual quality). There might as well be a story about differences in political structures and consequently in the functioning of political competition behind the results. Presumably, more fragmented control in local councils—due in substantial measure to the unconsolidated party system—might disperse and therefore weaken political accountability and political incentives for the local governments to pursue the public interest.<sup>4</sup> This finding merits more attention in subsequent empirical research. The measure of female participation did not relate to differences in the service satisfaction index. Neither did the dummy on democratically elected regional heads seem to be significantly related to perceptions of public services.

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<sup>4</sup> This is confirmed by a significant positive relationship between the strength of the majority party the perceptions of services which suggests that more concentrated political power might lead to better outcomes (the result is not reported since the POLF and POLMAJ variables are highly correlated leading to multicollinearity problems).

Although inconclusive, the overall results suggest that the pre-institutional social conditions do impact upon the service performance of local governments. The results do not, however, provide general support to the hypothesis that more affluent, better-educated communities with more equal income distribution have better governments. While more extreme forms of poverty led to lower service scores, the general income level (per capita income) was in fact negatively correlated with the service satisfaction index, indicating that less developed districts experienced more marked improvements in services. The specific and multifaceted interrelationships between the level of economic development, poverty, distribution of income, accountability, and service perceptions need a more nuanced analysis.

Some of the measures for differences in fiscal conditions were related to variations in the service index. As expected, per capita expenditures did seem have a positive impact, albeit at a very low level. Expenditure structures seem to impact upon perceptions of service quality. Respondents in districts with lower wage costs were more likely to report improvements. Lower shares of the local budget spent on civil servant salaries were associated with higher service satisfaction indices. Excessive wage bills might create budgetary pressure that might restrain the government from needed investments in the improvement of services. Or conversely, lower wage bills are related to more fiscal flexibility: the government has more resources to its disposal to allocate to sectors of particular importance. Moreover, higher wage bills are presumably associated with lower infrastructure expenditures and part of the effect might be attributed to the fact that changes in infrastructure (new schools, rehabilitated health centre buildings, school books etc.) might be more visible to respondents than other characteristics of service quality (teacher/class ratios, number of doctors, etc.) and thus driving perceptions. At the same time, per capita expenditures and the wage bill percentage negatively correlated. It is difficult to discern the effects of these two variables, whether differences in service perceptions are driven by the level (higher per capita expenditures) or correlated differences in the structure of expenditures (lower wage costs and presumably higher capital expenditures). Differences with regard to the revenue side of the budget, namely the share of the DAU in total revenues did not yield significant results.

Taken together, the statistical results support our hypothesis.<sup>5</sup> Differences in the political accountability of local governments lead to differences in service perceptions. More open and participatory governments are associated with better service indicators. The nature of local political competition also seems to exert influence upon service performance. More fragmented party structures in the councils are associated with lower service scores. This finding provides a particularly interesting starting point for further analysis aimed at discovering how political structures shape incentives and political dynamics at the local level, and these in turn impact upon service delivery. Fiscal conditions on the other hand do also impact upon service indicators. Higher per capita spending is associated with perceived improvements in service delivery. The results also suggest that expenditure structures impact service performance. In particular, higher wage bills were related with lower service scores. The effects were, however, statistically weaker than the effect of the accountability variables.

There are a number of general methodological questions that need to be addressed in validating these empirical results. The overall explanatory power of the model is quite limited, in particular considering the number of explanatory factors included in the empirical model. The R-Square for our model (Rsq) which are reported in Table 4 vary between 0.249 and 0.350 depending on the specification of the model. This means the included explanatory variables together account only for between 25 and 35 percent of the variation of the dependent variable, or—conversely—more than half of the variation in the performance of local governments remains unexplained by the model. The most likely culprit for this lack of explanatory power is the high degree of complexity of the hypothesised causal relationships and the use of relatively noisy indicators in the analysis.<sup>6</sup> The quality of public services seems to be affected by many factors beyond our empirical model. These potentially include variations in the capacity of local governments; previous levels of staffing and resource endowments; skill level, attitudes, and education of administrative staff; and organizational differences in local governments. Despite these difficulties the regression results are illustrative of some of the variations in political accountability and public service improvement since decentralization, and how these factors might interrelate with each

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<sup>5</sup> Hypothesis 2 is not testable with the cross-sectional data. It would require time series data that are not yet available.

<sup>6</sup> In fact, adjusted correlation coefficients in the given range are typical for research

other at the local level. Future work should focus on devising more precise indicators (potentially harder outcome our output data) and addressing issues of causality between these two variables with more nuance.

## **9 Conclusion**

This research has attempted to understand, both theoretically and empirically, how diverse outcomes of decentralization policies are brought about. It placed an important emphasis on trying to apprehend how local political institutions and processes affect performance levels of local governments. On a theoretical level, the research has built on accountability view on political incentives and local government behavior to illuminate the conditions under which political agents at the local level find it in their interest to respond to community interests and to improve public service delivery. Empirically, the analysis focused on the initial responses during the first four years after decentralization came into effect. The rather short-term nature of the empirical investigation naturally restrains any conclusive evaluation. At the same time, the empirical findings indicate that it is possible to draw valid and meaningful inferences from initial responses that took place in the indicated timeframe allowing me to test my hypothesis. It is apparently not too early to tell. Nevertheless, these findings might be challenged in the light of future evidence. In the following the major results of this enterprise will be summarized and critically discussed.

The general hypothesis tested in this paper is that the performance of local governments is to a significant extent determined by the effectiveness of political accountability systems ensuring public control of government actions. The empirical results broadly support this hypothesis. Incentives structures embedded in both formal political institutions and informal power relationships determine how local groups interact and bring about local policy choices. Through its effects on the level and allocation of resources political accountability is likely to improve the quantity and quality of public services provided by the local government.

We constructed an indicator based on household perceptions of education, health and general public services to measure improvements in public service delivery since decentralization. We have regressed this index on a wide range of political, fiscal and

socio-economic variables. Our results are broadly consistent with the predictions of the model demonstrating that citizens in communities with sound political processes perceived services to have improved more significantly. The results indicated that less political fragmentation in local councils, less political corruption, higher participation and easier access to information are all associated with higher performance perceptions. Higher attendance rates in planning meetings correlate with higher reported improvements in public services. This effect remained statistically robust across all specifications. While we should be cautious in interpreting the results as causality in the strict sense, they still provide an interesting pattern that should be addressed in further empirical analysis.

Poorly performing local governments are often deeply rooted in their political (and social) environment. Conversely, better performing governments were consistently more open to pressure of informed, organized and politically active communities, which strengthened their incentives to be responsive and manage and deliver services more efficiently. If political institutions fail to translate community demand into public spending and policies, due to weak electoral incentives, ineffective checks and balances and intransparency, governments often fail to deliver basic services because political and bureaucratic agents face incentives to misallocate public resources to draw private 'rents'. Conversely, higher accountability will increase the political costs of inefficient and inadequate public decisions and public service performance is likely to improve. This requires the interaction of institutions, the electoral regime and a well informed and a politically active community able to broadly participate directly and indirectly in exacting accountability.

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